

**FIRST  
COMMONWEALTH  
MORTGAGE  
TRUST**

**2017 ANNUAL REPORT**

## **TO OUR SHAREHOLDERS:**

The financial statements of First Commonwealth Mortgage Trust (“FCMT”) for the years ending December 31, 2017 and December 31, 2016, audited by Melton & Melton, L.L.P. are set forth at the end of this report.

FCMT’s total revenues in 2017 were \$499,730, down from \$509,865 the previous year. The FCMT 2017 net income was \$219,162, compared to 2016 net income of \$271,341. Net income per share for 2017 was \$0.16 compared to 2016 net income of \$0.19 per share. FCMT’s reduced income for 2017 can be attributed in part to certain non-recurring expenses related to implementation of the common stock redemption plan.

### **Corporate Overview**

First Commonwealth Mortgage Trust (“FCMT” or the “Trust”) was originally organized as a Massachusetts business trust in 1984 and reformed in Texas as a real estate investment trust in 2008. The Trust was formed for the purpose of originating and purchasing real estate loans, trust deeds, mortgages or real estate lien promissory notes associated with real properties (“Mortgage Loans”).

The Trust’s primary investment objective is to maximize cash distributions to its shareholders based on funds available for distribution, which includes funds provided from operations and, from time to time, gains realized on the sale of investments.

The Trust was organized and has qualified since inception as a real estate investment trust (“REIT”) in accordance with federal tax laws and regulations. So long as the Trust complies with such laws and regulations, with limited exceptions, the Trust will not be taxed under federal income tax laws on that portion of its taxable income that it distributes to its shareholders. The Trust intends to distribute substantially all of its real estate investment trust taxable income to its shareholders.

The business and affairs of the Trust are managed under the direction of its Trust Managers who are elected by the shareholders of FCMT.

The book value per share of FCMT Stock was \$6.35 at December 31, 2017. The original shares were issued at \$10.00 per share. Since 1985, dividends of \$20.93 per share have been distributed to the shareholders. Of these total dividends, a portion amounting to \$1.30 per share, were treated as non-taxable return of capital to the shareholders.

FCMT is essentially an unleveraged company. For example, on December 31, 2017 our liabilities were \$134,223.

FCMT has been impacted by low interest rates, in that yields on mortgage loans have decreased along with interest rates.

### **Stock Purchase Program**

The Trust Managers believe that in order to allow liquidity for shareholders, it is in the best interests of the shareholders, for the Trust to periodically offer to purchase shares. Therefore, at the 2017 annual meeting of shareholders, shareholders approved the adoption of a stock purchase program funded from available cash or sales of portfolio securities.

Under the program, at the Trust Managers discretion, the Trust may make offers to purchase Trust shares, not more than semi-annually upon certain conditions and limitations. The Trust Managers anticipate making such offer, within a reasonable time after the Trust's December 31, 2017 audited financial statements have been completed. Offers to purchase shares will be made at 90% of net book value less any dividends declared and payable to the selling shareholder.

Should the participating shareholders tender shares in excess of the amount the Trust has agreed to purchase, the Trust will purchase the shares tendered on a pro rata basis, except that the Trust may accept all shares tendered by shareholders owning own fewer than 1,000 shares.

Trust Managers anticipate making offers to purchase approximately 5% of the outstanding shares of the Trust semi-annually. During 2017, 70,403 shares were purchased under the plan at a cost of \$395,665.

FCMT maintains a website [www.fcmt.net](http://www.fcmt.net) that contains additional information about the Trust. Shareholder reports are posted on the website along with a history of dividend payments.

Shareholders may also contact the transfer agent below to change their mailing address, change share registration, obtain copies of IRS Form 1099, and arrange the direct deposit of dividends to their bank account:

Equiniti Trust Company  
1110 Centre Pointe Curve, Suite 101  
Mendota Heights, MN 55120-4100

Phone: 800-468-9716 Fax: 651-450-4033

The 2018 Shareholder meeting is scheduled for May 8, 2018. Please vote your proxy.



Robert A. Scharar  
President



Robert A. Burns  
Treasurer

March 31, 2018

## SELECTED FINANCIAL DATA 5-YEAR SUMMARY

| YEAR ENDED DECEMBER 31      | 2017       | 2016       | 2015         | 2014      | 2013         |
|-----------------------------|------------|------------|--------------|-----------|--------------|
| REVENUES:                   |            |            |              |           |              |
| INTEREST AND DIVIDENDS      | \$458,651  | \$464,133  | \$361,866    | \$369,648 | \$418,303    |
| SERVICE FEES & OTHER INCOME | 41,079     | 45,732     | 1,498,383    | 85,512    | 52,141       |
|                             | 499,730    | 509,865    | 1,860,249    | 455,160   | 470,444      |
| COST AND EXPENSES           | 280,568    | 238,524    | 595,942      | 360,875   | 1,391,441    |
| NET INCOME                  | \$ 219,162 | \$ 271,341 | \$ 1,264,307 | \$ 94,285 | \$ (920,997) |

### PER SHARE DATA

|            |         |         |         |         |           |
|------------|---------|---------|---------|---------|-----------|
| NET INCOME | \$ 0.16 | \$ 0.19 | \$ 0.86 | \$ 0.06 | \$ (0.62) |
| DIVIDENDS  | \$ 0.12 | \$ 0.11 | \$ 0.05 | \$ 0.04 | \$ 0.06   |

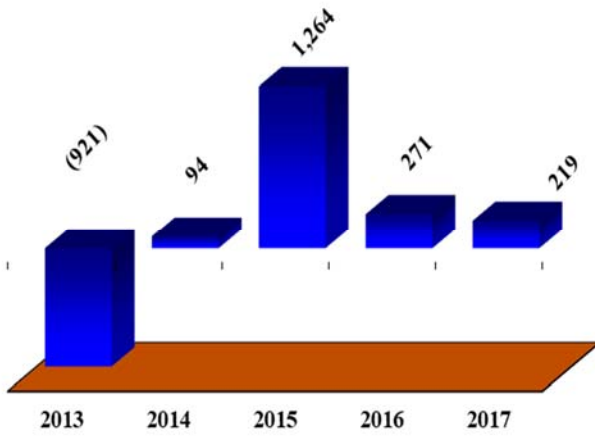
### YEAR END DATA

|                      |              |              |              |               |               |
|----------------------|--------------|--------------|--------------|---------------|---------------|
| TOTAL ASSETS         | \$ 8,631,218 | \$ 8,944,842 | \$ 8,793,609 | \$ 10,612,712 | \$ 10,844,283 |
| SHAREHOLDERS' EQUITY | \$ 8,496,995 | \$ 8,892,364 | 8,737,889    | 8,011,126     | 7,976,465     |
| SHARES OUTSTANDING   | \$ 1,337,768 | \$ 1,408,171 | 1,408,171    | 1,490,571     | 1,490,571     |
| BOOK VALUE PER SHARE | \$ 6.35      | \$ 6.31      | \$ 6.21      | \$ 5.37       | \$ 5.35       |

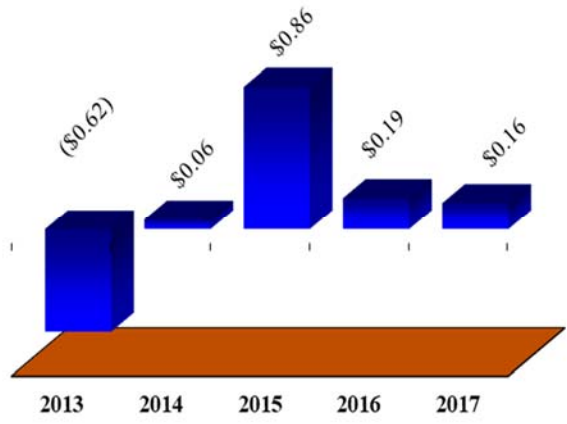
### OTHER DATA

|                                    |           |           |           |           |           |
|------------------------------------|-----------|-----------|-----------|-----------|-----------|
| LOANS ORIGINATED (000,000's)       | \$ 0.816  | \$ 0.550  | \$ 1.175  | \$ 0.420  | \$ 0.210  |
| CUMULATIVE TOTAL LOANS (000,000's) | \$ 97.739 | \$ 96.923 | \$ 96.373 | \$ 95.198 | \$ 94.778 |
| TOTAL ASSETS (000's)               | \$ 8,631  | \$ 8,945  | \$ 8,794  | \$ 10,613 | \$ 10,844 |
| EARNINGS YIELD ON BOOK VALUE       | 2.52%     | 3.01%     | 13.86%    | 1.12%     | -11.59%   |

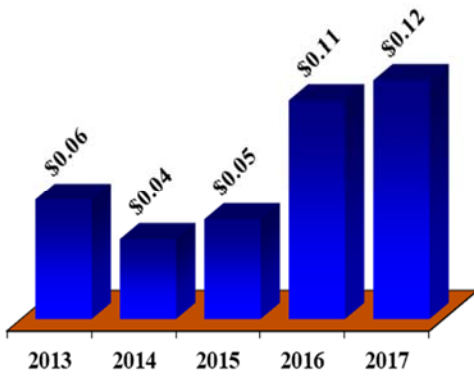
**Net Income (000's)**



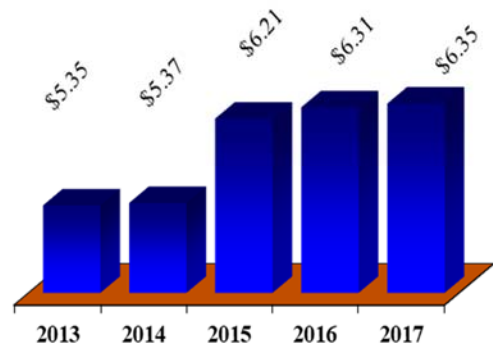
**Net Income per Share**



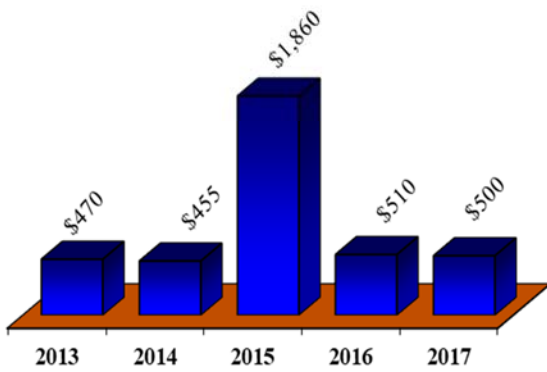
**Dividends Per Share**



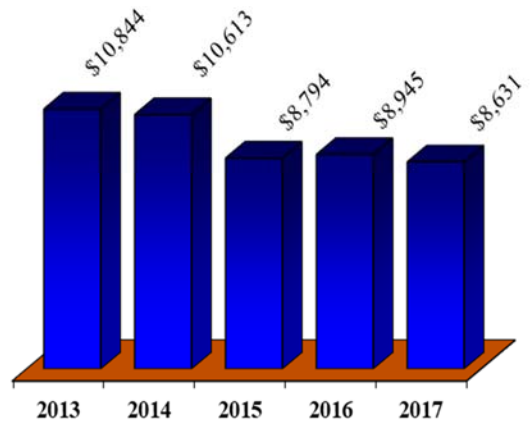
**Book Value Per Share**



**Revenues (000's)**



**Total Assets (000's)**



FIRST COMMONWEALTH MORTGAGE TRUST

FINANCIAL STATEMENTS  
FOR THE  
YEARS ENDED DECEMBER 31, 2017 AND 2016  
AND  
INDEPENDENT AUDITOR'S REPORT

**FIRST COMMONWEALTH MORTGAGE TRUST**

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**MELTON & MELTON, L.L.P.**  
CERTIFIED PUBLIC ACCOUNTANTS

## **INDEPENDENT AUDITOR'S REPORT**

To the Board of Trust Managers of  
**First Commonwealth Mortgage Trust**

We have audited the accompanying financial statements of First Commonwealth Mortgage Trust, which comprise the balance sheets as of December 31, 2017 and 2016, and the related statements of operations, comprehensive income, changes in equity, and cash flows for the years then ended, and the related notes to the financial statements.

### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of First Commonwealth Mortgage Trust as of December 31, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Melton & Melton, L.L.P.*

Houston, Texas  
March 2, 2018

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**BALANCE SHEETS**  
**December 31, 2017 and 2016**

|  | <u>2017</u>                | <u>2016</u>                | <u>2017</u>                | <u>2016</u>                |
|--|----------------------------|----------------------------|----------------------------|----------------------------|
| <b><u>ASSETS</u></b>   |                            |                            |                            |                            |
| <b>Mortgage Notes Receivable:</b>  |                            |                            |                            |                            |
| Mortgage notes receivable  | \$ 5,722,337               | \$ 5,771,368               | \$ 134,223                 | \$ 52,478                  |
| Cash and cash equivalents  | 673,485                    | 867,633                    | <u>134,223</u>             | <u>52,478</u>              |
| Restricted cash and cash equivalents   | 14,309                     | 16,509                     |                            |                            |
| Certificate of deposit - restricted  | 412,898                    | 325,000                    |                            |                            |
| Marketable securities  | 1,201,141                  | 1,112,976                  |                            |                            |
| Accrued interest receivable  | 331,690                    | 540,177                    |                            |                            |
| Other receivables  | 90,070                     | 102,530                    |                            |                            |
| Prepaid expenses   | -                          | 23,361                     |                            |                            |
| Land   | 161,454                    | 161,454                    |                            |                            |
| Investment in affiliate  | 23,834                     | 23,834                     |                            |                            |
|  | <b><u>\$ 8,631,218</u></b> | <b><u>\$ 8,944,842</u></b> | <b><u>\$ 8,631,218</u></b> | <b><u>\$ 8,944,842</u></b> |
| <b><u>LIABILITIES AND EQUITY</u></b>   |                            |                            |                            |                            |
| <b>Liabilities:</b>  |                            |                            |                            |                            |
| Accounts payable and other liabilities   |                            |                            |                            |                            |
| Total liabilities  |                            |                            |                            |                            |
| <b>Equity:</b>   |                            |                            |                            |                            |
| Shares of beneficial interest, no par value,<br>20,000,000 shares authorized, 1,420,168 and 1,490,571<br>shares issued and 1,337,768 and 1,408,171 outstanding<br>in 2017 and 2016, respectively |                            |                            | 14,328,158                 | 14,723,823                 |
| Accumulated deficit  |                            |                            | (5,349,599)                | (5,404,005)                |
| Accumulated other comprehensive income (loss)  |                            |                            | (38,252)                   | 15,858                     |
| Treasury shares, 82,400 shares of beneficial interest, at cost   |                            |                            | (443,312)                  | (443,312)                  |
| Total equity   |                            |                            | <u>8,496,995</u>           | <u>8,892,364</u>           |
|  |                            |                            | <b><u>\$ 8,631,218</u></b> | <b><u>\$ 8,944,842</u></b> |

(See Notes to Financial Statements)

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**STATEMENTS OF OPERATIONS**  
**For the Years Ended December 31, 2017 and 2016**

|   | <u>2017</u>       | <u>2016</u>       |
|---|-------------------|-------------------|
| <b>Revenue:</b>                                       |                   |                   |
| Interest income                                       | \$ 339,836        | \$ 375,947        |
| Dividends and interest income - marketable securities | 118,815           | 88,186            |
| Gain on sale of marketable securities                 | 36,489            | 30,773            |
| Miscellaneous income                                  | 4,590             | 14,959            |
|   | <u>499,730</u>    | <u>509,865</u>    |
| <b>Costs and Expenses:</b>                            |                   |                   |
| Management fees to affiliates                         | 95,560            | 93,443            |
| Professional fees                                     | 80,845            | 38,089            |
| General and administrative                            | 104,163           | 106,992           |
|   | <u>280,568</u>    | <u>238,524</u>    |
| Net income  | <u>\$ 219,162</u> | <u>\$ 271,341</u> |
| Weighted average shares outstanding                   | <u>1,372,487</u>  | <u>1,408,171</u>  |
| Net income per share, basic and diluted               | <u>\$ 0.16</u>    | <u>\$ 0.19</u>    |

(See Notes to Financial Statements)

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**STATEMENTS OF COMPREHENSIVE INCOME**  
**For the Years Ended December 31, 2017 and 2016**

|   | <b><u>2017</u></b>       | <b><u>2016</u></b>       |
|---|--------------------------|--------------------------|
| <b>Net Income</b>   | \$ 219,162               | \$ 271,341               |
| <b>Other Comprehensive Income (Loss):</b>                             |                          |                          |
| Unrealized gains (losses) on marketable securities                    | (17,621)                 | 68,806                   |
| Reclassification of realized gain on sale of<br>marketable securities | <u>(36,489)</u>          | <u>(30,773)</u>          |
| <b>Net Comprehensive Income</b>                                       | <b><u>\$ 165,052</u></b> | <b><u>\$ 309,374</u></b> |

(See Notes to Financial Statements)

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**STATEMENTS OF CHANGES IN EQUITY**  
**For the Years Ended December 31, 2017 and 2016**

|   | <u>Shares of</u>           |                             |                              | <u>Accumulated</u>                 |                                    |                            | <u>Other</u>           |                     |  |
|---|----------------------------|-----------------------------|------------------------------|------------------------------------|------------------------------------|----------------------------|------------------------|---------------------|--|
|   | <u>Beneficial Interest</u> | <u>Amount</u>               |                              | <u>Deficit</u>                     | <u>Comprehensive Income (Loss)</u> |                            | <u>Treasury Shares</u> | <u>Total Equity</u> |  |
|   | <u>Shares Outstanding</u>  | <u>Amount</u>               | <u>Accumulated Deficit</u>   | <u>Comprehensive Income (Loss)</u> | <u>Treasury Shares</u>             | <u>Total Equity</u>        |                        |                     |  |
| <b>Balance, December 31, 2015</b>         | 1,408,171                  | \$ 14,723,823               | \$ (5,520,447)               | \$ (22,175)                        | \$ (443,312)                       | \$ 8,737,889               |                        |                     |  |
| Dividends                                 | -                          | -                           | (154,899)                    | -                                  | -                                  | (154,899)                  |                        |                     |  |
| Net income                                | -                          | -                           | 271,341                      | -                                  | -                                  | 271,341                    |                        |                     |  |
| Other comprehensive income                | -                          | -                           | -                            | 38,033                             | -                                  | 38,033                     |                        |                     |  |
| <b>Balance, December 31, 2016</b>         | 1,408,171                  | 14,723,823                  | (5,404,005)                  | 15,858                             | (443,312)                          | 8,892,364                  |                        |                     |  |
| Purchase of shares of beneficial interest | (70,403)                   | (395,665)                   | -                            | -                                  | -                                  | (395,665)                  |                        |                     |  |
| Dividends                                 | -                          | -                           | (164,756)                    | -                                  | -                                  | (164,756)                  |                        |                     |  |
| Net income                                | -                          | -                           | 219,162                      | -                                  | -                                  | 219,162                    |                        |                     |  |
| Other comprehensive loss                  | -                          | -                           | -                            | (54,110)                           | -                                  | (54,110)                   |                        |                     |  |
| <b>Balance, December 31, 2017</b>         | <b><u>1,337,768</u></b>    | <b><u>\$ 14,328,158</u></b> | <b><u>\$ (5,349,599)</u></b> | <b><u>\$ (38,252)</u></b>          | <b><u>\$ (443,312)</u></b>         | <b><u>\$ 8,496,995</u></b> |                        |                     |  |

(See Notes to Financial Statements)

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**STATEMENTS OF CASH FLOWS**  
**For the Years Ended December 31, 2017 and 2016**

|   | <u>2017</u>              | <u>2016</u>              |
|---|--------------------------|--------------------------|
| <b>Cash Flows from Operating Activities:</b>                                      |                          |                          |
| Net income  | \$ 219,162               | \$ 271,341               |
| Adjustments to reconcile net income to net cash provided by operating activities: |                          |                          |
| Gain on sale of marketable securities   | (36,489)                 | (30,773)                 |
| Changes in operating assets and liabilities:                                      |                          |                          |
| Accrued interest receivable   | (63,879)                 | (98,070)                 |
| Other receivables   | (1,040)                  | (4,730)                  |
| Prepaid expenses  | 23,361                   | (23,361)                 |
| Accounts payable and other liabilities  | (3,953)                  | 1,531                    |
| Total adjustments   | <u>(82,000)</u>          | <u>(155,403)</u>         |
| Net cash provided by operating activities   | <u>137,162</u>           | <u>115,938</u>           |
| <b>Cash Flows from Investing Activities:</b>                                      |                          |                          |
| Mortgage note originations  | (714,802)                | (564,077)                |
| Principal collected on mortgage notes receivable                                  | 1,137,597                | 547,724                  |
| Purchase of certificate of deposit - restricted                                   | (87,898)                 | (325,000)                |
| Purchase of marketable securities   | (728,359)                | (511,039)                |
| Proceeds from sale of marketable securities                                       | <u>622,573</u>           | <u>219,225</u>           |
| Net cash provided by (used in) investing activities                               | <u>229,111</u>           | <u>(633,167)</u>         |
| <b>Cash Flows from Financing Activities:</b>                                      |                          |                          |
| Dividends - shareholders  | (164,756)                | (154,899)                |
| Purchase of shares of beneficial interest   | <u>(395,665)</u>         | <u>-</u>                 |
| Net cash used in financing activities   | <u>(560,421)</u>         | <u>(154,899)</u>         |
| Net decrease in cash and cash equivalents   | (194,148)                | (672,128)                |
| <b>Cash and Cash Equivalents, beginning of year</b>                               | <u>867,633</u>           | <u>1,539,761</u>         |
| <b>Cash and Cash Equivalents, end of year</b>                                     | <u><b>\$ 673,485</b></u> | <u><b>\$ 867,633</b></u> |
| <b>Noncash Investing and Financing Activities:</b>                                |                          |                          |
| Restricted cash offset with accounts payable and other liabilities                | <u><b>\$ 14,309</b></u>  | <u><b>\$ 16,509</b></u>  |
| Accrued interest rolled into mortgage notes receivable                            | <u><b>\$ 272,366</b></u> |                          |

(See Notes to Financial Statements)

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2017 and 2016**

**NOTE 1 - ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Organization**

First Commonwealth Mortgage Trust (“Trust”) was organized on September 26, 1984 and commenced operations on June 27, 1985. The Trust is a Texas real estate investment trust with a termination date of December 31, 2030. The Trust is engaged primarily in the business of investing in loans collateralized by mortgages on real estate. These loans are principally collateralized in Texas, Florida, and Arizona.

**Cash and Cash Equivalents**

The Trust considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

**Restricted Cash and Cash Equivalents**

The Trust collects escrow deposits for property taxes and insurance related to property listed as collateral for certain mortgage notes. The balance of restricted cash and cash equivalents and deposits collected and included in accounts payable and other liabilities at December 31, 2017 and 2016 is \$14,309 and \$16,509, respectively.

**Mortgage Notes Receivable and Allowance for Losses**

Mortgage notes receivable are carried at unpaid principal balances less allowance for losses. Management intends to hold mortgage notes receivable to maturity. Mortgage notes are principally collateralized by first mortgage loans on commercial or residential property and are due at various dates. Mortgage notes bear interest at rates ranging from 2% to 9%.

The allowance for losses is based on management’s estimate of the amount required to maintain an allowance adequate to reflect the risks inherent in the mortgage note portfolio after giving consideration to existing economic conditions, loss experience in relation to outstanding mortgage notes, changes in the mortgage note portfolio, borrowers’ performance in reducing mortgage note principal, adequacy of mortgage note collateral, and other relevant factors. A mortgage note is charged off against the allowance for losses when management determines the mortgage note is uncollectible. A mortgage note is placed on nonaccrual status when it becomes past due, as determined by management. Upon suspension of the accrual of interest, interest previously recognized but uncollected is reversed and charged against current income. Subsequent interest collected on the mortgage note is credited to principal if, in the opinion of management, collectibility of principal is doubtful; otherwise, the interest collected is recognized as revenue. Accrual of interest is resumed when a mortgage note is removed from nonaccrual status. Interest income is accrued based upon the principal amount outstanding. Commitment and origination fees are deferred and recognized as income using a method approximating the interest method over the life of the loan.



**FIRST COMMONWEALTH MORTGAGE TRUST**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2017 and 2016**

**NOTE 1 - ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

A mortgage note is considered impaired when it is probable that the scheduled principal or interest will not be collected. Impaired mortgage notes include mortgage notes that have been placed on nonaccrual status and are valued upon the present value of expected future cash flows discounted at the mortgage note's effective interest rate or collateral fair value, if the mortgage note is collateral dependent. If the measure of the impaired mortgage note is less than the recorded investment in the mortgage note, an impairment loss is included in the allowance for losses.

At December 31, 2017 and 2016, there were no impaired mortgage notes and no allowance for losses on mortgage notes receivable and accrued interest receivable and no commitments to lend additional funds to borrowers.

At December 31, 2017 and 2016, five mortgage notes receivable customers represented approximately 70% and 68%, respectively, of total mortgage notes receivable. Interest related to four mortgage notes receivable was approximately 64% of interest income for 2017 and 2016.

**Marketable Securities**

In accordance with the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 320, *Investment – Debt and Equity Securities*, investments in marketable securities with readily determinable fair values are classified as held-to-maturity, trading, or available-for-sale. The Trust classifies marketable securities as available-for-sale and reports the securities at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction. See Note 3 for discussion of fair value measurements. The Trust has no marketable securities classified as held-to-maturity or trading.

Purchases and sales of marketable securities are recorded on a trade-date basis. Interest income is recorded as earned on the accrual basis. Dividends are recorded on the ex-dividend date. The realized gain or loss on marketable securities is based on specific identification and reported in operations. The unrealized gain or loss on marketable securities is reported in accumulated other comprehensive income (loss) on the balance sheets.

**Land**

Land received in foreclosure proceedings is recorded at fair value on date of receipt. Purchased land is recorded at cost. Gains or losses resulting from disposals of land are credited or charged to operations currently.

Management reviews the carrying value of land for impairment whenever events or changes in circumstances indicate the carrying amount may not be recoverable. When required, impairment losses on land to be held and used or disposed of other than by sale are recognized based on the current fair value of the land. Land to be disposed of by sale is reported at the lower of its carrying amount or fair value less cost to sell. Management has determined that there is no impairment of land at December 31, 2017 or 2016.



**FIRST COMMONWEALTH MORTGAGE TRUST**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2017 and 2016**

**NOTE 1 - ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Net Income per Share**

Net income per share is calculated by dividing net income by the weighted average number of shares of beneficial interest outstanding during the year. The Trust has no items that give rise to anti-dilutive shares. Accordingly, basic and dilutive shares presented are the same.

**Comprehensive Income**

Comprehensive income is the total of (1) net income plus (2) all other changes in net assets arising from nonowner sources, which are referred to as items of other comprehensive income. The Trust has presented separate statements of comprehensive income. An analysis of changes in components of accumulated other comprehensive income (loss) is presented in the statements of changes in equity.

**Management Estimates**

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 at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Management believes that these estimates and assumptions provide a reasonable basis for the fair presentation of the financial statements.

**Recent Accounting Pronouncements**

In May 2014, the FASB issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers* (Topic 606). ASU 2014-09 supersedes the revenue recognition requirements in Topic 605, *Revenue Recognition*, and most industry-specific guidance throughout the Industry Topics of the Codification. Additionally, this update supersedes some cost guidance included in Subtopic 605-35, *Revenue Recognition—Construction-Type and Production-Type Contracts*. In addition, the existing requirements for the recognition of a gain or loss on the transfer of nonfinancial assets that are not in a contract with a customer (for example, assets within the scope of Topic 360, *Property, Plant, and Equipment*, and intangible assets within the scope of Topic 350, *Intangibles—Goodwill and Other*) are amended to be consistent with the guidance on recognition and measurement (including the constraint on revenue) in ASU 2014-09. ASU 2014-09, as further amended by ASU 2015-14, is effective for annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Management is currently evaluating the impact ASU 2014-09 will have on the Trust's financial statements.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments - Overall (Subtopic 825-10) - Recognition and Measurement of Financial Assets and Financial Liabilities*. ASU 2016-01 makes the following changes to existing accounting principles generally accepted in the United States of America for entities that are not public business entities:

- Requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income.

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2017 and 2016**

**NOTE 1 - ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

- Simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to determine impairment.
- Eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost.
- Requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments.
- Requires separate presentation of financial assets and financial liabilities by measurement category and form of financial assets (that is, securities or loans and receivables) on the balance sheets or the accompanying notes to the financial statements.
- Clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets.

ASU 2016-01 is effective for annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Management is currently evaluating the impact ASU 2016-01 will have on the Trust's financial statements.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows: Restricted Cash* (Topic 230). ASU 2016-18 applies to all entities that have restricted cash or restricted cash equivalents and are required to present a statement of cash flows under Topic 230. The amendments require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. ASU 2016-18 is effective for annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019, with early adoption permitted. Management is currently evaluating the impact ASU 2016-18 will have on the Trust's financial statements.

**NOTE 2 - MARKETABLE SECURITIES**

At December 31, 2017 and 2016, marketable securities consist of the following:

|   | 2017               |                                       |  |                       |
|---|--------------------|---------------------------------------|--|-----------------------|
|   | <u>Cost</u>        | <u>Gross<br/>Unrealized<br/>Gains</u> | <u>Gross<br/>Unrealized<br/>Losses</u> | <u>Fair<br/>Value</u> |
| Real estate investment trusts<br>("REIT") | \$1,112,787        | \$ 9,423                              | \$53,519                               | \$1,068,691           |
| Preferred stock - REIT                    | <u>126,606</u>     | <u>5,844</u>                          | <u>-</u>                               | <u>132,450</u>        |
|   | <u>\$1,239,393</u> | <u>\$15,267</u>                       | <u>\$53,519</u>                        | <u>\$1,201,141</u>    |

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2017 and 2016**

**NOTE 2 - MARKETABLE SECURITIES (CONTINUED)**

|   | 2016                                  |  |                       |                    |
|---|---------------------------------------|--|-----------------------|--------------------|
| <u>Cost</u>                               | <u>Gross<br/>Unrealized<br/>Gains</u> | <u>Gross<br/>Unrealized<br/>Losses</u> | <u>Fair<br/>Value</u> |                    |
| Real estate investment trusts<br>("REIT") | \$ 845,720                            | \$18,006                               | \$ -                  | \$ 863,726         |
| Preferred stock - REIT                    | <u>251,398</u>                        | <u>-</u>                               | <u>2,148</u>          | <u>249,250</u>     |
|   | <u>\$1,097,118</u>                    | <u>\$18,006</u>                        | <u>\$2,148</u>        | <u>\$1,112,976</u> |

Investment income is included in dividends and interest income - marketable securities on the statements of operations and consists of interest and dividends. The Trust had sales of marketable securities of \$622,573 and \$219,225 resulting in realized gains of \$36,489 and \$30,773 in 2017 and 2016, respectively.

**NOTE 3 - FAIR VALUE MEASUREMENTS**

FASB ASC 820, *Fair Value Measurements and Disclosures*, clarifies the definition of fair value for financial reporting, establishes a framework for measuring fair value, and requires additional disclosure about the use of fair value measurements in an effort to make the measurement of fair value more consistent and comparable.

Various inputs are used in determining fair value. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. In addition, FASB ASC 820 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. The three levels of the fair value hierarchy, including the types of marketable securities that fall under each category and the valuation methodologies used to measure fair value, are described below:

*Level 1* - Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.

*Real estate investment trusts and preferred stock:* Valued at the closing market price on a national exchange.

*Level 2* - Inputs to the valuation methodology are other than quoted market prices in active markets that are observable, either directly or indirectly, such as quoted prices for similar assets; quoted prices that are in inactive markets; inputs other than quoted prices that are observable for the assets; and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

*Level 3* - Inputs to the valuation methodology are unobservable inputs (i.e., projections, estimates, interpretations, etc.) that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2017 and 2016**

**NOTE 3 - FAIR VALUE MEASUREMENTS (CONTINUED)**

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Trust believes its valuation methods are appropriate, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date. The inputs and methodologies used for valuing investments in marketable securities are not an indication of the risk associated with those investments.

The following tables set forth by level, within the fair value hierarchy, the Trust's investments in marketable securities at fair value on a recurring basis at December 31, 2017 and 2016:

| <u>Description</u>                     | <u>2017</u>        |                |                | <u>Total</u>       |
|--|--------------------|----------------|----------------|--------------------|
|  | <u>Level 1</u>     | <u>Level 2</u> | <u>Level 3</u> |                    |
| Real estate investment trusts ("REIT") | \$1,068,691        |                |                | \$1,068,691        |
| Preferred stock - REIT                 | <u>132,450</u>     |                |                | <u>132,450</u>     |
| Total marketable securities            | <u>\$1,201,141</u> |                |                | <u>\$1,201,141</u> |

| <u>Description</u>                     | <u>2016</u>        |                |                | <u>Total</u>       |
|--|--------------------|----------------|----------------|--------------------|
|  | <u>Level 1</u>     | <u>Level 2</u> | <u>Level 3</u> |                    |
| Real estate investment trusts ("REIT") | \$ 863,726         |                |                | \$ 863,726         |
| Preferred stock - REIT                 | <u>249,250</u>     |                |                | <u>249,250</u>     |
| Total marketable securities            | <u>\$1,112,976</u> |                |                | <u>\$1,112,976</u> |

**NOTE 4 - INVESTMENT IN AFFILIATE**

The Trust participates with Holly Mortgage Trust ("Holly"), a Texas real estate investment trust, for the purpose of investing in second mortgages and equity participation mortgages. At December 31, 2017 and 2016, the Trust also owned 58,131 shares of beneficial interest in Holly, which comprised approximately 3.6% of the outstanding shares in Holly at December 31, 2017 and 2016. The investment in Holly is recorded using the cost method.

At December 31, 2017 and 2016, the investment was not evaluated for impairment because (a) the Trust did not estimate the fair value of this investment in accordance with FASB ASC 825, *Financial Instruments*, and (b) the Trust did not identify any events or changes in circumstances that may have had a significant adverse effect on the fair value of the investment.

**FIRST COMMONWEALTH MORTGAGE TRUST**  
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**December 31, 2017 and 2016**

**NOTE 5 - FEDERAL INCOME TAXES**

The Trust operates in such a manner as to qualify as a “real estate investment trust” under Sections 856 through 860 of the Internal Revenue Code of 1986, as amended, and the Treasury Regulations promulgated thereunder. Under those sections, the Trust will not be taxed on that portion of its qualifying income distributed to shareholders so long as at least 90% of the Trust’s otherwise taxable income is distributed to shareholders each year and other requirements of a qualified real estate investment trust are met. The Trust satisfied the income distribution requirements for the years ending December 31, 2017 and 2016. Management believes that all other requirements of a qualified real estate investment trust have been met.

The tax status of per-share dividend distributions declared attributable to the years presented is as follows:

|                   | <u>2017</u> | <u>2016</u> |
|-------------------|-------------|-------------|
| Ordinary income   | 100%        | 0%          |
| Return of capital | <u>0</u>    | <u>100</u>  |
|                   | <u>100%</u> | <u>100%</u> |

As of December 31, 2017, the Trust has a federal net operating loss carryforward of approximately \$2.5 million that can be deducted against future taxable income. The carryforward amount expires in 2032-2035. The Trust does not expect to pay federal income taxes, thus the tax effect of the net operating loss carryforward has been adjusted to zero by a valuation allowance of \$529,376 and \$672,732 at December 31, 2017 and 2016, respectively. The valuation allowance increased (decreased) approximately \$(143,000) and \$549,000 in 2017 and 2016, respectively. Included in the decrease of the valuation allowance in 2017 is the effect of change in effective tax rates of approximately \$328,000.

Management has evaluated the Trust’s tax positions and concluded that the Trust has taken no uncertain tax positions that require adjustment to the financial statements. Tax-related interest and penalties are recorded in income tax expense in the statements of operations. The Trust incurred no tax-related interest or penalties in 2017 or 2016. The Trust is subject to income tax examinations by federal and state tax authorities for years beginning in 2014 and after.

**NOTE 6 - MANAGEMENT AGREEMENT AND RELATED-PARTY TRANSACTIONS**

FCA Corp (“FCA”) is the Trust’s compensated manager and is related to the Trust through common management. Management fees from the Trust to FCA were approximately \$96,000 and \$93,000 for 2017 and 2016, respectively. Prepaid management fees to FCA were approximately \$23,000 at December 31, 2016. There were no prepaid management fees at December 31, 2017. The management fee for the Trust is based on 1.4% of the book value of its assets at the end of each prior fiscal year less accounting and certain board member fees.

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2017 and 2016**

**NOTE 6 - MANAGEMENT AGREEMENT AND RELATED-PARTY TRANSACTIONS  
(CONTINUED)**

In 2016, the Trust's mortgage notes receivable from Holly were collected in full. Interest income on the notes amounted to \$2,242 for 2016.

At December 31, 2017 and 2016, accounts receivable - affiliates, which are included in other receivables in the balance sheets, consist of:

|  | <u>2017</u>    | <u>2016</u>     |
|--|----------------|-----------------|
| Global REIT, L.P. (affiliated through common management) | \$ -           | \$20,000        |
| Holly  | <u>3,250</u>   | <u>-</u>        |
|  | <u>\$3,250</u> | <u>\$20,000</u> |

As a result of change in management of Global REIT, L.P. in 2017, there is no longer an affiliation through common management.

**NOTE 7 - CONCENTRATION RISKS**

The Trust maintains cash balances in a bank, which at times exceed federally insured limits. The Trust monitors the financial condition of the bank and has experienced no losses associated with this account.

Marketable securities are exposed to various risks such as significant world events, interest rate, credit, and overall market volatility risks. Due to the level of risk associated with certain securities, it is reasonably possible that changes in the fair value of marketable securities will occur in the near term and that such changes could materially affect the amounts reported in the balance sheets.

**NOTE 8 - GUARANTEE OF HOLLY LONG-TERM DEBT**

In October 2016, Holly entered into a \$325,000 loan agreement with First National Bank of Chickasha (the "Bank") in which the Trust guaranteed the loan. Upon becoming the guarantor, the Trust invested in a \$325,000 certificate of deposit with the Bank as collateral for the loan. The guarantee expires upon final payment on the loan in October 2018. In the event Holly defaults on the loan, the Trust will be obligated to surrender the certificate of deposit to pay the unpaid principal balance of the loan, plus any interest, charges, and fees, as well as be liable for any expenses incurred in enforcing rights under the guarantee agreement. Including accrued interest, the maximum potential amount of future (undiscounted) payments under the guarantee is approximately \$325,000, plus reasonable associated legal fees, at December 31, 2017 and 2016. In 2017 and 2016, the Trust recognized in both years \$3,250 as a loan guarantee fee, which is included in miscellaneous income in the statements of operations.

**FIRST COMMONWEALTH MORTGAGE TRUST**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2017 and 2016**

**NOTE 9 - LETTER OF CREDIT**

In 2017, the Trust entered into an \$87,898 letter of credit for a customer that expires in November 2018. As a condition for the letter of credit the Trust purchased a certificate of deposit for \$87,898 with the financial institution that issued the letter of credit. The certificate of deposit matures in December 2018 and is restricted for use against the letter of credit if drawn upon.

**NOTE 10 - STOCK REPURCHASE PROGRAM**

In 2017, the Trust approved a Stock Repurchase Program (“Stock Program”) to provide a level of liquidity to its shareholders as a result of no secondary market existing for the Trust’s shares. Pursuant to the Stock Program, the Trust issued a Notice of Voluntary Stock Repurchase Offer (“Repurchase Offer”) to its shareholders in 2017. In the Repurchase Offer, the Trust offered to repurchase Trust shares at \$5.62 per share, representing 90% of the Trust’s December 31, 2016 net book value per share less its \$0.06 dividend paid to shareholders in May 2017. The Repurchase Offer was limited to 5% of the currently outstanding Trust shares. In 2017, 70,403 shares of beneficial interest were purchased for \$395,665 and retired. Subsequently, the Trust may make offers to purchase additional Trust shares, not more than semi-annually and within a reasonable time period after June 30 and December 31, at a price per share determined by the Trust managers.

**NOTE 11 - BOOK VALUE PER SHARE**

Book value per share at December 31, 2017 and 2016 amounted to \$6.35 and \$6.31, respectively.

**NOTE 12 - SUBSEQUENT EVENTS**

The Trust has evaluated subsequent events through March 2, 2018, the date the financial statements were available to be issued.



# FIRST COMMONWEALTH MORTGAGE TRUST

## BOARD OF TRUST MANAGERS

**George Beatty, Jr.**

*Retired Environmental Consultant*

Mr. Beatty also serves as a trust manager of Holly Mortgage Trust and is a manager of Africap, LLC.

**William C. Brooks**

*Financial Consultant*

Mr. Brooks also serves as a trust manager of Holly Mortgage Trust and Ivy Realty Trust.

**Josef C. Hermans**

*Hotel Consultant*

*President, Terrace Hotel Corporation*

Mr. Hermans also serves as a trust manager and or a director of Holly Mortgage Trust, Ivy Realty Trust and Terrace Hotel Corp.

**William N. Walterman**

*Retired Banker*

Mr. Walterman currently is serving his first term as Trust Manager.

**Robert W. Scharar**

*President of First Commonwealth Mortgage Trust, Chairman of the Board of Trust Managers*

Mr. Scharar also serves as a trust manager of Holly Mortgage Trust, Ivy Realty Trust and holds positions with other entities, including but not limited to, Commonwealth International Series Trust, Africap, LLC, and FCA Corp.

## EXECUTIVE OFFICERS

**Robert W. Scharar**

*President*

**Robert A. Burns**

*Treasurer*

**William B. LeVay**

*Secretary*

All officers are employees of FCA Corp and serve as officers of other entities.

## TRANSFER AGENT

Equiniti Trust Company

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