

**MUNICIPAL EMPLOYEES CREDIT UNION
OF BALTIMORE, INC.
Baltimore, Maryland**

**FINANCIAL STATEMENTS
December 31, 2010 and 2009**

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Independent Auditor's Report

Board of Directors and
Supervisory Committee
Municipal Employees Credit Union of Baltimore, Inc.
Baltimore, Maryland

We have audited the accompanying statement of financial condition of Municipal Employees Credit Union of Baltimore, Inc. as of December 31, 2010, and the related statements of income, comprehensive income, members' equity, and cash flows for the year then ended. These financial statements are the responsibility of the Credit Union's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Credit Union as of December 31, 2009 were audited by other auditors whose report dated March 9, 2010, expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2010 financial statements referred to above present fairly, in all material respects, the financial condition of Municipal Employees Credit Union of Baltimore, Inc. as of December 31, 2010, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Clifton Gunderson LLP

Baltimore, Maryland
February 17, 2011

FINANCIAL STATEMENTS

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
STATEMENTS OF FINANCIAL CONDITION
December 31, 2010 and 2009

	2010	2009
ASSETS		
Cash and cash equivalents	\$ 13,207,132	\$ 24,291,043
Investments		
Available-for-sale	329,639,845	244,599,769
Held-to-maturity	60,262,226	73,893,212
Other	7,079,414	26,836,457
Loans to members, net	620,827,425	615,846,429
Accrued interest receivable	3,663,243	3,284,717
Property and equipment, net	4,529,438	5,592,046
National Credit Union Share Insurance Fund deposit	8,650,631	6,520,060
Cash surrender value of life insurance	24,878,192	23,963,981
Other assets	8,134,445	7,875,666
TOTAL ASSETS	\$ 1,080,871,991	\$ 1,032,703,380
LIABILITIES AND MEMBERS' EQUITY		
LIABILITIES		
Members' share and deposit accounts	\$ 884,602,984	\$ 841,498,145
Borrowed funds	69,387,302	66,222,222
Accrued expenses and other liabilities	13,897,360	16,955,214
Total liabilities	967,887,646	924,675,581
MEMBERS' EQUITY		
Retained earnings, substantially restricted	112,467,517	106,557,879
Accumulated other comprehensive income	516,828	1,469,920
Total members' equity	112,984,345	108,027,799
TOTAL LIABILITIES AND MEMBERS' EQUITY	\$ 1,080,871,991	\$ 1,032,703,380

The accompanying notes are an integral part of the financial statements.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
STATEMENTS OF INCOME
Years Ended December 31, 2010 and 2009

	<u>2010</u>	<u>2009</u>
INTEREST INCOME		
Loans to members	\$ 42,669,877	\$ 43,270,376
Investments and cash equivalents	<u>9,393,021</u>	<u>8,583,072</u>
Total interest and investment income	<u>52,062,898</u>	<u>51,853,448</u>
INTEREST EXPENSE		
Members' shares and deposit accounts	14,160,202	17,943,345
Bonus dividends and loan interest rebates	3,500,000	5,000,000
Borrowed funds	<u>1,605,370</u>	<u>1,101,033</u>
Total interest expense	<u>19,265,572</u>	<u>24,044,378</u>
Net interest income before provision for loan losses	32,797,326	27,809,070
PROVISION FOR LOAN LOSSES	<u>6,802,057</u>	<u>6,804,761</u>
Net interest income after provision for loan losses	<u>25,995,269</u>	<u>21,004,309</u>
NON-INTEREST INCOME		
Net gain on sale of available-for-sale investments	1,742,506	954,918
Service charges and other fees	10,026,486	10,021,685
Recapitalization gain on NCUSIF deposit	-	5,288,829
Other non-interest income	<u>5,573,923</u>	<u>5,846,066</u>
Total non-interest income	<u>17,342,915</u>	<u>22,111,498</u>
NON-INTEREST EXPENSE		
Salaries and benefits	19,311,864	19,225,533
Operations expenses	7,822,142	8,734,100
Occupancy expenses	2,426,294	2,308,827
Educational and promotional expenses	1,583,457	1,686,353
Loan servicing expenses	1,977,116	1,795,438
Professional and outside services expenses	1,924,952	1,627,872
Other expenses	2,382,721	1,921,803
Impairment loss on NCUSIF deposit and members insurance premiums	<u>-</u>	<u>2,350,000</u>
Total general and administrative expenses	<u>37,428,546</u>	<u>39,649,926</u>
NET INCOME	<u>\$ 5,909,638</u>	<u>\$ 3,465,881</u>

The accompanying notes are an integral part of the financial statements.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
STATEMENTS OF COMPREHENSIVE INCOME
Years Ended December 31, 2010 and 2009

	2010	2009
NET INCOME	<u>\$ 5,909,638</u>	<u>\$ 3,465,881</u>
 OTHER COMPREHENSIVE INCOME		
Reclassification adjustment for realized gains on investments included in net income	(1,742,506)	(954,918)
Unrealized holding gains on investments classified as available-for-sale	<u>789,414</u>	<u>1,500,407</u>
Total other comprehensive income (loss)	<u>(953,092)</u>	<u>545,489</u>
 COMPREHENSIVE INCOME	 <u>\$ 4,956,546</u>	 <u>\$ 4,011,370</u>

The accompanying notes are an integral part of the financial statements.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
STATEMENTS OF MEMBERS' EQUITY
Years Ended December 31, 2010 and 2009

	<u>Retained Earnings</u>				<u>Accumulated Other Comprehensive Income (Loss)</u>
	<u>Regular Reserves</u>	<u>Other Appropriated</u>	<u>Unappropriated</u>	<u>Total</u>	
BALANCE, DECEMBER 31, 2008	\$ 33,962,275	\$ 900,000	\$ 68,229,723	\$ 103,091,998	\$ 924,431
Net income	-	-	3,465,881	3,465,881	-
Total other comprehensive income					<u>545,489</u>
BALANCE, DECEMBER 31, 2009	33,962,275	900,000	71,695,604	106,557,879	1,469,920
Net income	-	-	5,909,638	5,909,638	-
Total other comprehensive loss					<u>(953,092)</u>
BALANCE, DECEMBER 31, 2010	<u>\$ 33,962,275</u>	<u>\$ 900,000</u>	<u>\$ 77,605,242</u>	<u>\$ 112,467,517</u>	<u>\$ 516,828</u>

The accompanying notes are an integral part of the financial statements.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
STATEMENTS OF CASH FLOWS
Years Ended December 31, 2010 and 2009

	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 5,909,638	\$ 3,465,881
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of securities, net	2,383,578	1,536,210
Provision for loan losses	6,802,057	6,804,761
Depreciation and amortization	1,477,835	1,666,065
Gain on sales of investments	(1,742,506)	(954,918)
Recapitalization gain on NCUSIF deposit	-	(5,288,829)
Effects of changes in operating assets and liabilities:		
Accrued interest receivable	(378,526)	(503,109)
Other assets	(258,779)	(1,509,307)
Accrued expenses and other liabilities	(3,057,854)	3,495,894
Net cash provided by operating activities	11,135,443	8,712,648
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of available-for-sale securities	(315,942,830)	(270,005,012)
Proceeds from maturities of available-for-sale investments	133,312,853	92,884,437
Proceeds from sales of available-for-sale investments	95,961,698	73,875,727
Purchases of held-to-maturity investments	(127,650,224)	(96,206,987)
Proceeds from maturities of held-to-maturity securities	141,315,249	38,392,880
Net change in other investments	19,757,043	4,275,234
Net increase in cash surrender value of life insurance	(914,211)	(909,096)
Net change in loans to members	(11,783,053)	26,630,331
(Increase) decrease in the NCUSIF deposit	(2,130,571)	764,098
Purchases of property and equipment	(415,227)	(1,591,006)
Net cash used in investing activities	(68,489,273)	(131,889,394)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from borrowed funds	105,900,708	55,000,000
Repayment of borrowed funds	(102,735,628)	(21,533,334)
Net increase in members' shares and deposits	43,104,839	102,565,207
Net cash provided by financing activities	46,269,919	136,031,873
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(11,083,911)	12,855,127
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	24,291,043	11,435,916
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 13,207,132	\$ 24,291,043
SUPPLEMENTAL CASH FLOW INFORMATION		
Dividends and interest paid on members' shares and deposits and interest paid on borrowed funds	\$ 15,765,572	\$ 18,293,084

The accompanying notes are an integral part of these financial statements.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Municipal Employees Credit Union of Baltimore, Inc. (the Credit Union) is a state-chartered credit union organized under the provisions of the Maryland Credit Union Act. Participation in the Credit Union is limited to those individuals that qualify for membership, including those who live, regularly work, worship or attend school in Baltimore City, and those who are a relative by blood or marriage of anyone who lives, regularly works, worships or attends school in Baltimore City. The field of membership is defined in the Credit Union's Charter and Bylaws.

Significant Accounting Policies

The Credit Union follows the accounting standards set by the Financial Accounting Standards Board (FASB). The FASB establishes generally accepted accounting principles (GAAP) that are followed to ensure consistent reporting of the financial condition, results of operations and cash flows of the Credit Union. References to GAAP issued by the FASB in these footnotes are to 'The FASB Accounting Standards Codification' commonly referred to as the Codification or ASC. The FASB finalized the Codification effective for periods ended on or after September 15, 2009. As such, the Credit Union has adopted the Codification in these financial statements; the Codification does not change how the Credit Union accounts for its transactions nor does it change the nature of the associated disclosures. Prior FASB standards like FASB Statement No. 5, Accounting for Contingencies, are no longer being issued by the FASB. Because the FASB encourages the use of plain English to describe broad topical references, these financial statements will generally no longer include references to specific technical guidance. For example, citations of the accounting requirements for contingencies would include a reference similar to "as required by the Contingencies Topic of the Codification."

Use of Estimates in Preparing Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the determination of fair value of accounts evaluated for impairment and disclosure.

Subsequent Events

Management evaluated subsequent events through February 17, 2011, the date the financial statements were available to be issued. Events or transactions occurring after December 31, 2010, but prior to February 17, 2011 that provided additional evidence about conditions that existed at December 31, 2010, have been recognized in the financial statements for the year ended December 31, 2010. Events or transactions that provided evidence about conditions that did not exist at December 31, 2010, but arose before the financial statements were available to be issued, have not been recognized in the financial statements for the year ended December 31, 2010.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Concentrations of Credit Risk

Most of the Credit Union's business activity is with its members who reside in or are employed in the City of Baltimore. The Credit Union may be exposed to credit risk from a regional economic standpoint, since a significant concentration of its borrowers work or reside in Baltimore, Maryland. However, the loan portfolio is well-diversified and the Credit Union does not have any significant concentrations of credit risk except unsecured loans, which by their nature increase the risk of loss compared to those loans that are collateralized. The Credit Union's policy for repossessing collateral is that when all other collection efforts have been exhausted, the Credit Union enforces its first lien holder status and repossesses the collateral. The Credit Union has full and complete access to repossessed collateral. Repossessed collateral normally consists of vehicles and residential real estate.

In addition, the ongoing financial deterioration resulting from the general economic conditions of the Credit Union's market area have yielded significant loan losses for the Credit Union and those with whom it does business, including other financial institutions and corporate credit unions. Management continues to monitor the Credit Union's operations for potential impairment and other accounting consequences.

Cash and Cash Equivalents

For the purpose of the statements of financial position and the statements of cash flow, cash and cash equivalents includes cash on hand, amounts due from financial institutions, and highly liquid debt instruments classified as cash that were purchased with maturities of three months or less. Amounts due from financial institutions may, at times, exceed federally insured limits.

Investments

Debt securities that management has the positive intent and ability to hold to maturity are classified as "held-to-maturity" and recorded at amortized cost. Securities not classified as held-to-maturity or trading, including equity securities with readily determinable fair values, are classified as "available-for-sale" and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

The Credit Union evaluates debt and equity securities for other-than-temporary impairment (OTTI), at least quarterly. This guidance specifies that (a) if the Credit Union does not have the intent to sell a debt security prior to recovery and (b) it is more-likely-than-not that it will not have to sell the debt security prior to recovery, the security would not be considered other-than-temporarily impaired unless there is a credit loss. When the Credit Union does not intend to sell the security and it is more-likely-than-not the Credit Union will not have to sell the security before recovery of its cost basis, it will recognize the credit component of an OTTI of a debt security in earnings and the remaining portion in other comprehensive income (loss). For held-to-maturity debt securities, the amount of OTTI recorded in other comprehensive income (loss) for the noncredit portion of a previous OTTI should be amortized prospectively over the remaining life of the security on the basis of the timing of future estimated cash flows of the security.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investments (continued)

The Credit Union's statements of income reflects the full impairment (that is, the difference between the security's amortized cost basis and fair value) on debt securities that the Credit Union intends to sell or would more-likely-than-not be required to sell before the expected recovery of the amortized cost basis. The credit component recognized in earnings is identified as the amount of principal cash flows not expected to be received over the remaining term of the security as projected on cash flow projections.

Other investments are classified separately and are stated at cost. If such investments are deemed to be impaired, the recorded cost is reduced by the amount of the impairment.

Federal Home Loan Bank (FHLB) Stock

The Credit Union, as a member of the FHLB of Atlanta, is required to maintain an investment in capital stock of the FHLB in an amount equal to the sum of a percentage of mortgages as designated by the FHLB, plus 4.5 percent of advances from the FHLB. No ready market exists for the FHLB stock, and it has no quoted market value.

Loans to Members, Net

The Credit Union grants mortgage, commercial and consumer loans to members. The ability of the members to honor their contracts is dependent upon the real estate and general economic conditions of the area.

Loans that the Credit Union has the intent and ability to hold for the foreseeable future or until maturity or pay-off are stated at their outstanding unpaid principal balances, less an allowance for loan losses and net deferred origination fees and costs. Interest income on loans is recognized over the term of the loan and is calculated using the simple interest method on principal amounts outstanding.

The accrual of interest income on loans is discontinued at the time the loan is 90 days past due, unless the credit is well-secured and in the process of collection. Other personal loans are typically charged off no later than 180 days past due. Past-due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if the collection of principal and interest is considered doubtful.

All interest accrued but not collected for loans that is placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method until qualifying for return to accrual. Loans are returned to accrual status when all of the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Loan fees and certain direct loan origination costs are deferred, and the net fee or cost is recognized as an adjustment to interest income using the interest method over the contractual life of the loans, adjusted for estimated prepayments based on the Credit Union's historical prepayment experience.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is likely. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of the underlying collateral and prevailing economic conditions. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Credit Union's allowance for loan losses, and may require the Credit Union to make additions to the allowance based on their judgment about information available to them at the time of their examinations.

The Credit Union's allowance for loan losses is that amount considered adequate to absorb probable losses in the portfolio based on management's evaluations of the size and current risk characteristics of the loan portfolio. Such evaluations consider prior loss experience, the risk rating and the levels of nonperforming loans. A loan is considered impaired when, based on current information and events, it is probable that the Credit Union will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Specific allowances for loan losses are established for impaired loans on an individual basis as required. The specific allowances established for these loans are based on a thorough analysis of the most probable source of repayment, including the present value of the loan's expected future cash flow, the loan's estimated market value or the estimated fair value of the underlying collateral. General allowances are established for loans that can be grouped into pools based on similar characteristics. In this process, general allowance factors are based on an analysis of historical charge-off experience and expected losses given default derived from the Credit Union's internal risk-rating process. These factors are developed and applied to the portfolio by loan type. The qualitative factors associated with the allowances are subjective and require a high degree of management judgment. These factors include the credit quality statistics, recent economic uncertainty, losses incurred from recent events and other relevant data.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Credit Union, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Credit Union does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Loan Servicing

Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. For sales of mortgage loans, a portion of the cost of originating the loan is allocated to the servicing right based on fair value. Fair value is based on market prices for comparable mortgage servicing contracts, when available or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds, and default rates and losses. Capitalized servicing rights are reported in other assets and are amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets.

Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights into tranches based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the capitalized amount for the tranche. If the Credit Union later determines that all or a portion of the impairment no longer exists for a particular tranche, a reduction of the allowance may be recorded as an increase to income.

Servicing fee income is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal, or a fixed amount per loan, and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income.

Off-Balance Sheet Credit Related Financial Instruments

In the ordinary course of business, the Credit Union has entered into commitments to extend credit. Such financial instruments are recorded when they are funded.

Property and Equipment

Building, leasehold improvements, and furniture and equipment are carried at cost, less accumulated depreciation and amortization. Buildings and furniture and equipment are depreciated using the straight-line method over the estimated useful lives of the assets. The cost of leasehold improvements is amortized using the straight-line method over the lesser of the useful life of the assets or the expected terms of the related leases. Expected terms include lease option periods to the extent that the exercise of such options is reasonably assured. Management reviews premises and equipment for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

National Credit Union Share Insurance Fund (NCUSIF) Deposit and Insurance Premium

The deposit in the NCUSIF is in accordance with National Credit Union Administration (NCUA) regulations, which in prior years required the maintenance of a deposit by each federally insured Credit Union in an amount equal to 1 percent of its insured members' shares. The deposit would be refunded to the Credit Union if its insurance coverage was terminated, if it

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

National Credit Union Share Insurance Fund (NCUSIF) Deposit and Insurance Premium
(continued)

converted its insurance coverage to another source, or if management of the fund was transferred from the NCUA Board. In January 2009, the financial condition resulting from the ongoing economic decline caused the NCUA to announce the impairment of the deposits of natural person credit unions in the NCUSIF.

The underlying causes of the impairment and assessment are events considered to have occurred before December 31, 2008. Because the amounts became estimable with the NCUA Board actions in 2009 prior to the close of the Credit Union's fiscal year-end, the Credit Union recognized the deposit impairment loss of \$4,498,841 and recorded the additional assessment of \$1,956,018, which resulted in a total charge of \$6,454,859 in the statement of income for the fiscal year ended December 31, 2008.

In May 2009, an amendment to the Federal Credit Union Act to Congress was passed to create the Corporate Credit Union Stabilization Fund (the Fund) that enables credit unions to spread the cost over a period of years. In June 2009, the NCUA issued guidance instructing federally insured credit unions to record other non-interest income for the previously impaired amounts, as well as reducing the insurance assessment estimate to 0.15 percent of insured deposits as of June 30, 2009. As a result of this guidance, the Credit Union recorded a recapitalization gain of approximately \$5,289,000 and a net premium assessment expense of \$2,350,000 for the year ended December 31, 2009.

The Credit Union also carries private insurance to cover members' deposits in excess of \$250,000 up to \$325,000. In addition to the payment of annual premiums, the coverage requires the payment of a refundable deposit made on the estimated aggregate coverage. As of December 31, 2010 and 2009, the balance on deposit was \$80,000 and \$550,000, respectively.

Members' Shares

Members' shares are the savings deposit accounts of the owners of the Credit Union. Share ownership entitles the members to vote in the annual elections of the Board of Directors and on other corporate matters. Irrespective of the amount of shares owned, no member has more than one vote. Members' shares are subordinated to all other liabilities of the Credit Union upon liquidation. Dividends on members' shares are based on available earnings at the end of a dividend period and are not guaranteed by the Credit Union. Dividend rates are set by the Credit Union's Board of Directors.

Members' Equity

The Credit Union is required, by regulation, to maintain a statutory regular reserve. This reserve, which represents a regulatory restriction of retained earnings, is not available for the payment of interest.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Advertising Costs

Advertising costs are expensed as incurred.

Income Taxes

The Credit Union is exempt, by statute, from federal income taxes; however, the Credit Union may be subject to unrelated business income tax (UBIT). The Credit Union may be subject to UBIT for the year ended December 31, 2010 as further discussed in Note 11. There was no UBIT for the year ended December 31, 2009.

The FASB issued new guidance on accounting for uncertainty in income taxes. The Credit Union adopted this new guidance for the year ended December 31, 2009. Management evaluated the Credit Union's tax positions and concluded that the Credit Union had taken no uncertain tax positions that require adjustment to the financial statements to comply with the provisions of this guidance. The Credit Union files a form 990 in the U.S. federal jurisdiction.

Defined Benefit Plan

The Credit Union participates in a qualified, noncontributory multiple employer defined benefit pension plan covering certain employees. The Credit Union funds the plan as required by the administrator of the multiple employer plan.

Defined Contribution Plan

The Credit Union has established a contributory 401(k) plan for qualified employees. The Credit Union's policy is to fund contributions as accrued.

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the members' equity section of the statements of financial condition. For 2010 and 2009, other comprehensive income includes reclassification adjustments for realized gains on investments included in net income.

Fair Value Measurements

Fair value measurement standards provide a comprehensive framework for measuring fair value and expands disclosures for assets and liabilities reported at fair value. Specifically, it sets forth a definition of fair value and establishes a hierarchy prioritizing the inputs to valuation techniques, giving the highest priority to quoted prices in active markets for identical assets and liabilities and the lowest priority to unobservable value inputs.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Reclassifications

Certain account reclassifications have been made to the 2009 financial statements in order to conform to classifications used in the current year.

Recent Accounting Pronouncements

In June 2009, the FASB issued additional guidance in the Transfers and Servicing Topic of the Codification. The Board's objective is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance and cash flows; and a transferors continuing involvement, if any, in transferred financial assets. This guidance must be applied to transfers occurring as of the beginning of the Credit Union's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application is prohibited.

On January 21, 2010, FASB issued Accounting Standards Update (ASU) 2010-06, Fair Value Measurements and Disclosures (FASB ASC Topic 820): Improving Disclosures about Fair Value Measurements. The ASU describes amendments that require new disclosures and clarify existing disclosure requirements about fair value measurement, originally issued as FASB Statement No. 157, Fair Value Measurements. The ASU is effective for interim and annual reporting periods beginning after December 15, 2009, except for disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years.

NOTE 2 – INVESTMENTS

Investments classified as available-for-sale consist of the following:

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
December 31, 2010				
U.S. government obligations and federal agencies securities	\$110,126,064	\$ 514,250	\$ (463,767)	\$110,176,547
Mortgage-backed securities	216,013,130	2,399,998	(1,949,319)	216,463,809
Bank Note	<u>2,983,823</u>	<u>15,666</u>	<u>-</u>	<u>2,999,489</u>
Total	<u>\$329,123,017</u>	<u>\$ 2,929,914</u>	<u>\$(2,413,086)</u>	<u>\$329,639,845</u>
December 31, 2009				
U.S. government obligations and federal agencies securities	\$ 82,450,317	\$ 454,420	\$ (113,573)	\$ 82,791,164
Mortgage-backed securities	<u>160,679,532</u>	<u>2,123,300</u>	<u>(994,227)</u>	<u>161,808,605</u>
Total	<u>\$243,129,849</u>	<u>\$ 2,577,720</u>	<u>\$(1,107,800)</u>	<u>\$244,599,769</u>

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 2 – INVESTMENTS (CONTINUED)

Investments classified as held-to-maturity consist of the following:

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
December 31, 2010				
U.S. government obligations and federal agencies securities	<u>\$60,262,226</u>	<u>\$ 65,898</u>	<u>\$ (472,370)</u>	<u>\$59,855,754</u>
December 31, 2009				
U.S. government obligations and federal agencies securities	<u>\$73,893,212</u>	<u>\$ 5,403</u>	<u>\$(1,261,718)</u>	<u>\$72,636,897</u>

Gross realized gains and losses on sales of investments available-for-sale were \$1,749,231 and \$6,725 in 2010 and \$984,291 and \$29,373 in 2009, respectively.

Investments by maturity as of December 31, 2010, are summarized as follows:

	<u>Available-for-Sale</u>		<u>Held-to-Maturity</u>		<u>Other</u>
	<u>Amortized Cost</u>	<u>Fair Value</u>	<u>Amortized Cost</u>	<u>Fair Value</u>	
No contractual maturity	\$ -	\$ -	\$ -	\$ -	\$ 7,079,414
Less than 1 year maturity	16,979,452	17,033,170	2,000,000	1,998,820	-
1 – 5 years maturity	70,054,466	70,249,380	26,531,153	26,547,017	-
5 – 10 years maturity	16,930,113	16,895,517	17,740,606	17,577,158	-
Over 10 years maturity	9,145,856	8,997,968	13,990,467	13,732,759	-
Mortgage-backed securities	<u>216,013,130</u>	<u>216,463,810</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total	<u>\$ 329,123,017</u>	<u>\$ 329,639,845</u>	<u>\$ 60,262,226</u>	<u>\$ 59,855,754</u>	<u>\$ 7,079,414</u>

Expected maturities of mortgage-backed securities may differ from contractual maturities because borrowers may have the right to call or prepay the obligations and are, therefore, classified separately with no specific maturity date. FHLB stock and federal funds have been classified with no contractual maturity.

Gross unrealized losses and fair value by length of time that the individual securities have been in a continuous unrealized loss position at December 31, 2010, are as follows:

<u>December 31, 2010</u>	<u>Fair Value Associated with Unrealized Losses Existing for:</u>		<u>Continuous Unrealized Losses Existing for:</u>		<u>Total Unrealized Losses</u>
	<u>Less than 12 Months</u>	<u>More than 12 Months</u>	<u>Less than 12 Months</u>	<u>More than 12 Months</u>	
Available-for-Sale					
U.S. government obligations and federal agencies securities	\$ 45,561,866	\$ -	\$ (463,767)	\$ -	\$ (463,767)
Mortgage-backed securities	<u>80,814,352</u>	<u>-</u>	<u>(1,949,319)</u>	<u>-</u>	<u>(1,949,319)</u>
Total	<u>\$ 126,376,218</u>	<u>\$ -</u>	<u>\$ (2,413,086)</u>	<u>\$ -</u>	<u>\$ (2,413,086)</u>

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
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NOTE 2 – INVESTMENTS (CONTINUED)

<u>December 31, 2010</u>	<u>Fair Value Associated with Unrealized Losses Existing for:</u>		<u>Continuous Unrealized Losses Existing for:</u>		<u>Total Unrealized Losses</u>
	<u>Less than 12 Months</u>	<u>More than 12 Months</u>	<u>Less than 12 Months</u>	<u>More than 12 Months</u>	
Held-to-Maturity					
U.S. government obligations and federal agencies securities	<u>\$37,259,878</u>	<u>\$ -</u>	<u>\$(472,370)</u>	<u>\$ -</u>	<u>\$(472,370)</u>

Based upon an evaluation of the available evidence, including recent changes in market rates, credit rating information and information obtained from regulatory filings, management believes the decline in fair value for these securities is temporary. In addition, the Credit Union does not intend to sell and will not be required to sell these investment securities prior to recovery of the amortized cost basis.

Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income in the period in which the other-than-temporary impairment is identified.

Other investments consist of the following:

	<u>2010</u>	<u>2009</u>
Federal funds sold	\$ 1,864,514	\$ 22,231,357
FHLB of Atlanta stock	<u>5,214,900</u>	<u>4,605,100</u>
Total	<u>\$ 7,079,414</u>	<u>\$ 26,836,457</u>

The Credit Union views its investment in the FHLB of Atlanta stock as a long-term investment. Accordingly, when evaluating for impairment, the value is determined based on the ultimate recovery of the par value rather than recognizing temporary declines in value. The determination of whether a decline affects the ultimate recovery is influenced by criteria, such as the following: 1) the significance of the decline in net assets of the FHLB of Atlanta as compared to the capital stock amount and length of time a decline has persisted, 2) impact of legislative and regulatory changes on the FHLB of Atlanta, and 3) the liquidity position of the FHLB of Atlanta.

The Credit Union does not believe that its investment in the FHLB of Atlanta stock is impaired as of this date. However, this estimate could change in the near term by the following: (1) significant other-than-temporarily losses are incurred on the FHLB of Atlanta's mortgage-backed securities causing a significant decline in its regulatory capital status, (2) the economic losses resulting from credit deterioration on the FHLB of Atlanta's mortgage-backed securities increases significantly, and (3) capital preservation strategies being utilized by the FHLB of Atlanta become ineffective.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
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NOTE 3 – LOANS TO MEMBERS

Loans to members consist of the following:

	<u>2010</u>	<u>2009</u>
Mortgage loans:		
Fixed rate – first mortgage	\$260,370,345	\$243,760,225
Variable rate – first mortgage	33,684,924	35,685,258
Member business loans	6,004,929	5,999,196
Fixed rate – home equity	34,012,469	41,241,739
Variable rate – home equity line of credit	<u>53,472,942</u>	<u>48,828,717</u>
	387,545,609	375,515,135
New vehicle loans	39,922,273	46,982,315
Used vehicle loans	87,713,149	92,109,510
Credit card loans, unsecured	24,574,973	22,294,875
Member business loans	3,035,848	1,813,416
Other consumer loans, primarily unsecured	<u>87,543,546</u>	<u>85,511,399</u>
	630,335,398	624,226,650
Deferred net loan origination costs	100,836	538,225
Allowance for loan losses	<u>(9,608,809)</u>	<u>(8,918,446)</u>
Total	<u>\$620,827,425</u>	<u>\$615,846,429</u>

The following is an analysis of the allowance for loan losses:

	<u>Years Ended December 31,</u>	
	<u>2010</u>	<u>2009</u>
Balance, beginning of year	\$ 8,918,446	\$ 7,819,428
Provision for loan losses	6,802,057	6,804,761
Recoveries	858,216	613,914
Loans charged off	<u>(6,969,910)</u>	<u>(6,319,657)</u>
Balance, end of year	<u>\$ 9,608,809</u>	<u>\$ 8,918,446</u>

The effect of nonaccrual loans was not significant to the results of operations in either year.

NOTE 4 – LOAN SERVICING

Mortgage loans serviced for others are not included in the accompanying statements of financial condition. The unpaid principal balances of these loans are summarized as follows:

	<u>2010</u>	<u>2009</u>
Mortgage loan portfolio serviced for FNMA	<u>\$ 65,995,271</u>	<u>\$ 85,987,824</u>

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 4 – LOAN SERVICING (CONTINUED)

The balance of capitalized servicing rights, net of valuation allowances, is included in other assets in the accompanying Statements of Financial Condition, and totaled \$466,799 and \$614,089 at December 31, 2010 and 2009, respectively.

NOTE 5 – PROPERTY AND EQUIPMENT

Property and equipment are summarized as follows:

	2010	2009
Building	\$ 314,800	\$ 259,693
Leasehold improvements	4,935,233	5,057,456
Furniture and equipment	11,021,389	10,620,464
	16,271,422	15,937,613
Accumulated depreciation and amortization	(11,741,984)	(10,345,567)
Total	\$ 4,529,438	\$ 5,592,046

Depreciation and amortization expense amounted to \$1,484,253 and \$1,666,065 for the years ended December 31, 2010 and 2009, respectively.

The Credit Union leases six offices. The operating leases contain renewal options and provisions requiring the Credit Union to pay property taxes and operating expenses over base period amounts. All rental payments are dependent only upon the lapse of time. Minimum rental payments under operating leases with initial or remaining terms of one year or more at December 31, 2010, are as follows:

Years Ending December 31,

2011	\$ 1,461,000
2012	1,455,000
2013	1,449,000
2014	1,486,000
2015	1,521,000
Subsequent years	1,263,000
Total	\$ 8,635,000

Rental expense for the years ended December 31, 2010 and 2009, for all facilities leased under operating leases totaled \$1,554,257 and \$1,474,894, respectively.

NOTE 6 – LIFE INSURANCE

The Credit Union is the owner and beneficiary of life insurance contracts. These underlying investments had not incurred a loss in value as of the year ended December 31, 2010. These policies were purchased with the intent that future cash surrender value (CSV) increases would serve as a benchmark in determining amounts due to executive management under deferred compensation arrangements.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
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NOTE 7 – MEMBERS’ SHARES AND DEPOSIT ACCOUNTS

Members’ shares and deposits are summarized as follows:

	<u>2010</u>	<u>2009</u>
Shares	\$303,417,271	\$296,608,987
Checking	62,374,311	59,197,183
Money market accounts	155,375,389	130,899,662
Individual retirement accounts	23,414,367	23,185,685
Other savings	2,694,849	2,755,428
Certificates of deposit (including IRA)	<u>337,326,797</u>	<u>328,851,200</u>
Total	<u>\$884,602,984</u>	<u>\$841,498,145</u>

Shares by maturity as of December 31, 2010, are summarized as follows:

No contractual maturity	\$547,276,187
0 – 1 year maturity	179,342,307
1 – 2 years maturity	61,988,115
2 – 3 years maturity	32,748,272
3 – 4 years maturity	32,039,773
4 – 5 years maturity	<u>31,208,330</u>
Total	<u>\$884,602,984</u>

Regular shares, checking accounts, money market accounts, individual retirement accounts (IRA) and other savings have no contractual maturity. IRA and savings certificate accounts have maturities of five years or less.

The NCUSIF insures members' shares and deposits up to \$250,000. IRAs are also insured up to \$250,000, separately from other types of deposit accounts owned.

The Credit Union also provides an additional \$75,000 of insurance through Excess Share Insurance (ESI), a private corporation, on accounts that exceed the NCUA insured amounts (currently \$250,000, up to \$325,000), and that meet certain requirements specified in the insurance contract.

The aggregate amount of certificates in denominations of \$100,000 or more at December 31, 2010 and 2009, is approximately \$89,652,000 and \$83,278,000, respectively.

At December 31, 2010 and 2009, overdraft demand shares reclassified to loans totaled \$537,751 and \$636,986, respectively.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 8 – BONUS DIVIDEND AND LOAN INTEREST REBATE

Bonus dividends and loan rebates in excess of contractual terms totaled \$3,500,000 and \$5,000,000 in 2010 and 2009, respectively.

NOTE 9 – OFF-BALANCE SHEET ACTIVITIES

The Credit Union is party to conditional commitments to lend funds in the normal course of business to meet the financing needs of its members. These commitments represent financial instruments to extend credit that include lines of credit, credit cards and home equity lines that involve, to varying degrees, elements of credit and interest rate risk in excess of amounts recognized in the financial statements.

The Credit Union's exposure to credit loss is represented by the contractual amount of these commitments. The Credit Union follows the same credit policies in making commitments as it does for those loans recorded in the financial statements.

Commitments to extend credit are agreements to lend to a member as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Because many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Credit Union evaluates each member's creditworthiness on a case-by-case basis. The amount of collateral obtained to secure borrowing on the lines of credit is based on management's credit evaluation of the member.

Unfunded commitments under commercial lines of credit, revolving credit lines and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines of credit are uncollateralized and usually do not contain a specified maturity date and ultimately may not be drawn upon to the total extent to which the Credit Union is committed.

Outstanding mortgage loan commitments at December 31, 2010 and 2009, total approximately \$3,651,000 and \$4,068,000, respectively.

Unfunded loan commitments under lines of credit are summarized as follows:

	<u>2010</u>	<u>2009</u>
Home equity	\$ 45,448,308	\$ 42,751,000
Credit card	43,569,000	42,646,000
Overdraft lines of credit	14,575,743	15,366,000
Other consumer	<u>39,691,943</u>	<u>39,280,000</u>
Total	<u>\$143,284,994</u>	<u>\$140,043,000</u>

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 10 – BORROWED FUNDS

The Credit Union utilizes a demand loan agreement with the FHLB of Atlanta. The advances are collateralized by FHLB stock and pledged mortgage collateral, which includes residential first mortgages, home equity lines of credit, second mortgages and commercial mortgage loan collateral, under an "Advances and Security Agreement" between the FHLB and the Credit Union. Based on the collateral held, the agreement provides for a maximum borrowing amount of approximately \$207,034,995 as of December 31, 2010. As of December 31, 2010 and 2009, the borrowings outstanding represented \$63,087,302 and \$66,322,408, respectively, with interest payable of \$107,352 and \$100,186, respectively. The advances have interest rates ranging from 1.17 percent to 4.90 percent. As of December 31, 2010, the outstanding balances by maturity dates are as follows:

	Balance
Less than 1 year maturity	\$ 6,111,111
1 – 2 years maturity	11,666,667
2 – 3 years maturity	7,666,667
3 – 4 years maturity	8,000,000
4 – 5 years maturity	-
Over 5 years maturity	29,642,857
Total	\$ 63,087,302

The Credit Union also has available a line of credit with a bank. The terms of the agreement provide for borrowings up to \$30,000,000. The first \$10,000,000 is unsecured. The remaining \$20,000,000 is secured by the Credit Union's investment portfolio. At December 31, 2010 and 2009, the borrowings outstanding were \$6,300,000 and \$0. The borrowings had an interest rate of 0.52% and a maturity date of January 03, 2011.

NOTE 11 – COMMITMENTS AND CONTINGENT LIABILITIES

The Credit Union is a party to various legal actions normally associated with collections of loans and other business activities of financial institutions, the aggregate effect of which, in management's opinion, would not have a material adverse effect on the financial condition or results of operations of the Credit Union.

The Credit Union is a state-chartered credit union described in Internal Revenue Code (IRC) Section 501(c) (14). As such, the Credit Union is exempt from federal taxation of income derived from the performance of activities that are in the furtherance of its exempt purposes. However, IRC Section 511 imposes a tax on the unrelated business income (as defined in Section 512) derived by state-chartered credit unions. Many states have similar laws. The specific application of Section 512 to the various activities conducted by state-chartered credit unions has been at issue for many years.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 12 – EMPLOYEE BENEFITS

The Credit Union transferred all of the defined benefit pension plan assets to a multiple employer plan in 2008. As a part of a multiple employer plan, the Credit Union is not required to record a prepaid or accrued pension amount and expenses plan contributions as they are made. The total defined benefit pension plan expense for the years ended December 31, 2010 and 2009, was approximately \$1,712,000 and \$1,915,000, respectively.

The Credit Union has a 401(k) pension plan that allows employees to defer a portion of their salary into the 401(k) plan. The Credit Union matches a portion of employees' wage reductions. Pension costs are accrued and funded on a current basis. The Credit Union contributed approximately \$263,000 and \$227,000, respectively, to the plan for the years ended December 31, 2010 and 2009.

The Credit Union entered into deferred compensation agreements with members of the Executive Management Team that provides benefits payable to these employees if they remain employed by the Credit Union until age 65. The benefits are subject to forfeiture if employment is terminated for cause as defined in the agreement. The estimated liability under the agreements is being accrued on a straight-line basis over the remaining years until the eligible employees attain age 65. The Credit Union has accrued approximately \$2,194,000 and \$1,476,000, respectively, under this agreement for the years ended December 31, 2010 and 2009.

The Credit Union entered into deferred compensation agreements with members of the Board of Directors that provides benefits payable to these directors when they retire from the Board. The estimated liability under the agreements is being accrued on a straight-line basis. The Credit Union has accrued approximately \$151,000 and \$138,000, respectively, under this agreement for the years ended December 31, 2010 and 2009.

NOTE 13 – MEMBERS' EQUITY

The Credit Union is subject to various regulatory capital requirements administered by the NCUA and the state of Maryland. Failure to meet minimum capital requirements can initiate certain mandatory—and possibly additional discretionary—actions by regulators that, if undertaken, could have a direct material effect on the Credit Union's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Credit Union must meet specific capital guidelines that involve quantitative measures of the Credit Union's assets, liabilities and certain off-balance-sheet items as calculated under generally accepted accounting principles. The Credit Union's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 13 – MEMBERS’ EQUITY (CONTINUED)

Quantitative measures established by regulation to ensure capital adequacy require the Credit Union to maintain minimum amounts and ratios (set forth in the table below) of net worth to total assets. Further, credit unions over \$10,000,000 in assets are also required to calculate a Risk-Based Net Worth (RBNW) requirement, which establishes whether or not the Credit Union will be considered "complex" under the regulatory framework. The Credit Union's RBNW requirements as of December 31, 2010 and 2009, were 6.13 percent and 6.27 percent, respectively. The minimum requirement to be considered "complex" under the regulatory framework is 6.00 percent. Management believes, as of December 31, 2010 and 2009, that the Credit Union meets all capital adequacy requirements to which it is subject.

Other appropriated retained earnings represent a restriction of retained earnings as established by the Board of Directors.

As of December 31, 2010, the most recent call reporting period, and 2009, the NCUA categorized the Credit Union as "well-capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well-capitalized," the Credit Union must maintain a minimum net worth ratio of 7.00 percent of assets. There are no conditions or events since that notification that management believes have changed the institution's category.

The Credit Union is required to maintain a statutory reserve. This reserve, which represents a regulatory restriction of retained earnings, is not available for the payment of dividends.

The Credit Union's actual capital amounts and ratios are presented in the following table:

	December 31, 2010		December 31, 2009	
	Amount	Ratio/ Requirement	Amount	Ratio/ Requirement
Amount needed to be classified as "adequately capitalized"	\$ 66,257,000	6.13%	\$ 64,750,000	6.27%
Amount needed to be classified as "well-capitalized"	75,661,000	7.00%	72,289,000	7.00%
Actual net worth	112,467,517	10.41%	106,558,000	10.32%

Because the RBNW requirement is less than the net worth ratio, the Credit Union retains its original category. Further, in performing its calculation of total assets, the Credit Union used the quarter-end balance option, as permitted by regulation.

NOTE 14 – RELATED-PARTY TRANSACTIONS

In the normal course of business, the Credit Union extends credit to directors, supervisory and credit committee members, and executive officers. The aggregate loans to related parties at December 31, 2010 and 2009, are approximately \$4,438,000 and \$5,047,000, respectively. Loans to related parties are made under the same terms available to other members. Shares from related parties at December 31, 2010 and 2009, amounted to approximately \$2,138,000 and \$1,855,000, respectively.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 15 – FAIR VALUE OF FINANCIAL INSTRUMENTS

Determination of Fair Value

The Credit Union uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Credit Union's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

Fair value measurements are to focus on an exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions.

Fair Value Hierarchy

The Credit Union groups its financial assets and financial liabilities generally measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

- Level 1* Valuation is based on quoted prices in active markets for identical assets or liabilities that the Credit union has the ability to access at the measurement date. Level 1 assets and liabilities generally include debt and equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.
- Level 2* Valuation is based on inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.
- Level 3* Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which determination of fair value requires significant management judgments or estimation.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2010 and 2009

NOTE 15 – FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Fair Value Hierarchy (continued)

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value estimation.

The following methods and assumptions were used by the Credit Union in estimating fair value disclosures for financial instruments:

Available-for-Sale Investments: Fair values for investments are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments, or on discounted cash flow models based on the expected payment characteristics of the underlying mortgage instruments.

The table below presents the balances of assets measured and presented in the statements of financial condition at fair value on a recurring basis:

	Total	(Level 1)	(Level 2)	(Level 3)
Available-for-sale securities	<u>\$ 329,640,000</u>	<u>\$ -</u>	<u>\$ 329,640,000</u>	<u>\$ -</u>

The following methods and assumptions were used by the Credit Union in estimating fair values of financial instruments as disclosed herein:

Cash and Cash Equivalents: The carrying amounts of cash and cash equivalents approximate their fair value.

Available-for-Sale and Held-to-Maturity Investments: Fair values for investments are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments or on discounted cash flow models based on the expected payment characteristics of the underlying mortgage instruments.

Other Investments: The carrying value approximates fair value based on the redemption provisions of the underlying investments.

Loans to Members: For variable-rate loans that reprice frequently and have no significant change in credit risk, fair values are based on carrying values. Fair values for certain mortgage loans (for example, one-to-four family residential), credit card loans and other consumer loans are estimated using a discounted cash flow calculation that applies interest rates currently being offered similar loans to a schedule of aggregated expected monthly maturities of these loans. Fair values for business real estate and business loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values for impaired loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

MUNICIPAL EMPLOYEES CREDIT UNION OF BALTIMORE, INC.
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NOTE 15 – FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Accrued Interest: Accrued interest receivable represents interest on loans and investments. The carrying amount of accrued interest receivable approximates fair value.

Members' Shares: The fair values disclosed for share draft and money market accounts are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). The carrying amounts of variable-rate, fixed-term share certificates approximate their fair values at the reporting date. Fair values for fixed-rate shares and share certificates are estimated using a discounted cash flow calculation that applies interest rates currently being offered on shares and certificates to a schedule of aggregated expected monthly maturities on shares and certificates.

Borrowed Funds: The fair values of the Credit Union's borrowed funds are estimated using discounted cash flow analyses based on the Credit Union's incremental borrowing rates for similar types of borrowing arrangements.

Off-Balance Sheet Credit-Related Instruments: Fair values for off-balance sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value for such financial instruments is nominal.

The estimated fair value of the Credit Union's financial instruments is summarized as follows:

	December 31, 2010		December 31, 2009	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets:				
Cash and cash equivalents	\$ 13,207,000	\$ 13,207,000	\$ 24,291,000	\$ 24,291,000
Investments available-for-sale	329,640,000	329,640,000	244,600,000	244,600,000
Investments held-to-maturity	60,262,000	59,856,000	73,893,000	72,637,000
Other investments	7,079,000	7,079,000	26,836,000	26,836,000
Loans to members, net	620,827,000	602,975,000	615,846,000	603,841,000
Accrued interest receivable	3,663,000	3,663,000	3,285,000	3,285,000
Financial liabilities:				
Members' shares and deposits	884,603,000	831,991,000	841,498,000	808,583,000
Borrowed funds	69,387,000	69,749,000	66,222,000	66,222,000
Accrued interest payable	4,367,000	4,367,000	5,115,000	5,115,000

This information is an integral part of the accompanying financial statements.