WELLS FINANCIAL CORP.
2016 ANNUAL REPORT

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Wells Financial Corp. and Subsidiary

Profile

Wells Financial Corp. (the "Company") is a Minnesota corporation organized in December 1994 at the direction of the Board of Directors of Wells Federal Bank, fsb, now known as Wells Federal Bank, (the "Bank") to acquire all of the capital stock that the Bank issued upon its conversion from mutual to stock form of ownership. The Company is a unitary commercial bank holding company which, under existing laws, generally is not restricted in the types of business activities in which it may engage. At the present time, because the Company does not conduct any active business, the Company does not employ any persons but utilizes the officers and staff of the Bank.

During 2012 the Bank converted from a federally chartered savings bank to a Minnesota state chartered commercial bank. The Bank is headquartered in Wells, Minnesota. The Bank has nine full service offices located in Faribault, Martin, Blue Earth, Nicollet, Freeborn, Watonwan and Steele Counties, Minnesota. The Bank was founded in 1934 and its deposits have been federally insured since 1934 by the Savings Association Insurance Fund ("SAIF") and its predecessor, the Federal Savings and Loan Insurance Corporation ("FSLIC"), and at present, by the Federal Deposit Insurance Corp. (FDIC). The Bank is a member of the Federal Home Loan Bank ("FHLB") System. The Bank is a community oriented, full-service retail commercial bank. The Bank attracts deposits from the general public and uses such deposits to invest in residential lending on owner occupied properties, commercial real estate and construction loans, agricultural real estate and operating loans, home equity and other consumer loans. Cash in excess of amounts needed for lending operations is used to purchase investment securities and to maintain required liquidity. The Bank has one subsidiary, Wells Insurance Agency (WIA). WIA is a full service insurance agency that sells property, casualty, life and health insurance.

On March 17, 2017 the Company announced a merger with Citizens Community Bancorp, Inc. (NASDAQ: CZWI), whereby the Company will merge into Citizens Community Bancorp, Inc. in a transaction valued at approximately $39.8 million. The board of directors of both companies approved the transaction, which is subject to the approvals of bank regulatory agencies and the shareholders of the Company. Shareholders of the Company will receive total consideration of $51.00 per share, which will consist of $41.31 in cash or 81% of the total consideration and the balance of the consideration will consist of 0.7636 shares of Citizens Community Bancorp, Inc. for each share of the Company. The stock consideration is subject to a pricing collar adjustment in certain circumstances based on the price of Citizens Community Bancorp, Inc. common stock at the time of closing. It is believed that the transaction will close sometime in the third quarter of 2017.

Wells Financial Corp. and Subsidiary
SELECTED CONSOLIDATED FINANCIAL AND OTHER DATA

(dollars in thousands, except per share amounts)

Financial Condition December 31,	2016	2015	2014	2013	2012
Total assets	$ 268,475	$ 274,779	$ 251,826	$ 243,801	$ 244,195
Loans held for sale	1,338	1,337	1,707	1,952	6,911
Loans receivable, net	197,086	197,595	182,050	165,401	157,901
Securities available for sale	33,632	34,450	34,177	41,569	23,068
Certificates of deposit	13,582	9,543	4,181	3,695	9,631
Cash and cash equivalents (1)	11,677	21,159	16,373	17,625	34,000
Deposits	233,010	239,950	221,972	214,370	214,928
Borrowed funds	-	-	-	-	150
Stockholders' equity	32,075	31,300	26,619	26,083	26,157

Summary of Operations Years Ended December 31,	2016	2015	2014	2013	2012
Interest income	$ 9,879	$ 9,548	$ 8,818	$ 8,475	$ 9,390
Interest expense	355	450	597	798	1,238
Net interest income	9,524	9,098	8,221	7,677	8,152
Provision for loan losses	40	70	520	640	840
Noninterest income	3,928	6,796	3,569	4,151	5,287
Noninterest expense	9,704	9,686	9,344	9,216	9,950
Net income	2,387	4,894	1,303	1,186	1,592

Other Selected Data As of and for Years Ended December 31,	2016	2015	2014	2013	2012
Return on average assets	0.88%	1.87%	0.52%	0.48%	0.66%
Return on average equity	7.53%	17.02%	4.93%	4.52%	6.23%
Stockholders' equity to assets	11.95%	11.39%	10.57%	10.70%	10.71%
Net interest rate spread (2)	3.70%	3.68%	3.53%	3.33%	3.70%
Nonperforming assets to total loans (3)	1.73%	1.85%	2.54%	3.37%	4.76%
Allowance for loan losses to total loans	0.96%	1.01%	1.17%	1.03%	1.09%
Allowance for loan losses to nonperforming assets (3)	55.78%	53.8%	46.3%	30.6%	22.8%
Basic earnings per share	$ 3.04	$ 6.35	$ 1.72	$ 1.54	$ 2.03
Diluted earnings per share	$ 3.04	$ 6.35	$ 1.72	$ 1.54	$ 2.03
Cash dividends declared per share	$ 1.00	$ 0.72	$ 0.60	$ 0.60	$ 0.25

(1) Includes Federal Funds Sold.
(2) Interest rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.
(3) Nonperforming loans are loans over 90 days past due. Nonperforming assets include nonperforming loans and foreclosed real estate.

To Our Stockholders and Customers:

I am pleased to present the annual report for Wells Financial Corp. On March 17, 2017, the Company announced a merger with Citizens Community Bancorp (Citizens) in which Citizens will be the surviving entity. In the merger, each share of common stock of Wells Financial will be exchanged for 0.7636 shares of Citizens common stock, subject to adjustment, and a cash payment of $41.31 per share. At closing, the merged entity is projected to have $940 million in assets with $725 million in loans and $750 million in deposits with twenty-five locations.

Citizens is the bank holding company for Citizens Community Federal N.A., a full-service national bank based in Altoona, Wisconsin. Citizens stock trades on the NASDAQ Global Market under the symbol “CZWI”.

The board of directors of both companies approved the transaction, which is subject to customary conditions, including the approvals of bank regulatory agencies and the shareholders of Wells Financial Corp.

Additional good news is the Company’s improved performance during 2016. When comparing core earnings for 2016 with core earnings for 2015, net income increased by $341,000, or 16.7%. As detailed in last year’s annual report, net income for 2015 included the realization of a one-time bargain purchase gain of $2,848,000 that resulted from the acquisition of Saint James Federal Savings and Loan Association. The increase in core earnings resulted, primarily, from an increase in net interest income. Diluted earnings per share on core earnings increased by $0.39, or 14.7%, from $2.65 in 2015 to $3.04 in 2016. Using core earnings, the return on average assets increased from 0.78% in 2015 to 0.88% for 2016 and the return on average equity increased from 7.12% to 7.53%.

Asset quality continues to improve as nonperforming assets to total loans decreased from 1.9% at December 31, 2015 to 1.3% at December 31, 2016. The improvement in asset quality resulted in the provision for loan losses decreasing from $70,000 in 2015 to $40,000 in 2016.

Thank you for your investment in, and support of, Wells Financial Corp. I feel the merger with Citizens is great news for the shareholders and customers of the Company and hope that you share my feelings.

Sincerely,

James D. Moll
President and Chief Executive Officer

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
(dollars in thousands)

General

The Company's business activities to date have been limited to its investment in and loan to the Bank and a loan made to the Company's Employee Stock Ownership Plan ("ESOP") to enable the ESOP to purchase shares of the Company's common stock. As a result of the limited operations of the Company, this discussion primarily relates to the Bank. The principal business of the Bank consists of attracting deposits from the general public and using such deposits, together with borrowings to invest in loans and investment securities.

The Company's primary source of income is the Bank's net income. The Bank's net interest income is determined by (i) the difference between yields earned on interest-earning assets and rates paid on interest-bearing liabilities (interest rate spread) and (ii) the relative amounts of interest-earning assets and interest-bearing liabilities. The Bank's interest rate spread is affected by regulatory, economic, and competitive factors that influence interest rates, loan demand, and deposit flows. In order to maintain interest rate spread and reduce interest rate risk, management has elected to diversify the Bank's loan portfolio by emphasizing its investment in agriculture and commercial mortgages, commercial operating and term loans and consumer loans.

The Bank's secondary sources of income are, primarily, the gain on sale of loans originated for sale and loan servicing fees. The volume of loans generated for sale remained relatively consistent in 2016 when compared to 2015.

The operations of the Bank and the entire banking industry are significantly affected by prevailing economic conditions, competition, and the monetary and fiscal policies of the federal government and governmental agencies. The demand for and supply of housing, competition among lenders, the level of interest rates, and the availability of funds influence lending activities. Deposit flows and costs of funds are influenced by prevailing market rates of interest, primarily on competing investments, account maturities, and the levels of personal income and savings in the Bank's market area.

Effective July 16, 2015, the Company completed its previously reported acquisition of St. James Federal Savings and Loan Association, St. James, Minnesota (St. James), in a conversion merger transaction. As a result of the conversion merger transaction, St. James converted from a mutual to stock institution and merged with and into the Bank, with the Bank as the surviving institution. The Company acquired 100% of the voting shares of St. James. The Company issued and sold 78,736 shares of common stock at a price of $27.36 per share, which reflected a 5% discount on the 30 day average price as prescribed in the merger agreement. The shares were offered to depositor and borrower members of St. James in a subscription offering and to stockholders of the Company and members of the general public in a community offering. The Company's ESOP acquired 8%, or 6,299 shares, of the newly issued shares using funds borrowed from the Company. The fair value of consideration paid to the prior depositors and borrowers of St. James was determined to approximate zero. Gross offering proceeds totaled approximately $2,154 including $172 purchased by the Company's ESOP. As a result of the stock offering, the Company had 814,758 shares of common stock outstanding as of the close of business on July 16, 2015. St. James' sole office, located in St. James, Minnesota, has become a branch office of the Bank. The Company's primary reasons for the acquisition are to provide for asset growth, improve capital and competitive positions, and increase the limit on loans to one borrower.

On March 17, 2017 the Company announced a merger with Citizens Community Bancorp, Inc. (NASDAQ: CZWI), whereby the Company will merge into Citizens Community Bancorp, Inc. in a transaction valued at approximately $39.8 million. The board of directors of both companies approved the transaction, which is subject to the approvals of bank regulatory agencies and the shareholders of the Company. Shareholders of the Company will receive total consideration of $51.00 per share, which will consist of $41.31 in cash or 81% of the total consideration and the balance of the consideration will consist of 0.7636 shares of Citizens Community Bancorp, Inc. for each share of the Company. The stock consideration is subject to a pricing collar adjustment in certain circumstances based on the price of Citizens Community Bancorp, Inc. common stock at the time of closing. It is believed that the transaction will close sometime in the third quarter of 2017.

The Company may from time to time make written or oral “forward-looking statements” including statements contained in this report and in other communications by the Company which are made in good faith pursuant to the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements, such as statements of the Company’s plans, objectives, estimates and intentions, involve risks and uncertainties and are subject to change based on various important factors (some of which are beyond the Company’s control). The following factors, among others, could cause the Company’s financial performance to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements: the strength of the United States economy in general and the strength of the local economies in which the Company conducts operations; the effects of, and changes in, trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System, inflation, interest rate, market and monetary fluctuations; the timely development of and acceptance of new products and services of the Company and the perceived overall value of the products and services by users, including the features, pricing and quality compared to competitor’s products and services; the willingness of users to substitute competitors’ products and services for the Company’s products and services; the success of the Company in gaining regulatory approval of its products and services, when required; the impact of changes in financial services’ laws and regulations (including laws concerning taxes, banking, securities and insurance); technological changes; acquisitions; changes in consumer spending and savings habits; and the success of the Company at managing the risks involved in the foregoing.

The Company cautions that the foregoing list of important factors is not exclusive. The Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company.

Critical Accounting Estimates

The consolidated financial statements include amounts that are based on informed judgments of management. These estimates and judgments are the result of management’s need to estimate the effect of matters that are inherently uncertain. Therefore, actual results could vary significantly from the estimates used. Management considers the following items to be the critical accounting estimates contained in the consolidated financial statements.

Allowance for Loan Losses. The allowance for loan losses is based on management’s periodic review of the loan portfolio. In evaluating the adequacy of the allowance for loan losses, management considers factors including, but not limited to, specific loan impairment, historical loss experience, the size and composition of the loan portfolio and current economic conditions. Although management believes that the allowance for loan losses is maintained at an adequate level, there can be no assurance that further additions will not be made to the allowance and that losses will not exceed the estimated amounts.

Available for Sale Securities. The fair value of equity securities is based on quoted market prices and the fair value of debt securities is generally determined based on matrix pricing utilizing yield curves, credit ratings and prepayment speeds. The Company believes the unrealized losses are temporary because the primary reason for the unrealized losses is changes in market interest rates from the date of purchase to the reporting date.

Foreclosed Real Estate. Foreclosed real estate is reported at its net realizable value less estimated costs to sell. The Company monitors the net realizable value of the property on a monthly basis, taking into consideration market and economic factors, including comparison to sales of like properties.

Mortgage Servicing Rights. Mortgage servicing rights are capitalized and then amortized over the period of estimated servicing income. Management periodically evaluates its capitalized mortgage servicing rights for impairment. The valuation of mortgage servicing rights is based on estimated prepayment speeds, ancillary income received from servicing the loans and current interest rates. Changes in these estimates may have a material effect on the valuation of the mortgage servicing rights. Although management believes that the estimates used to determine the value of the mortgage servicing rights are reasonable, future material adjustments may be necessary if economic conditions vary from those used to estimate the value of the servicing rights.

Loans Acquired in Business Combination. Loans acquired as part of the conversion/merger with St. James were recognized at fair value as of the acquisition date. The fair value was estimated by performing a discounted cash flow analysis. The valuation was performed at the loan level on real estate loans and at the cohort level for all other loan types, and is based on the objective attributes of the loans in the portfolio and current statistical performance variables used in the market place. The analysis was based on the contractually specified amounts of principal and interest to be received modified by our estimates of prepayment, default and loss severity to be experienced prospectively.

Wells Financial Corp. and Subsidiary

Average Balance Sheet (dollars in thousands)

The following table sets forth certain information relating to the Bank's average balance sheet and reflects the average yield on assets and average cost of liabilities for the periods indicated and the average yields earned and rates paid. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods presented. The yields for the periods presented include deferred loan origination fees that are considered adjustments to yield. Average balances are derived from month-end balances. Management does not believe that the use of month-end balances instead of daily average balances has caused any material difference in the information presented.

	Years Ended December 31,								
	2016			2015			2014		
	Average Balance	Interest	Average Cost/Yield	Average Balance	Interest	Average Cost/Yield	Average Balance	Interest	Average Cost/Yield
Interest-earning assets:									
Loans receivable (1)	$196,643	$9,023	4.59%	$188,984	$8,836	4.68%	$172,011	$8,088	4.70%
Investments (2)	59,656	856	1.43%	57,442	712	1.24%	59,933	730	1.22%
Total interest-earning assets	256,299	9,879	3.85%	246,426	9,548	3.88%	231,944	8,818	3.80%
Noninterest earning assets	14,153			15,454			16,501		
Total assets	$270,452			$261,880			$248,445		
Interest bearing liabilities:									
Savings, NOW and money Market accounts	$177,185	$102	0.06%	$163,854	$96	0.06%	$145,337	$90	0.06%
Certificates of deposit	57,426	253	0.44%	65,213	354	0.54%	72,900	507	0.70%
Total interest bearing liabilities	234,611	355	0.15%	229,067	450	0.20%	218,237	597	0.27%
Noninterest bearing liabilities	4,157			4,056			3,780		
Total liabilities	238,768			233,123			222,017		
Equity	31,684			28,757			26,428		
Total liabilities and equity	$270 ,452			$261,880			$248,445		
Net interest income		$9,524			$9,098			$8,221	
Interest rate spread (3)			3.70%			3.68%			3.53%
Net yield on interest earning assets (4)			3.72%			3.69%			3.54%
Ratio of average interest earning assets to average interest bearing liabilities	1.09X			1.08X			1.06X		

(1) Average balances include non-accrual loans and loans held for sale.
(2) Includes interest-bearing deposits in other financial institutions.
(3) Interest-rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.
(4) Net yield on interest-earning assets represents net interest income as a percentage of average interest-earning assets.

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Wells Financial Corp. and Subsidiary

(dollars in thousands)

Rate/Volume Analysis

The table below sets forth certain information regarding changes in interest income and interest expense of the Bank for the years indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (i) changes in volume (changes in average volume multiplied by old rate); (ii) changes in rates (changes in rate multiplied by old average volume); (iii) changes in rate-volume (changes in rate multiplied by the change in average volume). The combined effects of changes in both rate and volume that cannot be separately identified have been allocated proportionately to the change due to rate and the change due to volume.

	Years Ended December 31,					
	2016 vs. 2015			2015 vs. 2014		
	Increase (Decrease) Due to			Increase (Decrease) Due to		
	Volume	Rate	Net	Volume	Rate	Net
Interest Income:						
Loans receivable	$ 346	$ (159)	$ 187	$ 793	$ (45)	$ 748
Investments	26	118	144	(31)	13	(18)
Total interest-earning assets	372	(41)	331	762	(32)	730
Interest expense:						
Deposit accounts	(32)	(63)	(95)	(39)	(108)	(147)
Total interest-bearing liabilities	(32)	(63)	(95)	(39)	(108)	(147)
Change in net interest income	$ 404	$ 22	$ 426	$ 801	$ 76	$ 877

Wells Financial Corp. and Subsidiary

(dollars in thousands)

Financial Condition

Total assets decreased by $6,304 during 2016 from $274,779 at December 31, 2015 to $268,475 at December 31, 2016 due to a decrease in cash, which resulted from a decrease in retail deposits from the Bank's customers, primarily certificates of deposit.

Loans held for sale remained consistent at December 31, 2016 when compared to December 31, 2015. On December 31, 2015 and December 31, 2016, the Company had firm commitments to sell the loans that were classified as held for sale. Loans receivable decreased by $509, or less than 1%, from $197,595 at December 31, 2015 to $197,086 at December 31, 2016. The company was able to successfully replace maturities and paydowns, primarily, in residential real estate, home equity loans, and agricultural operating and term loans with growth, primarily, in commercial real estate, commercial operating and term loans, and construction loans in 2016.

In accordance with the Bank's internal classification of assets policy, management evaluates the loan portfolio on a quarterly basis to identify and determine the adequacy of the allowance for loan losses. As of December 31, 2016 and December 31, 2015, the balance in the allowance for loan losses and the allowance for loan losses as a percentage of total loans were $1,907 and $1,988 and 0.96% and 0.99%, respectively.

Loans on which the accrual of interest had been discontinued amounted to $1,710 and $2,061 at December 31, 2016 and 2015, respectively. The Company considers all nonaccrual loans impaired. The amount of impaired loans at December 31, 2016 and 2015 was $4,727 and $3,164, respectively, and the related allowance for loan loss for these loans was $282 and $440, respectively.

Liabilities decreased by $7,079 from $243,479 at December 31, 2015 to $236,400 at December 31, 2016. This decrease resulted primarily from deposit attrition, primarily certificates of deposit.

Stockholders' equity increased by $775 from $31,300 at December 31, 2015 to $32,075 at December 31, 2016. The increase in stockholders' equity resulted, primarily, from the retention of net income of $2,387 being partially offset by payments of $783 in cash dividends and the purchase of $849 in treasury stock.

Wells Financial Corp. and Subsidiary

(dollars in thousands)

Comparison of Operating Results for the Years Ended December 31, 2016 and 2015

General. Net income decreased by $2,507, or 51.2% for 2016 when compared to 2015 due to the bargain purchase gain of $2,848 that was recorded in 2015 which resulted from the conversion/merger with St. James Federal Savings and Loan Association. See Note 16 in the accompanying financial statements for additional information. The decrease in the bargain purchase gain was partially offset by an increase of $426 in net interest income.

Interest Income. Interest income increased by $331, or 3.5%, for 2016 when compared to 2015. The changes in interest income from the loan portfolio and investment securities and other interest bearing deposits resulted from changes in the average balances and yields on those interest earning assets. These changes are detailed in the Average Balance Sheet and Rate/Volume analysis above.

Interest Expense. Interest expense on deposits decreased by $95, or 21.1%, for 2016 when compared to 2015. These changes resulted from changes in the average balances and interest rates. These changes are detailed in the Average Balance Sheet and Rate/Volume analysis above.

Net Interest Income. Net interest income increased by $426, or 4.7%, for 2016 when compared to 2015 due to the changes in interest income and interest expense described above.

Provision for Loan Losses. The provision for loan losses decreased by $30, or 42.9%, for 2016 when compared to 2015. The provision reflects management's monitoring of the allowance for loan losses in relation to the size and quality of the loan portfolio and adjusts the provision for loan losses to adequately provide for loan losses. Due to changes in economic conditions and changes in the composition of the loan portfolio, it is possible that the provision for loan losses will increase in future periods.

Noninterest Income. Noninterest income decreased by $2,868, or 42.2%, for 2016 when compared to 2015 due to the bargain purchase gain recorded in 2015 of $2,848 that resulted from the conversion/merger with St. James in 2015.

Noninterest Expense. Noninterest expense increased by $18, or less than 1%, for 2016 when compared to 2015 due, primarily, to a $334 increase in compensation and benefits, offset by a decrease of $410 in the costs associated with holding other real estate obtained through foreclosures. Data processing costs increased by $62.

Income Tax Expense. Income tax expense increased by $77, or 6.2%, for 2016 when compared to 2015 due to the increase in income subject to taxes. The bargain purchase gain of $2,848 recorded in 2015 was not subject to income tax. Therefore, the difference in income tax as a percentage of income before taxes is due, primarily, to the non-taxable nature of the bargain purchase gain that was recognized in the conversion merger with St. James in 2015.

RSM US LLP

Independent Auditor's Report

To the Board of Directors and Stockholders
Wells Financial Corp. and Subsidiary
Wells, Minnesota

Report on the Financial Statements
We have audited the accompanying consolidated financial statements of Wells Financial Corp. and Subsidiary (the Company), which comprise the consolidated balance sheets as of December 31, 2016 and 2015, the related consolidated statements of income, comprehensive income (loss), stockholders' equity and cash flows for the years then ended, and the related notes to the consolidated financial statements (collectively, 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 audit as of and for the year ended December 31, 2016, in accordance with auditing standards generally accepted in the United States of America. We conducted our audit as of and for the year ended December 31, 2015, in accordance with standards of the Public Company Accounting Oversight Board (United States). 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. These procedures include examining, on a test basis, evidence supporting 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 Wells Financial Corp. and Subsidiary as of December 31, 2016 and 2015, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

RSM US LLP

Rochester, Minnesota
March 28, 2017

Wells Financial Corp. and Subsidiary

Consolidated Balance Sheets
December 31, 2016 and 2015
(Dollars in Thousands, Except Per Share Data)

Assets	2016	2015
Cash and cash equivalents, including interest-bearing accounts, 2016, $152; 2015, $6,078	$ 5,777	$ 12,059
Certificates of deposit, at cost	13,582	9,543
Federal funds sold	5,900	9,100
Securities available for sale	33,632	34,450
Federal Home Loan Bank stock, at cost	1,858	1,986
Loans held for sale	1,338	1,337
Loans receivable, net of allowance for loan loss of $1,907 in 2016; $1,988 in 2015	197,086	197,595
Accrued interest receivable	1,071	1,020
Premises and equipment, net	3,749	3,368
Mortgage servicing rights, net	1,787	1,863
Foreclosed real estate, net	1,709	1,632
Other assets	986	826
Total assets	$ 268,475	$ 274,779

Liabilities and Stockholders' Equity	2016	2015
Liabilities		
Deposits	$ 233,010	$ 239,950
Advances from borrowers for taxes and insurance	2,749	2,646
Accrued interest payable	21	12
Accrued expenses and other liabilities	620	871
Total liabilities	236,400	243,479
Commitments, Contingencies and Credit Risk (Notes 14 and 15)		
Stockholders' Equity		
Common stock, $0.10 par value; 7,000,000 shares authorized; 2,140,379 shares issued at December 31, 2016 2,266,236 shares issued at December 31, 2015	214	214
Additional paid-in capital	18,121	18,136
Retained earnings, substantially restricted	44,024	42,413
Accumulated other comprehensive income (loss)	(5)	66
Unallocated Employee Stock Ownership Plan shares	(82)	(146)
Treasury stock, 2016, 1,361,591 shares; 2015, 1,463,388 shares	(30,197)	(29,383)
Total stockholders' equity	32,075	31,300
Total liabilities and stockholders' equity	$ 268,475	$ 274,779

See Notes to Consolidated Financial Statements.

Wells Financial Corp. and Subsidiary

Consolidated Statements of Income
Years Ended December 31, 2016 and 2015
(Dollars in Thousands, Except Per Share Data)

	2016	2015
Interest income:		
Loans receivable	$ 9,023	$ 8,836
Investment securities and interest-bearing deposits	856	712
Total interest income	9,879	9,548
Interest expense:		
Deposits	355	450
Total interest expense	355	450
Net interest income	9,524	9,098
Provision for loan losses	40	70
Net interest income after provision for loan losses	9,484	9,028
Noninterest income:		
Gain on sale of loans held for sale	1,111	1,068
Loan servicing fees	802	848
Insurance commissions	1,003	685
Fees and service charges	451	462
Bargain purchase gain	-	2,848
Other	561	885
Total noninterest income	3,928	6,796
Noninterest expenses:		
Compensation and benefits	5,104	4,770
Occupancy	762	757
Data processing	1,027	965
Advertising	285	287
Amortization of mortgage servicing rights	355	351
Other real estate owned	71	481
Other	2,100	2,075
Total noninterest expenses	9,704	9,686
Income before income taxes	3,708	6,138
Income tax expense	1,321	1,244
Net income	$ 2,387	$ 4,894
Earnings per share:		
Basic	$ 3.04	$ 6.35
Diluted	3.04	6.35

See Notes to Consolidated Financial Statements.

Wells Financial Corp. and Subsidiary

Consolidated Statements of Comprehensive Income (Loss)
Years Ended December 31, 2016 and 2015
(Dollars in Thousands, Except Per Share Data)

	2016	2015
Net income	$ 2,387	$ 4,894
Other comprehensive loss:		
Unrealized loss on securities, net of related taxes	(71)	(27)
Comprehensive income	$ 2,316	$ 4,867

See Notes to Consolidated Financial Statements.

Wells Financial Corp. and Subsidiary

Consolidated Statements of Stockholders' Equity
Years Ended December 31, 2016 and 2015
(Dollars in Thousands, Except Per Share Data)

	Common Stock	Additional Paid-In Capital	Retained Earnings
Balances, December 31, 2014	$ 206	$ 17,123	$ 38,423
Net income	-	-	4,894
Issuance of 78,736 shares of common stock including 6,299 shares acquired by the ESOP, net of costs	8	999	-
Other comprehensive loss, net of related taxes	-	-	-
Cash dividends declared ($0.72 per share)	-	-	(556)
Stock-based compensation	-	14	-
Treasury stock purchases, 18,140 shares	-	-	-
Balances, December 31, 2015	214	18,136	42,413
Net income	-	-	2,387
Other comprehensive loss, net of related taxes	-	-	-
Cash dividends declared ($1.00 per share)	-	-	(783)
Stock-based compensation	-	(15)	7
Treasury stock purchases, 25,660 shares	-	-	-
Balances, December 31, 2016	**$ 214**	**$ 18,121**	**$ 44,024**

See Notes to Consolidated Financial Statements.

Accumulated Other Comprehensive Income (Loss)	Unallocated ESOP Plan Shares	Treasury Stock	Total Stockholders' Equity
$ 93	$ -	$ (28,878)	**$ 26,619**
-	-	-	**4,894**
-	(172)	-	**835**
(27)	-	-	**(27)**
-	-	-	**(556)**
-	26	-	**40**
-	-	(505)	**(505)**
66	(146)	(29,383)	**31,300**
-	-	-	**2,387**
(71)	-	-	**(71)**
-	-	-	**(783)**
-	64	35	**91**
-	-	(849)	**(849)**
$ (5)	**$ (82)**	**$ (30,197)**	**$ 32,075**

Wells Financial Corp. and Subsidiary
Consolidated Statements of Cash Flows
Years Ended December 31, 2016 and 2015
(Dollars in Thousands, Except Per Share Data)

	2016	2015
Cash Flows From Operating Activities		
Net income	$ 2,387	$ 4,894
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	40	70
Gain on sale of loans	(1,111)	(1,068)
Originations of loans held for sale	(33,729)	(33,266)
Proceeds from the sale of loans held for sale	34,839	34,704
Net change in mortgage servicing rights	76	23
Loss on sale of fixed assets	33	-
Gain on sales of foreclosed real estate, net	-	(4)
Gain on sales of securities	2	-
Deferred income taxes	(12)	253
Depreciation expense	196	195
Amortization of net deferred loan origination fees	(81)	(81)
Amortization of securities premiums	257	257
Impairment of foreclosed real estate	10	241
Stock-based compensation expense	71	40
Bargain purchase gain	-	(2,848)
Changes in assets and liabilities:		
Accrued interest receivable	(51)	(77)
Other assets	(209)	726
Accrued expenses and other liabilities	(137)	(27)
Net cash provided by operating activities	2,581	4,032
Cash Flows From Investing Activities		
Net decrease in loans	412	1,863
Net decrease (increase) in certificates of deposit	(4,049)	250
Net decrease (increase) in federal funds sold	3,200	(7,100)
Purchase of Federal Home Loan Bank stock	(184)	(132)
Proceeds from sale of Federal Home Loan Bank stock	312	258
Cash flows from available-for-sale securities	454	375
Net cash received in conversion/merger	-	1,337
Purchase of premises and equipment	(610)	(25)
Proceeds from sales of foreclosed real estate	51	1,931
Net cash used in investing activities	(414)	(1,243)
Cash Flows From Financing Activities		
Net decrease in deposits	(6,940)	(5,065)
Net increase in advances from borrowers for taxes and insurance	103	16
Issuance of 78,736 shares of common stock, net of issuance costs and ESOP shares	-	1,007
Dividends paid	(783)	(556)
Purchase of treasury stock	(829)	(505)
Net cash used by financing activities	(8,449)	(5,103)
Net decrease in cash and cash equivalents	(6,282)	(2,314)
Cash and Cash Equivalents		
Beginning	12,059	14,373
Ending	$ 5,777	$ 12,059

See additional cash flow information in Footnote19

See Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies

Nature of operations: Operations of Wells Financial Corp. (the Company) primarily consist of banking services through Wells Federal Bank (the Bank), and Wells Insurance Agency, Inc., a property and casualty insurance agency. The Company serves its customers through the Bank's nine locations in south central Minnesota.

Principles of consolidation: The accompanying consolidated financial statements include the accounts of Wells Financial Corp., its wholly owned subsidiary, Wells Federal Bank, and the Bank's wholly owned subsidiary, Wells Insurance Agency, Inc. All significant intercompany transactions and balances are eliminated in consolidation.

Basis of financial statement presentation: The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America.

Use of estimates: In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated balance sheets and revenues and expenses for the reporting period. Actual results could differ from those estimates. Estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, valuation of available-for-sale securities, mortgage servicing rights, and foreclosed real estate.

Cash and cash equivalents: Cash and cash equivalents include cash on hand, demand, and interest-bearing deposits at other financial institutions, and amounts due from banks (including cash items in the process of clearing). For the purpose of reporting cash flows, cash flows from loans (except loans originated for sale), federal funds sold, certificates of deposit, advances from borrowers for taxes and insurance, and deposits are reported net.

Federal Home Loan Bank stock: The Bank is a member of the Federal Home Loan Bank of Des Moines (FHLB) and, as such, is required to maintain a minimum investment in stock of the Federal Home Loan Bank that varies with the level of advances outstanding with the Federal Home Loan Bank. The stock is bought from and sold to the Federal Home Loan Bank based upon its $100 par value. The stock does not have a readily determinable fair value and, as such, is classified as restricted stock, carried at cost and evaluated for impairment. In accordance with this guidance, the stock's value is determined by the ultimate recoverability of the par value rather than by recognizing temporary declines. The determination of whether the par value will ultimately be recovered is influenced by criteria such as the following: (a) the significance of the decline in net assets of the Federal Home Loan Bank as compared to the capital stock amount and the length of time this situation has persisted, (b) commitments by the Federal Home Loan Bank to make payments required by law or regulation and the level of such payments in relation to the operating performance, (c) the impact of legislative and regulatory changes on the customer base of the Federal Home Loan Bank and (d) the liquidity position of the Federal Home Loan Bank. The Company has not recognized any impairment as of December 31, 2016 and 2015.

Securities available for sale: Securities classified as available-for-sale include all marketable equity securities and those debt securities the Company intends to hold for an indefinite period of time, but not necessarily to maturity. Any decision to sell a security classified as available-for-sale would be based on various factors, including significant movements in interest rates, changes in the maturity mix of the Company's assets and liabilities, liquidity needs, regulatory capital considerations and other similar factors.

Note 1. Summary of Significant Accounting Policies (Continued)

Securities available for sale are carried at fair value. Unrealized gains or losses, net of the related deferred tax effect, are reported as a net amount in accumulated other comprehensive income (loss). Amortization of premiums and accretion of discounts, computed by the interest method over their contractual lives, are recognized in interest income. Realized gains or losses, determined on the basis of the cost of specific securities sold, are included in earnings. Declines in the fair value of individual securities below their amortized cost that are determined to be other than temporary result in write-downs of the individual securities to their fair value, with the resulting write-downs included in current earnings as realized losses.

The Company evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. The Company employs a systematic methodology that considers available evidence in evaluating potential impairment of its investments. The assessment of whether such impairment has occurred is based on management's case-by-case evaluation of the underlying reasons for the decline in fair value. Once a decline in fair value is determined to be other than temporary, an impairment charge is recorded in investment income, and a new cost basis in the investment is established.

Securities with unrealized losses that the Company deems to be other than temporary are recognized as realized losses. The assessment of whether such impairment has occurred is based on management's case-by-case evaluation of the underlying reasons for the decline in fair value. As part of their assessment process, management determines whether (a) they do not have the intent to sell a debt security prior to recovery and (b) it is more likely than not that they will not have to sell the debt security prior to recovery, in which case the security would not be considered other than temporarily impaired, unless there is a credit loss. When management does not intend to sell the security, and it is more likely than not they will not have to sell the security before recovery of its cost basis, the Company will recognize the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income.

Loans held for sale: Loans held for sale are those loans the Company has the intent to sell in the foreseeable future. They are carried at the lower of aggregate cost or fair value. Gains and losses on sales of loans are recognized at settlement dates and are determined by the difference between the sales proceeds and the carrying value of the loans after allocating cost to servicing rights retained. All sales are made without recourse.

Interest rate lock commitments on mortgage loans to be funded and sold are valued at fair value and are included in other assets or liabilities, if material.

Loans receivable: The Company generally originates single-family residential loans within its primary lending area of south central Minnesota and northern Iowa. These loans are secured by the underlying properties. The Company is also active in originating residential real estate, commercial real estate, agricultural real estate, commercial construction real estate, residential construction real estate, home equity, commercial operating, agricultural operating, vehicle, and consumer loans.

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at the amount of unpaid principal, reduced by an allowance for loan losses, unaccreted discount and net deferred origination fees. Interest is accrued daily on the outstanding balances.

Interest on loans is generally recognized over the terms of the loans using the simple-interest method on principal amounts outstanding.

Note 1. Summary of Significant Accounting Policies (Continued)

The Company determines a loan to be delinquent when payments have not been made according to contractual terms, typically evidenced by nonpayment of a monthly installment by the due date. Accrual of interest is discontinued for loans at the time the loan is 90 days delinquent, unless the credit is well-secured and in the process of collection. All interest accrued but not collected for loans that are placed on nonaccrual status is reversed against interest income. Accrual of interest is generally resumed when the borrower has demonstrated the ability to make all periodic interest and principal payments.

Allowance for loan losses: The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that collectability of the principal is unlikely. Subsequent recoveries, if any, are credited to the allowance.

The allowance is an amount that management believes will be adequate to absorb estimated losses relating to specifically identified loans, as well as probable credit losses inherent in the balance of the loan portfolio, based on an evaluation of the collectability of existing loans and prior loss experience. This evaluation also takes into consideration such factors as changes in the nature and volume of the loan portfolio, the value of underlying collateral, overall portfolio quality, review of specific problem loans, and current economic conditions that may affect the borrower's ability to pay. While management uses the best information available to make its evaluation, future adjustments to the allowance may be necessary if there are significant changes in economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan losses and may require the Bank to make additions to the allowance based on their judgment about information available to them at the time of their examinations.

The allowance consists of specific and general components.

The Company maintains a loan loss reserve for all commercial loans and agricultural operating loans in the portfolio using a risk-rating system. The calculated allowance is evaluated against the historical loss default rate for each loan type above (net of recoveries) to determine an appropriate level of allowance by loan type.

Homogeneous loans with similar risk and loss characteristics are also assessed for probable losses. These loan pools include consumer, residential real estate, agricultural real estate, home equity, and vehicle loans. Historical loss default rates are multiplied by the total of each portfolio segment to determine an appropriate level of allowance by segment.

The general allowance for loan losses also includes estimated losses resulting from macroeconomic factors and adjustments to account for imprecision of the loan loss model. Macroeconomic factors adjust the allowance for loan losses upward or downward based on the current point in the economic cycle and are applied to the loan loss model through a separate allowance element. The Company reviews the macroeconomic factors in order to conclude they are adequate based on current economic conditions.

Note 1. Summary of Significant Accounting Policies (Continued)

The specific component of the allowance for loan losses relates to loans that are considered to be impaired. A loan is impaired when it is probable, based on current information and events, the Company will be unable to collect all contractual principal and interest payments due in accordance with the terms of the loan agreement. Impaired loans are measured on an individual basis based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. The Company obtains external appraisals on real estate–related impaired loans. Other valuation techniques are used as well, including internal valuations, comparable property analyses, and contractual sales information. The Company may further discount appraisal values based on their age and the relationship to the listed comparables. The amount of impairment, if any, and any subsequent changes are included in the provision for loan losses.

Accrual of interest on impaired loans is discontinued when management believes the borrower's financial condition is such that collection of interest is doubtful. Impaired loans also include loans that have been renegotiated in a troubled debt restructuring. Cash collections on impaired loans are generally credited to the loan balance, and no interest income is recognized on those loans until the principal balance has been determined to be collectible.

Troubled debt restructurings: A loan is classified as a troubled debt restructuring when a borrower is experiencing financial difficulties that lead to a restructuring of the loan, and the Company grants concessions to the borrower in the restructuring that it would not otherwise consider. These concessions may include rate reductions, principal forgiveness, extension of maturity date, and other actions intended to minimize potential losses. Performance prior to the restructuring is considered when assessing whether the borrower can meet the new terms and may result in the loan being returned to accrual at the time of the restructuring or after a shorter performance period.

Loan origination fees and related costs: Loan origination and commitment 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 Company's historical prepayment experience.

Loan servicing: The Company sells loans to investors in the secondary market and generally retains the right to service mortgage loans sold to others. Mortgage servicing rights retained are initially measured at fair value and have been recognized as a separate asset and are being amortized in proportion to and over the period of estimated net servicing income.

Mortgage servicing rights are subject to change based primarily on changes in the mix of loans, interest rates, prepayment speeds, or default rates from the estimates used in the valuation of the mortgage servicing rights. Such changes may have a material effect on the amortization and valuation of mortgage servicing rights. Although management believes that the assumptions used to evaluate the mortgage servicing rights for impairment are reasonable, future adjustment may be necessary if future economic conditions differ substantially from the economic assumptions used to determine the value of the mortgage servicing rights.

Note 1. Summary of Significant Accounting Policies (Continued)

Mortgage servicing rights are periodically evaluated for impairment based on the fair value of those rights. Fair values are estimated using discounted cash flows based upon estimated prepayment speeds, ancillary income received from loan servicing, and current interest rates. For purposes of measuring impairment, the rights must be stratified by one or more predominant risk characteristics of the underlying loans. The Company stratifies its capitalized mortgage servicing rights based on interest rates and the term of the underlying loans. The amount of impairment recognized is the amount, if any, by which the amortized cost of the rights for each stratum exceeds their fair value.

Foreclosed real estate: Real estate properties acquired through, or in lieu of, loan foreclosure are initially recorded at their fair value less estimated costs to sell at the date of foreclosure, establishing a new cost basis. Any write-down to fair value less estimated costs to sell at the time of transfer to foreclosed real estate is charged to the allowance for loan loss, establishing a new cost basis. Costs relating to improvement of property are capitalized, whereas costs relating to the holding of property are expensed. Valuations are periodically performed by management, and charge-offs to expense are made if the carrying value of a property exceeds its estimated fair value less estimated costs to sell.

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 entity, (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 entity does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Core deposit intangible assets: The Company has $180 and $285 in recorded core deposit intangible assets at December 31, 2016 and 2015. The amounts are included in the consolidated balance sheets under the caption other assets. The core deposit intangible assets are being amortized on a straight line basis over 8 years. Amortization recorded in the years ending December 31, 2016 and 2015 was $105 and $68, respectively

Advertising: Advertising costs are expensed as incurred.

Premises and equipment: Land is carried at cost. Bank premises, leasehold improvements, and furniture, fixtures and equipment are carried at cost, less accumulated depreciation and amortization. Repairs and maintenance are expensed as incurred while major additions and improvements are capitalized. Gains and losses on dispositions are included in other income and expense. Bank premises and furniture, fixtures and equipment are depreciated using the straight-line method over the estimated useful lives of the assets ranging from 10 to 40 years for bank premises and three to seven years for furniture, fixtures and equipment. The cost of leasehold improvements is being amortized using the straight-line method over the terms of the related leases, generally seven to 10 years.

Comprehensive income: Accounting principles generally accepted in the United States of America 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 on the consolidated statement of comprehensive income (loss). Such items, along with net income, are components of comprehensive income (loss). Gains and losses on available-for-sale securities are reclassified to net income as the gains or losses are realized upon sale of the securities. Other-than-temporary impairment charges are reclassified to net income at the time of the charge.

Note 1. Summary of Significant Accounting Policies (Continued)

Income taxes: Deferred taxes are provided on an asset and liability method, whereby deferred tax assets are recognized for deductible temporary differences and operating loss or tax credit carryforwards, and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the amounts of assets and liabilities recorded for income tax and financial reporting purposes. The Company is allowed bad-debt deductions based on actual charge-offs. Deferred tax assets are reduced by a valuation allowance when management determines that it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Earnings per share: Basic earnings per common share are computed based upon the weighted-average number of common shares outstanding during each year. Dilutive per share amounts assume conversion, exercise or issuance of all potential common stock instruments, unless the effect is to reduce a loss or increase income per common share.

Employee stock plans: The Company accounts for stock-based compensation plans under the recognition and measurement principles of Equity and Compensation—Stock Compensation topics of the Accounting Standards Codification (ASC), which require that the compensation cost relating to share-based payment transactions be recognized in financial statements. That cost is measured based on the fair value of the equity or liability instruments issued. The effect of these topics is to require entities to measure the cost of employee services received in exchange for stock awards based on the grant-date fair value of the award, and to recognize the cost over the period the employee is required to provide services for the award.

Fair value of financial instruments: The following methods and assumptions were used by the Company in estimating the fair value of its financial instruments:

Cash and cash equivalents: The carrying amounts reported for cash and cash equivalents approximate their fair values.

Certificates of deposit: Due to the short duration of the instruments, the carrying amounts reported for certificates of deposit approximate their fair values.

Federal funds sold: The carrying amounts reported for federal funds sold approximate their fair values.

Securities available for sale: The fair value of debt securities was generally determined based on matrix pricing. Matrix pricing is a mathematical technique that utilizes observable market inputs including, for example, yield curves, credit ratings and prepayment speeds. The fair value of government-sponsored enterprise equity securities is determined based on documented trade history.

Federal Home Loan Bank stock: The carrying amount approximates fair value.

Loans held for sale: Fair values are based on quoted market prices of similar loans sold on the secondary market.

Note 1. Summary of Significant Accounting Policies (Continued)

Loans and accrued interest receivable: For variable-rate loans that reprice frequently and that have experienced no significant change in credit risk, fair values are based on carrying values. Fair values for all other loans are estimated based on discounted cash flows, using interest rates currently being offered for loans with similar terms to borrowers with similar credit quality. The carrying amount of accrued interest receivable approximates its fair value.

Mortgage servicing rights: Fair values are estimated using discounted cash flows based on current market rates and conditions.

Deposits and other liabilities: The fair values disclosed for demand deposits and savings accounts are, by definition, equal to their carrying amounts, which represent the amounts payable on demand. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on those certificates. The carrying amounts of advances by borrowers for taxes and insurance and accrued interest payable approximate their fair values.

Off-balance-sheet instruments: Since the majority of the Company's off-balance-sheet instruments consist of non–fee-producing commitments to originate and sell loans, the Company has determined they do not have a significant fair value.

Derivatives—rate-lock commitments: The Company enters into commitments to originate loans whereby the interest rate on the loan is determined prior to funding (rate-lock commitment). Rate-lock commitments on mortgage loans held for sale are derivatives. Derivative instruments are recognized in the consolidated balance sheet at fair value, and changes in the fair value thereof are recognized in the consolidated statement of income. The Company originates single-family residential loans for sale pursuant to programs primarily with the Federal Home Loan Mortgage Corporation (FHLMC). Under the structure of the programs, at the time the Company initially issues a loan commitment in connection with such programs, it does not lock in a specific interest rate. At the time the interest rate is locked in by the borrower, the Company concurrently enters into a forward loan sale agreement with respect to the sale of such loan at a set price in an effort to manage the interest rate risk inherent in the locked loan commitment.

The forward loan sale agreement also meets the definition of a derivative instrument. Any change in the fair value of the loan commitment after the borrower locks in the interest rate is substantially offset by the corresponding change in the fair value of the forward loan sale agreement related to such loan. The period from the time the borrower locks in the interest rate to the time the Company funds the loan and sells it to FHLMC is generally 60 days. The fair value of each instrument will rise or fall in response to changes in market interest rates subsequent to the dates the interest rate locks and forward loan sale agreements are entered into. In the event that interest rates rise after the Company enters into an interest rate lock, the fair value of the loan commitment will decline. However, the fair value of the forward loan sale agreement related to such loan commitment should increase by substantially the same amount, effectively eliminating the Company's interest rate and price risk.

Note 1. Summary of Significant Accounting Policies (Continued)

At December 31, 2016, the Company had $2,501 of loan commitments outstanding related to loans being originated for sale, all of which were subject to interest rate locks and forward loan sale agreements as described above. The fair values of outstanding interest rate-lock commitments and forward sale commitments were considered immaterial to the Company's consolidated financial statements as of December 31, 2016 and 2015, and therefore, are not recognized in the consolidated financial statements and are not included in the disclosures in Note 18.

Fair value measurements: The Fair Value topic of the ASC defines fair value, establishes a framework for measuring fair value, and requires certain disclosures about fair value measurement. This topic also emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and sets out a fair value hierarchy, with the highest priority being quoted prices in active markets. Fair value measurements are disclosed by level within that hierarchy.

Recent accounting pronouncements: In August 2014, the FASB issued ASU 2014-14, Troubled Debt Restructurings by Creditors (Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure, which requires, if certain conditions are met, an entity to derecognize a mortgage loan with a government guarantee upon foreclosure and to recognize a separate other receivable. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. This ASU was effective for the Company for annual periods ending after December 15, 2015. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue Recognition – Revenue from Contracts with Customers (Topic 606).* This ASU provides guidance on when to recognize revenue from contracts with customers. The objective of this ASU is to eliminate diversity in practice related to this topic and to develop guidance that would streamline and enhance revenue recognition requirements. The ASU defines five steps to recognize revenue including, identify the contract with a customer, identify the performance obligations in the contract, determine a transaction price, allocate the transaction price to the performance obligations and then recognize the revenue when or as the entity satisfies a performance obligation. This update is effective for public entities annual reporting periods beginning after December 15, 2017, and the Company is currently assessing the potential impact to the consolidated financial statements.

In September 2015, the FASB issued ASU 2015-16, *Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments*. This ASU eliminates the requirement to retrospectively account for changes to provisional amounts initially recorded in a business combination. ASU 2015-16 requires that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustments are determined, including the effect of the change in provisional amount as if the accounting had been completed at the acquisition date. The provisions of this ASU are effective for fiscal years beginning after December 15, 2015, and should be applied prospectively to adjustments to provisional amounts that occur after the effective date. The adoption of this standard is not expected to have a material impact on the Company's financial statements.

Note 1. Summary of Significant Accounting Policies (Continued)

In January 2016, the FASB issued ASU 2016-01, Financial Instruments—Overall (Subtopic 825-10): Recognitions and Measurement of Financial Assets and Financial Liabilities. ASU 2016-01 included the following changes: require equity investments to be measured at fair value with changes in fair value recognized in net income, simplify the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment, eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities, eliminate the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet, require public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, require 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, require separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements, and clarify 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. This ASU will be effective for the Company for annual periods ending after December 15, 2018. The adoption of this ASU is not expected to have a material impact on the Company's consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). The guidance in this ASU supersedes the leasing guidance in Topic 840, Leases. Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning January 1, 2020, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The adoption of this ASU is not expected to have a material impact on the Company's consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which creates a new credit impairment standard for financial assets measured at amortized cost and available-for-sale debt securities. The ASU requires financial assets measured at amortized cost (including loans, trade receivables and held-to-maturity debt securities) to be presented at the net amount expected to be collected, through an allowance for credit losses that are expected to occur over the remaining life of the asset, rather than incurred losses. The ASU requires that credit losses on available-for-sale debt securities be presented as an allowance rather than as a direct write-down. The measurement of credit losses for newly recognized financial assets (other than certain purchased assets) and subsequent changes in the allowance for credit losses are recorded in the statement of income as the amounts expected to be collected change. The ASU is effective for fiscal years beginning January 1, 2021. Early adoption is permitted for fiscal years beginning after December 15, 2018. The Company does not intend to early adopt. The Company is currently evaluating the impact of adopting this new guidance on its financial statements and expects the impact to be significant.

Note 1. Summary of Significant Accounting Policies (Continued)

In January 2017, the FASB issued ASU 2017-04 which removes step two of the goodwill impairment test, which requires a hypothetical purchase price allocation. A goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. All other goodwill impairment guidance will remain largely unchanged.

The update is effective in fiscal years beginning after December 15, 2021. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The adoption of this amendment is not expected to have a significant effect on the Company's consolidated financial statements.

Segment reporting: The Company's activities are considered to be a single industry segment for financial reporting purposes. The Company is engaged in commercial and retail banking, investment and insurance services with operations in southern Minnesota. Substantially all income is derived from a diverse base of commercial and retail lending activities.

Note 2. Certificates of Deposit

Certificates of deposit with a carrying value of $13,582 and $9,543 at December 31, 2016, and 2015, respectively, had weighted-average yields of 1.40% and 1.20% at December 31, 2016, and 2015, respectively and weighted average contractual maturities of 1.3 and 1.6 years, respectively.

(Dollars in Thousands, Except Per Share Data)

Note 3. Securities Available for Sale

	December 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Residential mortgage-backed agencies	$ 18,233	$ 29	$ (192)	$ 18,070
Small business administration commercial pools	3,405	11	(17)	3,399
Obligations of state and political subdivisions	11,963	133	(142)	11,954
Government-sponsored enterprise equity	40	169	-	209
	$ 33,641	$ 342	$ (351)	$ 33,632

	December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Residential mortgage-backed agencies	$ 20,290	$ 35	$ (183)	$ 20,142
Small business administration commercial pools	2,572	9	(7)	2,574
Obligations of state and political subdivisions	11,442	212	(12)	11,642
Government-sponsored enterprise equity	40	52	-	92
	$ 34,344	$ 308	$ (202)	$ 34,450

(Dollars in Thousands, Except Per Share Data)

Note 3. Securities Available for Sale (Continued)

Contractual maturities: The amortized cost and fair value of securities available for sale as of December 31, 2016, by contractual maturity are shown below. Maturities may differ from contractual maturities in residential mortgage-backed securities and Small Business Administration (SBA) pools because the mortgages underlying the securities may be called or repaid without any penalties. In addition, government-sponsored enterprise equity securities have no maturity. Therefore, these securities are not included in the maturity categories in the following maturity summary.

	December 31, 2016	
	Amortized Cost	Fair Value
Due in one year or less	$ 1,887	$ 1,861
Due in one to five years	5,387	5,471
Due after five through 10 years	4,425	4,358
Due after 10 years	264	264
	11,963	11,954
Residential mortgage-backed agencies	18,233	18,070
SBA commercial pools	3,405	3,399
Government-sponsored enterprise equity	40	209
	$ 33,641	$ 33,632

Pledged securities: Securities with a carrying value of $18,709 and $22,127 at December 31, 2016 and 2015, respectively, were pledged to secure borrowed funds and for other purposes as required or permitted by law.

Changes in other comprehensive income (loss) — unrealized gains on securities available for sale:

	Years Ended December 31	
	2016	2015
Balance, beginning	$ 66	$ 93
Unrealized losses during the year	(114)	(46)
Deferred tax effect relating to unrealized losses	43	19
Balance, ending	$ (5)	$ 66

(Dollars in Thousands, Except Per Share Data)

Note 3. Securities Available for Sale (Continued)

Temporarily impaired securities:

	December 31, 2016					
	Continuous Unrealized Losses Existing 12 Months or Less		Continuous Unrealized Losses Existing Greater Than 12 Months		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Residential mortgage-backed agencies	$ 9,780	$ 124	$ 3,612	$ 68	$ 13,392	$ 192
SBA pools	1,050	10	925	7	1,975	17
Obligations of states and political subdivisions	6,666	142	-	-	6,666	142
	$ 17,496	$ 276	$ 4,537	$ 75	$ 22,033	$ 351

	December 31, 2015					
	Continuous Unrealized Losses Existing 12 Months or Less		Continuous Unrealized Losses Existing Greater Than 12 Months		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Residential mortgage-backed agencies	$ 7,975	$ 76	$ 6,075	$ 107	$ 14,050	$ 183
SBA pools	1,126	7	-	-	1,126	7
Obligations of states and political subdivisions	2,759	4	925	8	3,684	12
	$ 11,860	$ 87	$ 7,000	$ 115	$ 18,860	$ 202

There were 58 securities in unrealized loss positions as of December 31, 2016 and 37 securities in unrealized loss positions as of December 31, 2015. Unrealized losses are deemed to be temporary. Most of these underlying securities consist of mortgage-backed securities. Market fluctuations are caused primarily by changes in interest rates and prepayments of underlying mortgages. Volatility in economic conditions influences the prices of these securities. Gross realized gains and losses, and proceeds on the sale of available-for-sale securities during the years ended December 31, 2016 and 2015 were not significant.

(Dollars in Thousands, Except Per Share Data)

Note 4. Loans Receivable and Loans Held for Sale

Composition of loans receivable:

	December 31	
	2016	2015
Residential real estate	$ 56,338	$ 60,161
Commercial real estate	37,308	32,935
Agricultural real estate	38,355	39,271
Commercial construction real estate	6,411	2,264
Residential construction real estate	1,668	1,370
Home equity, home improvement and second mortgages	30,659	32,645
Commercial operating and term	10,670	9,322
Agricultural operating and term	10,318	12,867
Vehicle	2,209	2,622
Consumer	5,208	6,328
Total loans	199,144	199,785
Net deferred loan origination fees	(151)	(202)
Allowance for loan loss	(1,907)	(1,988)
Loans receivable, net	$ 197,086	$ 197,595

Loans are made to individuals as well as commercial and tax-exempt entities. Specific loan terms vary as to interest rate, repayment and collateral requirements based on the type of loan requested and the creditworthiness of the prospective borrower. Credit risk tends to be geographically concentrated in that a majority of the loan customers are located in the markets serviced by the Company.

The Company's extension of credit is governed by the individual loan policies that were established to control the quality of the Company's loans. These policies and procedures are reviewed and approved by the Board of Directors on a regular basis.

Residential real estate loans: The Company originates residential real estate loans in its service area and also originates loans throughout Minnesota through its correspondent bank relationships. These loans are one to four family loans. Currently, the majority of residential real estate loans being originated are sold to the secondary market and are reported in the financial statements as loans held for sale.

Commercial real estate loans: The Company's goal is to create and maintain a high-quality portfolio of commercial real estate loans with customers who meet the quality and relationship profitability objectives of the Company. Commercial real estate loans are subject to underwriting standards and processes similar to commercial operating and term loans. These loans are underwritten using historical and projected cash flows, and the repayment of these loans is largely dependent on the successful operation of the property. Loan performance may be adversely affected by factors impacting the general economy or conditions specific to the real estate market, such as geographic location and property type.

Agricultural real estate loans: The Company originates loans secured by agricultural real estate in its service area. Agricultural land in the Company's service area is considered to be prime agricultural land. These loans are underwritten using both a cash flow analysis and appraised values. These are amortizing loans, and loan-to-value ratios generally do not exceed 60 percent at loan inception.

Note 4. Loans Receivable and Loans Held for Sale (Continued)

Commercial construction real estate loans: The Company defines construction loans as loans where the loan proceeds are controlled by the Company and used exclusively for the improvement of real estate in which the Company holds a mortgage. Commercial construction loans are underwritten based on projected cash flows and value of the construction project, generally up to 80% of cost or appraised value, whichever is less. Construction cost over-runs and construction delays may have a negative impact on the property valuation when completed. Due to the inherent risk in this type of loan, they are subject to other industry-specific policy guidelines outlined in the Company's credit risk policy and are monitored closely.

Residential construction real estate loans: Residential construction loans originated by the Company generally are limited to six-month terms. When construction is completed, these loans are converted to permanent financing or sold to the secondary market. Construction cost over-runs and construction delays may have a negative impact on the property valuation when completed and prevent the Company from selling the permanent financing to the secondary market.

Commercial operating and term loans: Commercial operating and term loans are originated in the Company's primary service area. These loans are made to individuals, partnerships, corporations, limited liability partnerships and limited liability companies for the purpose of assisting in the development of a business enterprise. Loans to closely held businesses will generally be guaranteed in full or for a meaningful amount by the businesses' major owners. Commercial loans are made based primarily on the historical and projected cash flow of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not perform as forecasted, and collateral securing loans may fluctuate in value due to economic or individual performance factors. Minimum standards and underwriting guidelines have been established for all commercial loan types.

Agricultural operating and term loans: Agricultural operating and term loans are originated in the Company's primary service area and are generally used to purchase agricultural equipment or crop inputs. These loans are primarily secured by agricultural real estate and agricultural equipment or crops. Agricultural term and operating loans are made based primarily on the historical and projected cash flow of the borrower and secondarily on the underlying collateral. Based on an analysis of the customer's credit, the Company will lend up to 85% of the current market value of the collateral. The cash flows of borrowers, however, may not behave as forecasted, and collateral securing loans may fluctuate in value due to economic or individual performance factors.

Consumer loans, including home equity, home improvement and second mortgages, and vehicle loans: The Company originates direct consumer loans, including home equity lines and loans, credit cards, and vehicle loans, using a scoring-based credit analysis as part of the underwriting process. Each loan type has a separate specified scoring that consists of several factors, including debt to income, type of collateral and loan-to-collateral value, credit history, and Company relationship with the borrower.

(Dollars in Thousands, Except Per Share Data)

Note 4. Loans Receivable and Loans Held for Sale (Continued)

Loans receivable:

	December 31, 2016					
	Current	30–59 Days Past Due	60–89 Days Past Due	Loans Past Due 90 Days or More	Total Past Due	Total
Residential real estate	$ 53,529	$ 975	$ 630	$ 1,204	$ 2,809	$ 56,338
Commercial real estate	37,284	24	-	-	24	37,308
Agricultural real estate	38,345	-	-	10	10	38,355
Commercial construction real estate	6,382	29	-	-	29	6,411
Residential construction real estate	1,668	-	-	-	-	1,668
Home equity, home improvement and second mortgages	29,949	460	17	233	710	30,659
Commercial operating and term	10,409	13	-	248	261	10,670
Agricultural operating and term	10,318	-	-	-	-	10,318
Vehicle	2,174	23	7	5	35	2,209
Consumer	5,126	29	43	10	82	5,208
Total loans	$ 195,184	$ 1,553	$ 697	$ 1,710	$ 3,960	$ 199,144
Nonperforming loans	$ -	$ -	$ -	$ 1,710	$ 1,710	$ 1,710

	December 31, 2015					
	Current	30–59 Days Past Due	60–89 Days Past Due	Loans Past Due 90 Days or More	Total Past Due	Total
Residential real estate	$ 57,608	$ 857	$ 194	$ 1,502	$ 2,553	$ 60,161
Commercial real estate	32,935	-	-	-	-	32,935
Agricultural real estate	38,884	-	-	387	387	39,271
Commercial construction real estate	2,264	-	-	-	-	2,264
Residential construction real estate	1,370	-	-	-	-	1,370
Home equity, home improvement and second mortgages	31,892	597	79	77	753	32,645
Commercial operating and term	9,061	154	36	71	261	9,322
Agricultural operating and term	12,860	7	-	-	7	12,867
Vehicle	2,591	12	3	16	31	2,622
Consumer	6,304	16	-	8	24	6,328
Total loans	$ 195,769	$ 1,643	$ 312	$ 2,061	$ 4,016	$ 199,785
Nonperforming loans	$ -	$ -	$ -	$ 2,061	$ 2,061	$ 2,061

(Dollars in Thousands, Except Per Share Data)

Note 4. Loans Receivable and Loans Held for Sale (Continued)

Recorded investment in nonaccrual loans and loans past due 90 days or more and still accruing by class of loans as of December 31, 2016 and 2015, were as follows:

	December 31, 2016	
	Nonaccrual	Loans Past Due 90 Days or More and Still Accruing
Residential real estate	$ 1,204	$ -
Agricultural real estate	10	-
Home equity, home improvement and second mortgages	233	-
Commercial operating and term	248	-
Vehicle	5	-
Consumer	10	-
Total	$ 1,710	$ -

	December 31, 2015	
	Nonaccrual	Loans Past Due 90 Days or More and Still Accruing
Residential real estate	$ 1,502	$ -
Agricultural real estate	387	-
Home equity, home improvement and second mortgages	77	-
Commercial operating and term	71	-
Vehicle	16	-
Consumer	8	-
Total	$ 2,061	$ -

(Dollars in Thousands, Except Per Share Data)

Note 4. Loans Receivable and Loans Held for Sale (Continued)

No interest income was recognized on nonaccrual loans for the years ended December 31, 2016 and 2015.

The Company utilizes an internal asset classification system as a means of reporting problem and potential problem loans. Under the Company's risk-rating system, the Company classifies problem and potential problem loans as "Special Mention," "Substandard" and "Doubtful," which correspond to risk ratings five, six and seven, respectively. Substandard loans include those characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Loans classified as Doubtful, or risk-rated seven, have all the weaknesses inherent in those classified as Substandard, with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. Loans that do not currently expose the Company to sufficient risk to warrant classification in one of the aforementioned categories, but possess weaknesses that deserve management's close attention, are deemed to be Special Mention, or risk-rated five. Risk ratings are updated any time the situation warrants.

Loans not meeting the criteria above that are analyzed individually as part of the above-described process are considered to be pass-rated loans. Loans listed as not rated are included in groups of homogeneous loans with similar risk and loss characteristics. The following tables present the risk category of loans by class of loans based on the most recent analyses performed and the contractual aging as of December 31, 2016 and 2015:

	December 31, 2016				
	Pass	Special Mention	Substandard	Doubtful	Total
Commercial real estate	$ 35,853	$ 857	$ 598	$ -	$ 37,308
Agricultural real estate	37,981	374	-		38,355
Commercial construction real estate	5,263	575	573	-	6,411
Commercial operating and term	9,868	627	175	-	10,670
Agricultural operating and term	10,172	146		-	10,318
Total	$ 99,137	$ 2,579	$ 1,346	$ -	$ 103,062

	December 31, 2015				
	Pass	Special Mention	Substandard	Doubtful	Total
Commercial real estate	$ 29,952	$ 1,558	$ 1,425	$ -	$ 32,935
Agricultural real estate	38,913	358	-	-	39,271
Commercial construction real estate	2,264	-	-	-	2,264
Commercial operating and term	9,221	57	44	-	9,322
Agricultural operating and term	12,867	-	-	-	12,867
Total	$ 93,217	$ 1,973	$ 1,469	$ -	$ 96,659

(Dollars in Thousands, Except Per Share Data)

Note 4. Loans Receivable and Loans Held for Sale (Continued)

For consumer, residential real estate, agricultural real estate, home equity, vehicle and residential construction loan classes, the Company collectively evaluates loans for impairment. The Company evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. Loans where credit quality and aging indicate potential weakness are placed on nonaccrual and are deemed to be nonperforming.

Impaired loans also include loans modified in a troubled debt restructuring where concessions have been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in interest rate on the loan, payment extensions, forgiveness of principal, forbearance or other actions intended to maximize collections. The following tables present troubled debt restructurings by class of loans for the years ended December 31, 2016 and 2015:

	Year Ended December 31, 2016		
	Number of Contracts	Premodification Outstanding Recorded Investment	Postmodification Outstanding Recorded Investment
Total debt restructuring:			
Residential real estate	2	$ 66	$ 66
Modified payment terms			

	Year Ended December 31, 2015		
	Number of Contracts	Premodification Outstanding Recorded Investment	Postmodification Outstanding Recorded Investment
Total debt restructuring:			
Residential real estate	3	$ 368	$ 368
Modified payment terms and interest rates			

There were no loans modified in a troubled debt restructuring that subsequently defaulted for the years ended December 31, 2016 and 2015.

(Dollars in Thousands, Except Per Share Data)

Note 4. Loans Receivable and Loans Held for Sale (Continued)

Loans individually evaluated for impairment by class of loans as of December 31, 2016 and 2015, are as follows:

	December 31, 2016				
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Residential real estate	$ 1,068	$ 1,068	$ -	$ 1,129	$ 48
Commercial real estate	575	575	-	575	19
Agricultural real estate	374	374	-	381	19
Home equity, home improvement and second mortgages	342	342	-	363	23
Commercial operating and term	55	55	-	59	2
Vehicle and Consumer	46	46	-	52	4
With an allowance recorded:					
Residential real estate	500	500	103	524	17
Commercial real estate	1,113	1,113	32	1,516	61
Commercial construction real estate	573	573	93	594	21
Home equity, home improvement and second mortgages	27	27	27	29	2
Commercial operating and term	53	53	26	56	2
Vehicle and Consumer	1	1	1	2	1
Total	$ 4,727	$ 4,727	$ 282	$ 5,280	$ 218

	December 31, 2015				
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Residential real estate	$ 463	$ 463	$ -	$ 491	$ 24
Commercial real estate	575	575	-	648	21
With an allowance recorded:					
Residential real estate	499	499	86	534	36
Commercial real estate	1,531	1,531	287	1,551	57
Home equity, home improvement and second mortgages	31	31	31	32	2
Commercial operating and term	54	54	27	67	3
Vehicle and Consumer	11	11	9	9	-
Total	$ 3,164	$ 3,164	$ 440	$ 3,332	$ 143

(Dollars in Thousands, Except Per Share Data)

Note 4. Loans Receivable and Loans Held for Sale (Continued)

Allowance for loan losses:

	Year Ended December 31, 2016				
	Balance, Beginning	Charge-offs	Recoveries	Provision	Balance, Ending
Residential real estate	$ 457	$ (146)	$ 13	$ (23)	$ 301
Commercial real estate	559	-	-	(102)	457
Agricultural real estate	198	-	-	115	313
Commercial construction real estate	12	-	-	104	116
Residential construction real estate	7	-	-	23	30
Home equity, home improvement and second mortgages	394	(92)	60	(44)	318
Commercial operating and term	201	(6)	6	(31)	170
Agricultural operating and term	59	-	-	65	124
Vehicle	26	(4)	1	(1)	22
Consumer	75	(17)	64	(66)	56
Total	$ 1,988	$ (265)	$ 144	$ 40	$ 1,907

	Year Ended December 31, 2015				
	Balance, Beginning	Charge-offs	Recoveries	Provision	Balance, Ending
Residential real estate	$ 545	$ -	$ -	$ (88)	$ 457
Commercial real estate	722	-	-	(163)	559
Agricultural real estate	155	-	-	43	198
Commercial construction real estate	12	-	-	-	12
Residential construction real estate	13	-	-	(6)	7
Home equity, home improvement and second mortgages	431	(125)	22	66	394
Commercial operating and term	109	(159)	-	251	201
Agricultural operating and term	31	-	-	28	59
Vehicle	28	-	4	(6)	26
Consumer	112	(81)	99	(55)	75
Total	$ 2,158	$ (365)	$ 125	$ 70	$ 1,988

(Dollars in Thousands, Except Per Share Data)

Note 4. Loans Receivable and Loans Held for Sale (Continued)

The allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of December 31, 2016 and 2015, are as follows:

	December 31, 2016		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Allowance for loan losses:			
Residential real estate	$ 103	$ 198	$ 301
Commercial real estate	32	425	457
Agricultural real estate	-	313	313
Commercial construction real estate	93	23	116
Residential construction real estate	-	30	30
Home equity, home improvement/second mortgages	27	291	318
Commercial operating and term	26	144	170
Agricultural operating and term	-	124	124
Vehicle	1	22	22
Consumer	-	56	56
Total	$ 282	$ 1,626	$ 1,907

	December 31, 2016		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Loans:			
Residential real estate	$ 1,568	$ 54,770	$ 56,338
Commercial real estate	1,688	35,620	37,308
Agricultural real estate	374	37,981	38,355
Commercial construction real estate	573	5,838	6,411
Residential construction real estate	-	1,668	1,668
Home equity, home improvement/second mortgages	369	30,290	30,659
Commercial operating and term	108	10,562	10,670
Agricultural operating and term	-	10,318	10,318
Vehicle	1	2,208	2,209
Consumer	46	5,162	5,208
Total	$ 4,727	$ 194,417	$ 199,144

(Dollars in Thousands, Except Per Share Data)

Note 4. Loans Receivable and Loans Held for Sale (Continued)

	December 31, 2015		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Allowance for loan losses:			
Residential real estate	$ 86	$ 371	$ 457
Commercial real estate	287	272	559
Agricultural real estate	-	198	198
Commercial construction real estate	-	12	12
Residential construction real estate	-	7	7
Home equity, home improvement/second mortgages	31	363	394
Commercial operating and term	27	174	201
Agricultural operating and term	-	59	59
Vehicle	2	24	26
Consumer	7	68	75
Total	$ 440	$ 1,548	$ 1,988

	December 31, 2015		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Loans:			
Residential real estate	$ 962	$ 59,199	$ 60,161
Commercial real estate	2,106	30,829	32,935
Agricultural real estate	-	39,271	39,271
Commercial construction real estate	-	2,264	2,264
Residential construction real estate	-	1,370	1,370
Home equity, home improvement/second mortgages	-	32,645	32,645
Commercial operating and term	31	9,291	9,322
Agricultural operating and term	54	12,813	12,867
Vehicle	2	2,620	2,622
Consumer	9	6,319	6,328
Total	$ 3,164	$ 196,621	$ 199,785

Loans with a carrying value of $109,561 and $102,138 at December 31, 2016 and 2015, respectively, were pledged to secure borrowed funds.

(Dollars in Thousands, Except Per Share Data)

Note 4. Loans Receivable and Loans Held for Sale (Continued)

Related-party loans: The Company has entered into transactions with its executive officers, directors, significant shareholders, and their affiliates (related parties). The aggregate amounts of loans to such related parties at December 31, 2016 and 2015, were $214 and $204, respectively. During 2016 and 2015, new loans to such related parties were $78 and $116, respectively, repayments were $66 and $157, respectively. Related party loans were reduced by $97 in 2015 because of officer and director retirements, while there were no officer and director retirements that impacted these loans in 2016. In the opinion of management, these loans have terms similar to other customer loans and do not present more than normal risk of collection.

Loans held for sale: As of December 31, 2016 and 2015, the Company's loans held for sale were $1,338 and $1,337, respectively, and consisted of one- to four-family residential real estate loans.

Interest rate lock commitments related to the origination of mortgage loans that will be sold are considered derivative instruments. The Company estimates the fair value of these derivatives using the difference between the guaranteed interest rate in the commitments and the current market interest rate. To reduce the net interest rate exposure arising from its loan sale activity, the Company enters into a commitment to sell these loans at the same time that the interest rate lock commitment is quoted. The commitments to sell loans are also considered derivative instruments, with offsetting estimated fair values based on changes in current market rates. These commitments are not designated as hedging instruments and, therefore, changes in fair value are recognized immediately into income. The fair values of the Company's derivative instruments are offsetting and deemed to be immaterial. The net gain on the derivative instruments was $453 and $348 in 2016 and 2015, respectively, and is included in the caption, gain on sale of loans held for sale, in the consolidated statements of income.

Note 5. Loan Servicing

Mortgage loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balances of these loans as of December 31, 2016 and 2015, were $297,700 and $317,047, respectively, and consist of one- to four-family residential real estate loans. These loans are serviced primarily for the Federal Home Loan Mortgage Corporation, Federal Home Loan Bank and Federal National Mortgage Association.

Custodial escrow balances maintained in connection with the foregoing loan servicing, and included in advances from borrowers for taxes and insurance, were $2,328 and $2,310 at December 31, 2016 and 2015, respectively.

Mortgage servicing rights are summarized as follows for the years ended December 31, 2016 and 2015:

	2016	2015
Balance at beginning of year, net	$ 1,863	$ 1,886
Mortgage servicing rights capitalized	281	343
Amortization expense	(357)	(351)
Valuation provision	-	(15)
Balance at end of year, net	$ 1,787	$ 1,863

(Dollars in Thousands, Except Per Share Data)

Note 5. Loan Servicing (Continued)

The estimated fair value of mortgage servicing rights was $2,174 and $2,293 at December 31, 2016 and 2015, respectively. At December 31, 2016 and 2015, the valuation allowance was $20 and $50, respectively.

The following table indicates the estimated future amortization expense for mortgage servicing rights. The estimated amortization expense is based on existing asset balances. The timing of amortization expense actually recognized in future periods may differ significantly depending upon prepayment speeds affected by economic conditions, mortgage interest rates, and other matters.

Years Ending December 31,		
2017	$	344
2018		309
2019		276
2020		244
2021		199
Thereafter		415
	$	1,787

Note 6. Premises and Equipment

	December 31			
	2016		2015	
Land	$	615	$	515
Buildings and improvements		5,296		4,931
Leasehold improvements		303		473
Furniture, fixtures and equipment		2,794		3,059
		9,008		8,978
Less accumulated depreciation and amortization		5,259		5,610
	$	3,749	$	3,368

(Dollars in Thousands, Except Per Share Data)

Note 7. Foreclosed Real Estate

An analysis of activity for foreclosed real estate is as follows:

	Years Ended December 31	
	2016	2015
Balance at beginning of year	$ 1,632	$ 3,656
Transfers from loans	144	262
Proceeds from sales	(51)	(1,931)
New loans from sale	(6)	(118)
Charge-offs/write-downs	(10)	(241)
Net gain on sales	-	4
Balance at end of year	$ 1,709	$ 1,632

Expenses applicable to foreclosed real estate include the following amounts reported in other real estate owned expense:

	Years Ended December 31	
	2016	2015
Net gain on sales	$ -	$ (4)
Impairment	10	241
Operating expenses, net of rental income	71	244
	$ 81	$ 481

Note 8. Deposits

	December 31	
	2016	2015
Demand deposits, noninterest-bearing	$ 21,311	$ 21,084
NOW and money market accounts	104,320	105,962
Savings accounts	54,571	50,892
Certificates of deposit	52,808	62,012
	$233,010	$ 239,950

The aggregate amount of certificates of deposit over $100 was $12,044 and $15,243 at December 31, 2016 and 2015, respectively. The aggregate amount of certificates of deposit over $250 was $533 and $1,053 at December 31, 2016 and 2015, respectively.

(Dollars in Thousands, Except Per Share Data)

Note 8. Deposits (Continued)

A summary of scheduled maturities of certificates of deposit is as follows:

Years Ending December 31,	
2017	$ 36,206
2018	8,313
2019	6,667
2020	1,556
2021	66
	$ 52,808

Note 9. Borrowed Funds

The Company has no outstanding advances from the FHLB of Des Moines as of December 31, 2016 and 2015. The maximum borrowing capacity, based on securities and loans pledged, from the FHLB of Des Moines was $76,601 as of December 31, 2016.

Note 10. Income Tax Matters

The components of income tax expense are as follows:

	Years Ended December 31	
	2016	2015
Federal:		
Current	$ 940	$ 734
Deferred	22	190
	962	924
State:		
Current	350	257
Deferred	9	63
	359	320
Total	$ 1,321	$ 1,244

(Dollars in Thousands, Except Per Share Data)

Note 10. Income Tax Matters (Continued)

Total income tax expense differed from the amounts computed by applying the statutory U.S. federal income tax rate (35 percent) to income before income taxes as a result of the following:

	Years Ended December 31	
	2016	2015
Computed expected tax expense	$ 1,298	$ 2,148
State income taxes, net of federal benefit	233	208
Bargain purchase gain	-	(997)
Effect of graduated rates	(37)	(61)
Tax exempt income	(92)	(79)
Other	(81)	25
Income tax expense	$1,321	$ 1,244

The Company utilizes a two-step process to recognize and measure uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount that is more than 50 percent likely of being realized upon ultimate settlement. The Company and its subsidiary file consolidated federal and state income tax returns. At December 31, 2016, the federal and Minnesota tax returns that the Company files are open for examination by taxing authorities for the years 2013, 2014 and 2015. The Company considers many factors when evaluating and estimating the Company's tax positions, which may require periodic adjustments. At December 31, 2016, the Company did not record any liabilities for uncertain tax positions.

The Company recognizes accrued penalty and interest on uncertain tax positions, if any, as a component of its income tax expense.

(Dollars in Thousands, Except Per Share Data)

Note 10. Income Tax Matters (Continued)

The net deferred tax assets (liabilities) included in the accompanying consolidated balance sheets in other assets includes the following:

	December 31	
	2016	2015
Deferred tax assets:		
Allowance for loan losses	$ 772	$ 795
Management stock bonus plan	4	6
Accrued compensation	8	29
Impairment of securities	196	196
Repossessed property	307	297
Unaccreted discount	23	35
Accrual to cash	-	14
Securities available for sale	4	-
Other	160	177
Total deferred tax assets	1,474	1,549
Deferred tax liabilities:		
Premises and equipment	216	224
FHLB stock	131	130
Mortgage servicing rights	723	745
Deferred loan origination fees	21	25
Securities available for sale	-	39
Prepaid expenses	52	52
Accrued real estate taxes	51	41
Other	197	222
Total deferred tax liabilities	1,391	1,478
Net deferred tax assets	$ 83	$ 71

Retained earnings include approximately $2,211 related to the pre-1987 allowance for loan losses for which no deferred federal income tax liability has been recognized. This amount represents an allocation of income to bad-debt deductions for tax purposes only. If the Bank no longer qualifies as a bank or in the event of a liquidation of the Bank, income would be created for tax purposes only, which would be subject to the then-current corporate income tax rate. The unrecorded deferred income tax liability on the above amount for financial statement purposes was approximately $884.

(Dollars in Thousands, Except Per Share Data)

Note 11. Equity, Regulatory Capital and Dividend Restrictions

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. 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 Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of total Tier I capital and common equity Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 2016, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2016, the most recent notification of the Federal Deposit Insurance Corporation categorized the Bank as "well capitalized" under the regulatory framework for Prompt Corrective Action. To be categorized as "well capitalized," the Bank must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios. There are no conditions or events since that notification that management believes have changed the Bank's category.

The following table summarizes the Bank's compliance with its regulatory capital requirements:

	Actual		Minimum for Capital Adequacy Purposes		Minimum to be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Percent	Amount	Percent	Amount	Percent
As of December 31, 2016:						
Tier I capital						
(to average assets)	$ 27,167	10.28%	$ 10,567	4.00%	$ 13,208	5.00%
Common equity Tier I capital						
(to risk weighted assets)	27,167	13.61%	8,980	4.50%	12,972	6.50%
Tier I capital						
(to risk weighted assets)	27,167	13.61%	11,974	6.00%	15,965	8.00%
Total risk based capital						
(to risk weighted assets)	29,194	14.63%	15,965	8.00%	19,956	10.00%
As of December 31, 2015:						
Tier I capital						
(to average assets)	$ 28,734	10.48%	$ 10,967	4.00%	$ 13,709	5.00%
Common equity Tier I capital						
(to risk weighted assets)	28,734	14.56%	8,884	4.50%	12,832	6.50%
Tier I capital						
(to risk weighted assets)	28,734	14.56%	11,845	6.00%	15,793	8.00%
Total risk based capital						
(to risk weighted assets)	30,722	15.56%	15,793	8.00%	19,742	10.00%

Note 11. Equity, Regulatory Capital and Dividend Restrictions (Continued)

In July 2013, the federal banking agencies issued a final rule revising the regulatory capital rules applicable to most national bank and federal savings associations as well as their holding companies generally beginning on January 1, 2015. The rule implements the Basel Committee's December 2010 framework known as "Basel Ill" for strengthening international capital standards as well as certain provisions of the Dodd-Frank Act. The final rule implements a revised definition of regulatory capital, a new common equity Tier 1 minimum capital requirement of 4.50%, and a higher minimum Tier 1 capital requirement of 6.00% (which is an increase from 4.00%). Under the final rule, the total capital ratio remains at 8.00% and the minimum leverage ratio (Tier 1 capital to total assets) for all banking organizations, regardless of supervisory rating, is 4.00%.

Additionally, under the final rule, in order to avoid limitations on capital distributions, including dividend payments and certain discretionary bonus payments to executive officers, a banking organization must hold a 2.5% capital conservation buffer composed of common equity Tier 1 capital above its minimum risk-based capital requirements. The buffer is measured relative to risk-weighted assets. The final rule also enhances risk sensitivity and addresses weaknesses identified by the regulators over recent years with the measure of risk weighted assets, including through new measures of creditworthiness to replace references to credit ratings, consistent with the requirements of the Dodd-Frank Act.

Except for the largest internationally active banking organizations (which are subject to the "advanced approaches" provisions of the final rule), the new minimum capital requirements generally become effective for all banking organizations on January 1, 2015, whereas the capital conservation buffer and the deductions from common equity Tier 1 capital phase in over time, beginning on January 1, 2016 and through January 1, 2019. Similarly, non-qualifying capital instruments phase out over time.

(Dollars in Thousands, Except Per Share Data)

Note 12. Earnings Per Share

A reconciliation of the income and common stock share amounts used in the calculation of basic and diluted earnings per share follows:

	Year Ended December 31, 2016		
	Income	Weighted-average Shares	Per Share Amount
Basic earnings per share:			
Net income	$ 2,387	784,653	$3.04
Effect of dilutive securities:			
Stock options	-	576	
Diluted earnings per share:			
Net income plus assumed conversions	$ 2,387	785,230	$3.04

	Year Ended December 31, 2015		
	Income	Weighted-average Shares	Per Share Amount
Basic earnings per share:			
Net income	$ 4,894	770,569	$ 6.35
Effect of dilutive securities:			
Stock options	-	629	
Diluted earnings per share:			
Net income plus assumed conversions	$ 4,894	771,198	$ 6.35

Note 13. Employee Benefit Plans

Defined contribution 401(k) plan: The Company provides a 401(k) plan that covers substantially all of the Bank's employees who are eligible as to age and length of service. A participant may elect to make contributions of up to 15 percent of the participant's annual compensation. At the discretion of the Board of Directors, the Bank may make matching and other contributions to the plan. Discretionary matching contributions of $90 and $80 (up to 3 percent of participant annual compensation) were made for the years ended December 31, 2016 and 2015, respectively.

Employee stock ownership plan: An employee stock ownership plan (ESOP) was adopted in 1995, covering all full-time employees of the Company who have attained age 21 and completed one year of service during which they worked at least 1,500 hours.

The Company makes annual discretionary contributions to the ESOP. As these funds are available, the ESOP acquires shares of Company stock and allocates the shares to ESOP participants. Dividends on allocated ESOP shares are recorded as a reduction of retained earnings. In 2016 no shares were purchased for ESOP participants. In 2015 6,299 shares were purchased, and 2,342 and 2,505 shares, respectively, were allocated to ESOP participants at a cost of approximately $64 and $64 for 2016 and 2015, respectively, which was charged to compensation expense.

The ESOP held 87,264 and 91,459 shares of Company stock at December 31, 2016 and 2015, respectively. At December 31, 2016 and 2015, 84,282 and 86,135 shares, respectively, have been released for allocation to participants. Allocated shares held by the ESOP are treated as outstanding in computing earnings per share.

Stock option plans:

Wells Financial Corp. 2003 Stock Option Plan: In 2003 the Company approved the Wells Financial Corp. 2003 Stock Option Plan (the Plan). Pursuant to the Plan, stock options for 120,000 common shares may be granted to officers, directors, employees and other persons providing services to the Company. The Plan options have a maximum term of 10 years and are granted with an exercise price equal to the market price on the grant date. Awards to nonemployee directors are exercisable on the grant date. Awards to employees are generally exercisable on the grant date subject to employment conditions.

Options granted under the Plan may be options that qualify as Incentive Stock Options, as defined in Section 422 of the Internal Revenue Code of 1986, as amended, or options that do not so qualify.

(Dollars in Thousands, Except Per Share Data)

Note 13. Employee Benefit Plans (Continued)

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. Grant-date fair values were computed using the following assumptions: estimated life (in years), risk-free interest rate, expected volatility and dividend rate. The expected volatility is based on historical volatility for the estimated term of the award. The risk-free interest rates for periods within the contractual life of the awards are based on the U.S. Treasury yield curve in effect at the time of the grant. The expected life is based on historical exercise experience. The dividend yield assumption is based on the Company's history and expectation of dividend payouts.

Stock option activity and balances as of December 31, 2016 and 2015, and during the years then ended are presented below:

	Years Ended December 31				
	2016			2015	
Fixed Options	Aggregate Intrinsic Value	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding, beginning of year	$ 33	9,050	$ 28.32	16,950	$ 29.10
Granted		-	-	-	-
Exercised		(3,600)	26.39	-	-
Forfeited		(3,850)	29.60	(7,900)	30.00
Outstanding, end of year	$ 15	1,600	$ 29.60	9,050	$ 28.32

The aggregate intrinsic value of a stock option in the table above represents the total pretax intrinsic value (the amount by which the current market value of the underlying stock exceeds the exercise price of the option) that would have been received by the option holders, had all option holders exercised their options on December 31, 2016. The intrinsic value changes based on changes in the market value of the Company's stock. The total intrinsic value of options exercised during 2016 was $14. The Company has purchased treasury stock and uses these shares for options exercised.

The status of the 1,600 options outstanding at December 31, 2016, is presented below:

Date of Award	Shares	Exercise Price Per Share	Remaining Contractual Life (Years)	Number Exercisable	Exercisable Intrinsic Value
March 20, 2007	7,950	$ 29.60	0.2	1,600	$ 15

For the years ended December 31, 2016 and 2015, the Company did not recognize any compensation expense related to awards issued under this plan.

(Dollars in Thousands, Except Per Share Data)

Note 13. Employee Benefit Plans (Continued)

Management stock bonus plan: The Company adopted the Wells Federal Bank 2003 Stock Bonus Plan in 2003 (the 2003 Plan). The Company authorized nonvested stock awards of up to 50,000 shares to directors, officers and employees of the Company. These awards vest at the rate of 25 percent per year of continuous service with the Company. There are 17,425 shares available to be issued under the 2003 Plan at December 31, 2016 and 2015.

The status of nonvested shares outstanding as of December 31, 2016 and 2015, and the changes during the years then ended are presented below:

	Years Ended December 31	
	2016	2015
Outstanding at beginning of year	1,237	1,781
Granted	-	-
Forfeited	-	-
Vested	(544)	(544)
Outstanding at end of year	693	1,237

The total fair value of shares vested during the years ended December 31, 2016 and 2015, was $9 and $18, respectively. The Company recorded compensation expense of $7 and $13 related to this plan for the years ended December 31, 2016 and 2015, respectively. At December 31, 2016, there was a total of $3 of unrecognized compensation expense related to stock-based compensation arrangements granted under this plan. The expense expected to be recognized is $3 in 2017. The total tax benefit recognized in the consolidated financial statements for the years ended December 31, 2016 and 2015, related to shares granted under the plan was $4 and $11, respectively. The total tax benefit realized on the tax returns for years ended December 31, 2016 and 2015, was $4 and $17, respectively.

Note 14. Commitments and Contingencies

The Company leases certain branch facilities under operating leases. Some leases require the Company to pay related insurance, maintenance and repairs, and real estate taxes. The Company also has an agreement with its data processor whereby the processor agrees to provide certain data and item processing services that expire in 2020. The agreement automatically renews in five-year intervals unless terminated by either party. Future minimum rental and data processing commitments under these agreements as of December 31, 2016, are estimated as follows:

Years Ending December 31,	Rental	Data Processing
2017	$ 45	$ 551
2018	-	521
2019	-	521
2020	-	130

Note 14. Commitments and Contingencies (Continued)

Total rental expense related to operating leases was approximately $115 and $159 for the years ended December 31, 2016 and 2015, respectively. Total data processing expense related to servicing agreements was $1,027 and $985 for the years ended December 31, 2016 and 2015, respectively.

In the normal course of business, the Company may be involved in various legal proceedings. In the opinion of management, any liability resulting from such proceedings would not have a material adverse effect on the consolidated financial statements.

Note 15. Financial Instruments With Off-Balance-Sheet Risk

The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include primarily commitments to extend credit. Those instruments involve, to varying degrees, elements of credit risk and interest rate risk in excess of the amount recognized in the consolidated balance sheet.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit, standby letters of credit, and financial guarantees written is represented by the contractual notional amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Commitments to extend credit on loans totaled approximately $43,815 and $44,081 at December 31, 2016 and 2015, respectively.

Commitments to extend credit are agreements to lend to a customer 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. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if it is deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but normally includes real estate and personal property.

Note 16. Business Combination

Effective July 16, 2015, the Company completed its acquisition of St. James Federal Savings and Loan Association, St. James, Minnesota (St. James), in a conversion merger transaction. As a result of the conversion merger transaction, St. James converted from a mutual to stock institution and merged with and into the Bank, with the Bank as the surviving institution. The Company acquired 100% of the voting shares of St. James. The Company issued and sold 78,736 shares of common stock at a price of $27.36 per share, which reflected a 5% discount on the 30 day average price as prescribed in the merger agreement. The shares were offered to depositor and borrower members of St. James in a subscription offering and to stockholders of the Company and members of the general public in a community offering. The Company's ESOP acquired 8%, or 6,299 shares, of the newly issued shares using funds borrowed from the Company. The fair value of consideration paid to the prior depositors and borrowers of St. James was determined to approximate zero. Gross offering proceeds totaled approximately $2,154, including $172 purchased by the Company's ESOP. As a result of the stock offering, the Company had 814,758 shares of common stock outstanding as of the close of business on July 16, 2015. St. James' sole office, located in St. James, Minnesota, has become a branch office of the Bank. The Company's primary reasons for the acquisition are to provide for asset growth, improve capital and competitive positions, and increase the limit on loans to one borrower.

(Dollars in Thousands, Except Per Share Data)

Note 16. Business Combination (continued)

The Company has determined that the acquisition constitutes a business combination as defined by the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 805, *Business Combinations.* Accordingly, the assets acquired and liabilities assumed are presented at their estimated fair values as required by the guidance. Fair values were determined based on the requirements of ASC Topic 820, *Fair Value Measurements.*

The determination of these fair values required management to make estimates about discount rates, future expected cash flows, market conditions and other future events which are highly subjective in nature. The assets acquired and liabilities assumed in the transaction are presented at estimated fair value on the acquisition date.

The Company recorded the following assets and liabilities as of July 16, 2015. The discounts and premiums resulting from the fair value adjustments will be accreted or amortized over the anticipated lives of the underlying assets and liabilities. The excess fair value of assets acquired over liabilities assumed, resulted in a $2,848 bargain purchase gain. The merger resulted in a gain because of the legal and financial barriers that St. James would have incurred to convert to a stock form of ownership in a stand-alone transaction, including the related transaction costs associated with a conversion and stock issuance. The bargain purchase gain was recorded in non-interest income in the Company's consolidated statements of income for the year ended December 31, 2015.

	July 16, 2015
Recognized amounts of identifiable assets acquired and liabilities assumed	
Fair value of assets acquired	
Cash	$ 1,337
Certificates of deposit	5,616
Securities – available for sale	995
Loans	17,506
Premises and equipment	366
Real estate owned	35
Accrued interest and other assets	131
Core deposit intangible	208
Total assets acquired	$ 26,194
Fair value of liabilities assumed	
Deposits	$ 23,043
Deferred tax liability	238
Accrued interest and other liabilities	65
Total liabilities assumed	$ 23,346
Net assets acquired	$ 2,848

(Dollars in Thousands, Except Per Share Data)

Note 16. Business Combination (continued)

The fair value of the loan portfolio was estimated by performing a discounted cash flow analysis. The valuation was performed at the loan level on real estate loans and at the cohort level for all other loan types, and is based on the objective attributes of the loans in the portfolio (e.g., the rate of interest on the loan, the original term of the loan, the current term of the loan, etc.) and current statistical performance variables used in the market place. The analysis was based on the contractually specified amounts of principal and interest to be received modified by our estimates of prepayment, default and loss severity to be experienced prospectively. The prepayment, default and loss severity assumptions were applied at the loan level based on the characteristics of the loan.

The composition of the acquired loans at July 16, 2015 was as follows:

	Contractual Amount	Fair Value Adjustments	Fair Value
Residential real estate	$ 6,480	$ 74	$ 6,554
Revolving, open end residential real estate	336	(1)	335
Agricultural real estate	5,437	57	5,494
Agricultural operating and term	2,588	2	2,590
Commercial real estate	1,262	2	1,264
Automobile loans	721	(8)	713
Other consumer	602	(46)	556
Total	$ 17,426	$ 80	$ 17,506

The Company estimated that $79 of the contractual amounts receivable for loans acquired will not be collected.

The following table presents pro forma financial information assuming the acquisition occurred prior to 2015:

Year ended December 31,	2015
Revenues (interest and noninterest income)	$ 13,815
Net income	2,081
Diluted net income per share	2.43
Diluted weighted-average shares	2.43

To determine pro forma information, the Company adjusted its 2015 historical results to include the historical results of St. James.

Stock issuance costs incurred totaled $1,147. The stock issuance costs were offset against the proceeds of the offering, which was recognized as paid-in capital.

Merger costs of $332 were expensed during the year ended December 31, 2015.

Note 17. Concentrations

Concentration by geographic location: The Company makes agricultural, commercial, residential and consumer loans to customers primarily in south central Minnesota and northern Iowa. Although the Company's loan portfolio is diversified, there is a relationship in this region between the agricultural economy and the economic performance of loans made to nonagricultural customers. The Company's lending policies for agricultural and nonagricultural customers require loans to be well-collateralized and supported by cash flows. Collateral for agricultural loans includes equipment, crops, livestock and land. Credit losses from loans related to the agricultural economy are consistent with credit losses experienced in the portfolio as a whole. The concentration of credit in the regional agricultural economy is taken into consideration by management in determining the allowance for loan losses.

Concentration by institution: The nature of the Company's business requires that it maintain amounts due from banks that, at times, may exceed federally insured limits. The Company has not experienced any losses in such amounts. At December 31, 2016 and 2015, the Company had $9,156 and $13,582 respectively, on deposit with United Bankers Bank, which is included in cash and cash equivalents and federal funds sold on the consolidated balance sheets. The Company has evaluated its customers and has not identified any major customers as defined by generally accepted accounting principles.

Note 18. Fair Value Measurements

ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

ASC Topic 820 establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date

Level 2: Significant other observable inputs other than Level 1 prices, such as 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

Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

Note 18. Fair Value Measurements (Continued)

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. While management believes the Company's valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Investment securities available for sale: The fair values of exchange-listed equity securities are based on quoted market prices and are categorized as Level 1 of the fair value hierarchy. The fair values of debt securities were generally determined based on matrix pricing. Matrix pricing is a mathematical technique that utilizes observable market inputs including, for example, yield curves, credit ratings and prepayment speeds. Fair values determined using matrix pricing are categorized as Level 2 in the fair value hierarchy.

The Company is required, on a nonrecurring basis, to adjust the carrying value of certain assets or provide valuation allowances related to certain assets, using fair value measurements in accordance with generally accepted accounting principles.

Impaired loans: The specific reserves for collateral-dependent impaired loans are based on the fair value of the collateral less estimated costs to sell. The fair value of collateral was determined based on appraisals, with further adjustments made to the appraised values due to various factors, including the age of the appraisal, age of comparables included in the appraisal, and changes in the market and in the collateral. As these significant adjustments are based on unobservable inputs, the resulting fair value measurements have been categorized as Level 3 measurements.

Foreclosed real estate: Foreclosed real estate is recorded at fair value based on property appraisals, less estimated selling costs, at the date of transfer. The carrying value of foreclosed real estate is not remeasured to fair value on a recurring basis, but is subject to fair value adjustments when the carrying value exceeds the fair value, less estimated selling costs. Property appraisals are based on assumptions generally not observable in the marketplace, and the related nonrecurring fair value measurement adjustments have been classified as Level 3.

(Dollars in Thousands, Except Per Share Data)

Note 18. Fair Value Measurements (Continued)

Mortgage servicing rights: Mortgage servicing rights are initially measured at fair value in the Company's consolidated balance sheet. The Company utilizes the amortization method to subsequently measure its capitalized servicing assets. In accordance with ASC Topic 860, the Company must record impairment charges when the carrying value of certain strata exceeds their estimated fair value. To estimate the fair value of servicing rights, the Company computes the present value of expected future cash flows associated with the servicing rights using assumptions that market participants would use in estimating future servicing income and expense. Such assumptions include estimates of the cost of servicing loans, loan default rates, an appropriate discount rate, and prepayment speeds. For purposes of evaluating and measuring impairment of capitalized servicing rights, the Company stratifies such assets based on the predominant risk characteristics of the underlying financial instruments that are expected to have the most impact on projected prepayments, cost of servicing, and other factors affecting future cash flows associated with the servicing rights. Such factors may include financial asset or loan type, note rate and term. The amount of impairment recognized is the amount by which the carrying value of the capitalized servicing rights for a stratum exceeds estimated fair value. Impairment is recognized through a valuation allowance. The determination of fair value of capitalized servicing rights is considered a Level 2 valuation.

The following tables summarize assets and (liabilities) measured at fair value as of December 31, 2016 and 2015, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

	December 31, 2016			
	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Recurring:				
Investment securities available for sale:				
Residential mortgage-backed securities	$ -	$ 18,070	$ -	$ 18,070
SBA pools	-	3,399	-	3,399
Obligations of states and political subdivisions	-	1,954	-	1,954
Government-sponsored enterprise equity Securities	-	209	-	209
Nonrecurring:				
Foreclosed real estate	-	-	1,709	1,709
Collateral-dependent impaired loans	-	-	1,985	1,985

(Dollars in Thousands, Except Per Share Data)

Note 18. Fair Value Measurements (Continued)

	December 31, 2015			
	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Recurring:				
Investment securities available for sale:				
Residential mortgage-backed securities	$ -	$ 20,142	$ -	$ 20,142
SBA pools	-	2,574	-	2,574
Obligations of states and political subdivisions	-	11,642	-	11,642
Government-sponsored enterprise equity Securities	-	92	-	92
Nonrecurring:				
Foreclosed real estate	-	-	1,632	1,632
Collateral-dependent impaired loans	-	-	1,685	1,685

For the fiscal years ended December 31, 2016 and 2015 there were no transfers in or out of Levels 1, 2, and 3.

ASC Topic 825 requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not recognized at fair value on a recurring basis or nonrecurring basis. The methodologies for estimating the fair value of financial assets and financial liabilities that are recognized at fair value on a recurring or nonrecurring basis are discussed above. The methodologies for financial assets and financial liabilities are discussed in Note 1.

(Dollars in Thousands, Except Per Share Data)

Note 18. Fair Value Measurements (Continued)

The estimated fair values of the Company's financial instruments are as follows:

		December 31			
		2016		2015	
	Level in Fair Value Hierarchy	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:					
Cash and cash equivalents	Level 1	$ 5,777	$ 5,777	$ 12,059	$ 12,059
Certificates of deposit	Level 2	13,582	13,582	9,543	9,543
Federal funds sold	Level 2	5,900	5,900	9,100	9,100
Securities available for sale	Level 2	33,632	33,632	34,450	34,450
FHLB stock	Level 2	1,858	1,858	1,986	1,986
Loans held for sale	Level 2	1,338	1,338	1,337	1,337
Loans receivable, net	Level 2	197,086	198,566	197,595	199,971
Accrued interest receivable	Level 2	1,071	1,071	1,020	1,020
Mortgage servicing rights	Level 2	1,787	2,174	1,863	2,293
Financial liabilities:					
Deposits	Level 2	233,010	225,423	239,950	232,350
Advances from borrowers for taxes and insurance	Level 2	2,749	2,749	2,646	2,646
Accrued interest payable	Level 2	620	620	12	12

Interest rate risk: The Company assumes interest rate risk (the risk that general interest rate levels will change) as a result of its normal operations. As a result, the fair values of the Company's financial instruments will change when interest rate levels change, and that change may be either favorable or unfavorable to the Company. Management attempts to match maturities of assets and liabilities to the extent believed necessary to manage interest rate risk. However, borrowers with fixed-rate obligations are more likely to prepay in a falling-rate environment and less likely to prepay in a rising-rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising-rate environment and less likely to do so in a falling-rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by adjusting terms of new loans and deposits and by investing in securities with terms that mitigate the Company's overall interest rate risk.

The fair value of commitments to extend credit is based on fees currently charged to enter into similar agreements with comparable credit risks and the current creditworthiness of the parties. Commitments are generally short-term in nature and, if drawn upon, are issued under current market terms and conditions for credits with comparable risks. Therefore, the fair values of these financial instruments are not significant.

(Dollars in Thousands, Except Per Share Data)

Note 19. Additional Cash Flow Information

	Years Ended December 31	
	2016	2015
Cash flows from securities:		
Available-for-sale securities		
Maturities and calls	$ 9,526	$ 7,658
Sale of securities	166	-
Purchases	(9,238)	(7,283)
	$ 454	$ 375
Supplemental disclosures of cash flow information:		
Cash payments for:		
Interest	$ 347	$ 455
Income taxes	1,300	1,155
Supplemental schedule of noncash investing and financing activities:		
Loans originated in sale of foreclosed real estate	$ -	$ 118
Foreclosed real estate acquired in settlement of loans	144	262

On July 16, 2015, the Company purchased Saint James Federal Savings and Loan Association. Noncash investing and financing amounts are presented in Note 16.

(Dollars in Thousands, Except Per Share Data)

Note 20. Financial Information of Wells Financial Corp. (Parent Only)

The Company's condensed statements of financial condition as of December 31, 2016 and 2015 and related condensed statements of income and cash flows for the years then ended:

Condensed Balance Sheets

Assets	2016	2015
Cash	$ 4,774	$ 2,094
Prepaid fees and other assets	101	166
Investment in Wells Federal Bank	27,235	29,060
Total Assets	$ 32,110	$ 31,320
Liabilities and Stockholders' Equity		
Liabilities	$ 35	$ 20
Stockholders' equity	32,075	31,300
Total liabilities and stockholders' equity	$ 32,110	$ 31,320

Condensed Statements of Income

	2016	2015
Interest Income	$ 23	$ -
Compensation and benefits	(52)	(24)
Other expense	(283)	(152)
Loss before income taxes	(312)	(176)
Income tax benefit	126	58
Net loss before dividends and equity in undistributed income of subsidiary	(186)	(118)
Dividends from subsidiary	4,235	1,600
Equity in undistributed income of subsidiary	(1,662)	3,412
Net income	$ 2,387	$ 4,894

(Dollars in Thousands, Except Per Share Data)

Note 20. Financial Information of Wells Financial Corp. (Parent Only) (Continued)

Condensed Statements of Cash Flows

	2016	2015
Cash Flows From Operating Activities		
Net Income	$ 2,387	$ 4,894
Adjustments to reconcile net income to net cash provided by operating activities:		
Stock based compensation	91	26
Equity in undistributed net income of subsidiary	1,764	(3,584)
Other assets	55	52
Other liabilities	15	20
Net cash provided by operating activities	4,312	1,408
Cash Flows From Financing Activities		
Issuance of shares of common stock	-	1,007
Purchase of treasury stock	(849)	(505)
Dividends paid	(783)	(556)
Net cash used in financing activities	(1,632)	(54)
Net increase in cash	2,680	1,354
Cash and Cash Equivalents		
Beginning	2,094	740
Ending	$ 4,774	$ 2,094

Note 21. Subsequent Event

On February 2, 2017 the Bank was granted regulatory approval to pay a $3.2 million dividend to the Company. This dividend represents 25% ($1,256) of the Bank's 2015 net income and 75.0% ($1,930) of the Bank's 2016 net income. This dividend was paid on February 15, 2017. On February 14, 2017 the Company declared a $0.25 per share dividend, payable on March 17, 2017 to shareholders of record on March 3, 2017.

On March 17, 2017 the Company announced a merger with Citizens Community Bancorp, Inc. (NASDAQ: CZWI), whereby the Company will merge into Citizens Community Bancorp, Inc. in a transaction valued at approximately $39.8 million. The board of directors of both companies approved the transaction, which is subject to the approvals of bank regulatory agencies and the shareholders of the Company. Shareholders of the Company will receive total consideration of $51.00 per share, which will consist of $41.31 in cash or 81% of the total consideration and the balance of the consideration will consist of 0.7636 shares of Citizens Community Bancorp, Inc. for each share of the Company. The stock consideration is subject to a pricing collar adjustment in certain circumstances based on the price of Citizens Community Bancorp, Inc. common stock at the time of closing. It is believed that the transaction will close sometime in the third quarter of 2017.

Other Corporate Information

Wells Financial Corp. (Company) and Wells Federal Bank (Bank)
53 First Street SW, P.O. Box 310, Wells, MN 56097

The Company and the Bank are incorporated in the State of Minnesota. The Company had 778,788 of its common stock, $0.10 par value, outstanding at December 31, 2016. The Company trades on OTCQB under the symbol "WEFP". There are no broker/dealers affiliated with the Company and the quotation is not being published on behalf of the Company. The Company's transfer agent is: Computershare, 211 Quality Circle, Suite 210, College Station, TX 77845.

The Company acquired all of the capital stock that the Bank issued upon its conversion from mutual to stock form of ownership. The Company's business activities are limited to its investment in the Bank. The Bank is a State chartered commercial bank headquartered in Wells, Minnesota. The Bank has nine full service offices. The Bank owns the facilities at seven of its locations and leases the other two locations. The Bank attracts deposits from the general public and uses such deposits to invest in residential lending on owner occupied properties, commercial real estate and construction loans, agricultural real estate and operating loans, home equity and other consumer loans. The Bank had one subsidiary at December 31, 2016, Wells Insurance Agency (WIA). WIA is a full service insurance agency that sells property, casualty, life and health insurance products.

Board of Directors of Wells Financial Corp.

Randel I. Bichler, Chairman of the Board

David Buesing

Richard Mueller

Gerald D. Bastian

James D. Moll

Executive Officers of Wells Financial Corp.

James D. Moll, CPA
President and Chief Executive Officer

Patrick S. Scott
Treasurer and Principal Financial and Accounting Officer

Richard Mueller
Secretary

The Company's Annual Report for the fiscal year ended December 31, 2016 is available without charge upon written request. For a copy of the Annual Report or any other investor information, please write to the Secretary of the Company, at the Company's corporate office in Wells, Minnesota.