The

CLATSOP community bank™

2016 Annual Report

MOSS-ADAMS LLP

Certified Public Accountants | Business Consultants

February 21, 2017

Shareholders,

Clatsop Community Bank’s 2016 audited financial statements are presented for your review. This was our eighth complete year of operations and we are pleased with the Bank’s financial performance and growth. The Bank continued its track record of profitability, with positive earnings for the sixth consecutive year.

Deposits and loans grew in 2016 despite strong competition. The Bank was able to increase total deposits by $4.9 million, representing a 7.2% increase year-over-year. Similarly the Bank's loan portfolio grew by $3.4 million, or 6.8% year-over-year. Although the economy is still recovering, loan demand has not rebounded to pre-crisis levels. High quality loans are not abundant and competition for these quality credits is formidable. Despite these challenges the Bank is competing well.

The Bank possesses an experienced, talented team, which works diligently to build full customer relationships primarily throughout Clatsop County. We continue to attract customers who value the desirable combination of premium, personalized service with timely, local decision making. Moreover, our customers appreciate the fact that their deposits are put to work in their very own community.

Overall, your Bank possesses a strong capital base which provides a solid foundation for continued growth. We look forward to a prosperous 2017 and beyond. Thank you for your continued support.

Joseph Schulte	Ken Ulbricht
President & CEO	Chairperson

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Note: These financial statements have not been reviewed or confirmed for accuracy or relevance by the Federal Deposit Insurance Corporation.

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REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Shareholders
Clatsop Community Bank

Report on Financial Statements
We have audited the accompanying financial statements of Clatsop Community Bank (the Bank) which comprise the balance sheets as of December 31, 2016 and 2015, and the related statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

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

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

REPORT OF INDEPENDENT AUDITORS (continued)

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Clatsop Community Bank as of December 31, 2016 and 2015, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Moss Adams LLP

Portland, Oregon
February 24, 2017

CLATSOP COMMUNITY BANK
BALANCE SHEETS

	December 31, 2016	December 31, 2015
ASSETS		
Cash and due from banks	$ 1,558,276	$ 1,369,666
Interest bearing deposits with other banks	653,000	4,549,288
Cash and cash equivalents	2,211,276	5,918,954
Time deposits with other financial institutions	978,417	490,000
Investment securities available-for-sale, at fair value	21,952,106	14,646,854
Loans, net of allowance for loan losses and net deferred loan fees	54,178,287	50,729,426
Restricted equity securities, at cost	293,700	85,500
Premises, equipment, and leasehold improvements, net of accumulated depreciation and amortization	2,473,219	2,589,485
Other real estate owned and repossessed assets	-	30,000
Cash surrender value of bank-owned life insurance	2,127,058	2,056,860
Deferred tax asset, net	1,154,165	1,199,150
Accrued interest receivable and other assets	355,627	285,901
Total assets	$ 85,723,855	$ 78,032,130
LIABILITIES		
Noninterest-bearing demand deposits	$ 25,203,453	$ 21,746,029
Interest-bearing demand deposits, savings and money market accounts	37,939,956	34,120,389
Time certificates of deposit	9,798,533	12,199,168
Total deposits	72,941,942	68,065,586
Borrowed funds	2,500,000	-
Accrued interest payable and other liabilities	181,998	211,573
Total liabilities	75,623,940	68,277,159
COMMITMENTS AND CONTINGENCIES (Notes 10, 11 and 12)		
SHAREHOLDERS' EQUITY		
Common stock, no par value, 10,000,000 shares authorized; 1,054,660 and 1,050,160 shares issued and outstanding at December 31, 2016 and 2015, respectively	10,250,363	10,250,363
Additional paid-in capital	819,746	736,465
Accumulated deficit	(660,908)	(1,175,488)
Accumulated other comprehensive loss	(309,286)	(56,369)
Total shareholders' equity	10,099,915	9,754,971
Total liabilities and shareholders' equity	$ 85,723,855	$ 78,032,130

CLATSOP COMMUNITY BANK
STATEMENTS OF INCOME

	Years Ended December 31, 2016	2015
INTEREST INCOME		
Interest and fees on loans	$ 2,877,231	$ 2,871,813
Interest on available-for-sale securities	300,989	246,987
Interest on deposits with other banks	31,391	11,911
Total interest income	3,209,611	3,130,711
INTEREST EXPENSE		
Interest on deposits	132,642	142,181
Interest on borrowed funds	2,971	338
Total interest expense	135,613	142,519
Net interest income before provision for loan losses	3,073,998	2,988,192
PROVISION FOR LOAN LOSSES	-	-
Net interest income	3,073,998	2,988,192
NONINTEREST INCOME		
Deposit service charges	85,413	78,122
Gain on sale of securities	30,093	44,474
Gain on sale of other real estate owned and repossessed assets	4,953	11,042
Gain on sale of government guaranteed loans	84,585	105,068
Increase in cash surrender value of life insurance	70,198	71,103
Other noninterest income	1,588	880
Total noninterest income	276,830	310,689
NONINTEREST EXPENSE		
Salaries and employee benefits	1,432,570	1,348,794
Occupancy expense	194,853	179,916
Data processing	202,690	201,747
Depreciation expense	130,224	135,140
Professional fees	108,990	108,513
Advertising	85,915	74,719
Regulatory assessments	46,691	54,633
Share-based compensation expense	83,281	44,500
Subscriptions	47,516	45,663
Supplies and printing	33,401	32,601
Other noninterest expense	268,117	289,344
Total noninterest expense	2,634,248	2,515,570
INCOME BEFORE PROVISION FOR INCOME TAXES	716,580	783,311
PROVISION FOR INCOME TAXES	202,000	235,000
NET INCOME	$ 514,580	$ 548,311
Basic earnings per share of common stock	$ 0.49	$ 0.52
Diluted earnings per share of common stock	$ 0.48	$ 0.51

See accompanying notes.

STATEMENTS OF COMPREHENSIVE INCOME

	Years Ended December 31, 2016	2015
NET INCOME	$ 514,580	$ 548,311
Other comprehensive income (loss):		
Unrealized holding losses on investment securities available-for-sale	(377,824)	(98,133)
Reclassification adjustment for realized gains on investment securities included in net income	(30,093)	(44,474)
Income tax effects	155,000	54,200
Other comprehensive loss, net of tax	(252,917)	(88,407)
COMPREHENSIVE INCOME	$ 261,663	$ 459,904

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Common Stock Shares	Common Stock Amount	Additional Paid In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
BALANCE, December 31, 2014	1,045,960	$ 10,250,363	$ 691,965	$ (1,723,799)	$ 32,038	$ 9,250,567
Net income	-	-	-	548,311	-	548,311
Restricted stock awards vested	4,200	-	-	-	-	-
Share-based compensation	-	-	44,500	-	-	44,500
Other comprehensive loss, net of tax	-	-	-	-	(88,407)	(88,407)
BALANCE, December 31, 2015	1,050,160	10,250,363	736,465	(1,175,488)	(56,369)	9,754,971
Net income	-	-	-	514,580	-	514,580
Restricted stock awards vested	4,500	-	-	-	-	-
Share-based compensation	-	-	83,281	-	-	83,281
Other comprehensive loss, net of tax	-	-	-	-	(252,917)	(252,917)
BALANCE, December 31, 2016	1,054,660	$ 10,250,363	$ 819,746	$ (660,908)	$ (309,286)	$ 10,099,915

CLATSOP COMMUNITY BANK
STATEMENTS OF CASH FLOWS

	Years Ended December 31, 2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 514,580	$ 548,311
Adjustments to reconcile net income to net cash from operations:		
Net amortization of premiums on investment securities available-for-sale	191,310	139,506
Gain on sale of investment securities	(30,093)	(44,474)
Gain on sale of other real estate owned and repossessed assets	(4,953)	(11,042)
Gain on sale of government guaranteed loans	(84,585)	(105,068)
Depreciation and amortization expense	130,224	135,140
Share-based compensation expense	83,281	44,500
Loss on disposal of capitalized fixed asset costs	-	4,259
Increase in cash surrender value of bank-owned life insurance	(70,198)	(71,103)
Deferred tax provision	199,985	232,502
Changes in cash and cash equivalents due to changes in:		
Accrued interest receivable and other assets	(69,744)	(11,391)
Accrued interest payable and other liabilities	(29,575)	34,330
Net cash from operating activities	830,232	895,470
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from the sale of available-for-sale securities	3,741,558	4,907,965
Proceeds from principal paydowns on available-for-sale securities	3,590,811	2,831,247
Proceeds from the maturity and call of available-for-sale securities	1,500,000	-
Purchase of available-for-sale securities	(16,706,564)	(7,145,479)
Purchase of time deposits with other financial institutions	(488,590)	(490,000)
Proceeds from redemption of restricted equity securities	230,100	41,200
Purchase of restricted equity securities	(438,300)	(13,700)
Proceeds from sales of government guaranteed loans	1,238,502	1,156,620
Net increase in loans	(4,602,778)	(4,585,673)
Proceeds from the sale of other real estate owned and repossessed assets	34,953	42,042
Purchases of premises, equipment, software, and leasehold improvements	(13,958)	(46,068)
Net cash from investing activities	(11,914,266)	(3,301,846)

See accompanying notes.

	Years Ended December 31, 2016	2015
CASH FLOWS FROM FINANCING ACTIVITIES		
Net change in deposit accounts	$ 4,876,356	$ 7,264,577
Proceeds from borrowings	2,500,000	-
Repayments of borrowed funds	-	(1,000,000)
Net cash from financing activities	7,376,356	6,264,577
NET CHANGE IN CASH AND CASH EQUIVALENTS	(3,707,678)	3,858,201
CASH AND CASH EQUIVALENTS, beginning of period	5,918,954	2,060,753
CASH AND CASH EQUIVALENTS, end of period	$ 2,211,276	$ 5,918,954
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Interest paid in cash	$ 123,164	$ 131,720
Taxes paid in cash	$ 2,000	$ 2,000
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITIES		
Change in fair value of investment securities available-for-sale, net of tax	$ (252,917)	$ (88,407)
Transfer of loan to repossessed assets	$ -	$ 30,000

See accompanying notes.

Note 1 – Organization and Summary of Significant Accounting Policies

Organization and nature of operations – Clatsop Community Bank (the Bank), an Oregon business corporation, incorporated for the purpose of becoming a commercial bank headquartered in Seaside, Oregon in August 2007. The Bank received its charter from the State of Oregon and commenced banking operations on April 22, 2008.

The Bank, from its Seaside headquarters office and a branch location in Astoria, Oregon, provides banking services to businesses and individuals located primarily in and around Clatsop County, Oregon. The Bank is subject to regulation by certain federal and state agencies and undergoes periodic examination by these regulatory authorities.

Basis of financial statement presentation – The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and with prevailing practices within the banking industry. In preparing the financial statements, management is required to make certain estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the balance sheet and the reported amounts of revenues and expenses for the reporting period. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change related to the determination of the allowance for loan losses, values of other real estate owned, stock-based compensation, fair values of investment securities, and depreciation of premises, equipment, and leasehold improvements.

Cash and cash equivalents – Cash and cash equivalents include cash and due from banks, and temporary investments such as federal funds sold and interest-bearing balances due from other banks. Cash and cash equivalents generally have a maturity of 90 days or less at the time of purchase.

The Bank maintains balances in correspondent bank accounts which at times may exceed federally insured limits. Management believes that the risk of loss associated with such balances is minimal due to the financial strength of the correspondent banks. The Bank has not experienced any losses in such accounts.

Time deposits with other financial institutions – Interest-earning deposits at other financial institutions include certificates of deposit with an original term greater than 90 days. These certificates of deposit are carried at amortized cost. As of December 31, 2016, the certificates of deposit had interest rates of 2.25% and $243,417 matures in 2019, $490,000 matures in 2020, and $245,000 matures in 2021.

Investment securities – The Bank is required to specifically identify its investment securities as “trading accounts,” “available-for-sale,” or “held-to-maturity.”

Note 1 – Organization and Summary of Significant Accounting Policies (continued)

Investments are classified in the trading category if the Bank's intention is to hold the investment principally for the purpose of realizing short-term gains during periods of 90 days or less. Such investments are carried at fair value and changes in fair value are recognized in earnings during the period in which they arise. The Bank held no investments in this trading category during 2016 or 2015.

Securities are classified as available-for-sale if the Bank intends to hold those debt securities 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 such as: (1) changes in market interest rates and related changes in the prepayment risk, (2) needs for liquidity, (3) changes in the availability of and the yield on alternative instruments, and (4) changes in funding sources and terms. Unrealized holding gains and losses, net of tax, on available-for-sale securities are reported as other comprehensive income and carried as accumulated comprehensive income or loss within shareholders' equity until realized.

Investments for which the Bank has the positive intent and ability to hold until maturity are classified as held-to-maturity and carried at amortized cost. The Bank held no investments in the held-to-maturity category during 2016 or 2015.

Premiums and discounts arising from the purchase of investment securities are recognized in interest income using the effective interest method. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Management reviews investment securities on an ongoing basis for the presence of other-than-temporary impairment (OTTI) or permanent impairment, taking into consideration current market conditions; fair value in relationship to cost; extent and nature of the change in fair value; issuer rating changes and trends; whether management intends to sell a security or if it is likely that the Bank will be required to sell the security before recovery of the amortized cost basis of the investment, which may be maturity; and other factors. For debt securities, if management intends to sell the security or it is likely that the Bank will be required to sell the security before recovering its cost basis, the entire impairment loss would be recognized in earnings as an OTTI. If management does not intend to sell the security and it is not likely that the Bank will be required to sell the security, but management does not expect to recover the entire amortized cost basis of the security, only the portion of the impairment loss representing credit losses would be recognized in earnings. The credit loss on a security is measured as the difference between the amortized cost basis and the present value of the cash flows expected to be collected. Projected cash flows are discounted by the original or current effective interest rate depending on the nature of the security being measured for potential OTTI. The remaining impairment related to all other factors, that is, the difference between the present value of the cash flows expected to be collected and fair value, is recognized as a charge to other comprehensive income.

Note 1 – Organization and Summary of Significant Accounting Policies (continued)

Loans, net of allowance for loan losses and deferred loan fees – Loans are stated at the amount of unpaid principal, net of an allowance for loan losses and net of deferred loan fees or costs. Interest on loans is calculated using the simple-interest method on daily balances of the principal amount outstanding. Loan origination fees and certain direct origination costs are capitalized and recognized as an adjustment to the yield of the related loan.

Loans are classified as impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal and interest when due, in accordance with the terms of the original loan agreement. The carrying value of impaired loans is based on the present value of expected future cash flows (discounted at each loan's effective interest rate) or, for collateral dependent loans, at fair value of the collateral. If the measurement of each impaired loan's value is less than the recorded investment in the loan, an impairment allowance is created by either charging the provision for loan losses or allocating an existing component of the allowance for loan losses.

Loans, including impaired loans, are classified as nonaccrual if the collection of principal and interest is doubtful. Generally, this occurs when a loan is past due as to maturity or payment of principal or interest by 90 days or more, unless such loans are well-secured and in the process of collection. If a loan or portion thereof is partially charged-off, the loan is considered impaired and classified as nonaccrual. Loans that are less than 90 days past due may also be classified as nonaccrual if repayment in full of principal and/or interest is in doubt.

When a loan is classified as nonaccrual, all uncollected accrued interest is reversed to interest income and the accrual of interest income is terminated. Generally, any cash payments are applied as a reduction of principal outstanding. In cases where the future collectability of the principal balance in full is expected, interest income may be recognized on a cash basis. A loan may be restored to accrual status when the borrower's financial condition improves so that full collection of principal is considered likely.

A troubled debt restructuring is a formal restructure of a loan where the Bank, for economic or legal reasons related to the borrower's financial difficulties, grants a concession to the borrower. The concessions may be granted in various forms, including reduction in the stated interest rate, reduction in the loan balance or accrued interest, and extension of the maturity date. Troubled debt restructurings are measured at the time of restructure for impairment, and are subjected to the Bank's impaired loan accounting policy.

Note 1 – Organization and Summary of Significant Accounting Policies (continued)

The allowance for loan losses is established through a provision for loan losses charged to expenses. Loans are charged against the allowance for loan losses when management believes that the collectability of principal is unlikely. The allowance is an amount that management believes will be adequate to absorb possible losses on existing loans that may become uncollectible, based on evaluations of the collectability of loans and prior loan loss experience. These evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, and current economic conditions that may affect the borrower's ability to pay. Various regulatory agencies, as a regular part of their examination process, periodically review the Bank's allowance for loan losses. Such agencies may require the Bank to recognize additions to the allowance based on their judgment of information available to them at the time of their examinations.

A reserve for unfunded commitments is maintained at a level that, in the opinion of management, is adequate to absorb probable losses associated with the Bank's commitment to lend funds under existing agreements such as letters or lines of credit. Management determines the adequacy of the reserve for unfunded commitments based upon reviews of individual credit facilities, current economic conditions, the risk characteristics of the various categories of commitments and other relevant factors. The reserve is based on estimates, and ultimate losses may vary from current estimates. These estimates are evaluated on a regular basis and, as adjustments become necessary, they are reported in earnings in the periods in which they become known.

Restricted equity securities – Restricted equity securities consist of investments in Independent Bankers Financial Corporation (IBFC) stock and Federal Home Loan Bank (FHLB) stock.

The Bank's investment in IBFC stock is a restricted equity security accounted for using the equity method of accounting. As a customer financial institution of IBFC, the Bank was required to purchase a minimum of $100,000 in shares of IBFC stock. As a financial institution customer of IBFC, the Bank has access to a federal funds line of credit and correspondent banking relationship with The Independent Bankers Bank, a subsidiary of IBFC. During the year ended December 31, 2016, the Bank purchased $100,000 in shares of IBFC stock. At December 31, 2016 and 2015, the carrying value of the IBFC stock was $100,000 and $0, respectively.

As a member of the Federal Home Loan Bank (FHLB) system, the Bank is required to maintain a minimum investment level in FHLB stock based on specific percentages of the Bank's outstanding mortgages, total assets, or FHLB advances. These securities are reported at par value, which represents the Bank's cost. On June 1, 2015, the FHLB Des Moines announced the completion of its merger with the FHLB Seattle effective May 31, 2015. At that time, the combined entity repurchased excess stock above what was needed to support borrowings, resulting in a reduction of outstanding FHLB stock.

Note 1 – Organization and Summary of Significant Accounting Policies (continued)

Restricted equity securities are evaluated for impairment based on ultimate recoverability. The determination of whether the investment is impaired is based on the Bank's assessment of the ultimate recoverability of par value rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability is influenced by criteria such as (1) the significance of decline in the net assets of the FHLB or IBFC as compared to the capital stock amount for the FHLB or IBFC and the length of time this situation has persisted, (2) commitments by the FHLB or IBFC to make payments required by law or regulation and the level of such payments in relation to the operating performance of the institution, (3) the impact of the legislative and regulatory changes on institutions and, accordingly, on the customer base of the institution, and (4) the liquidity position of the institution. Management's review for impairment is based on ultimate recoverability of the Bank's cost basis in its investment and concludes that the restricted equity securities are not impaired as of December 31, 2016 or 2015.

Premises, equipment, and leasehold improvements – Premises, equipment, and leasehold improvements are stated at cost less accumulated depreciation and amortization. Depreciation is provided over each asset's estimated useful life, on a straight-line basis. Buildings are depreciated over 39 years. Furniture, fixtures and equipment are depreciated over three to seven years. Leasehold improvements are amortized over the life of the related lease, or the life of the asset, whichever is shorter. The costs of maintenance and repairs are expensed as they are incurred. Expenditures for major renovations and betterments are capitalized.

Management reviews long-lived assets any time that a change in circumstance indicates that the carrying amount of these assets may not be recoverable. Recoverability of these assets is determined by comparing the carrying value of the asset to the forecasted undiscounted cash flows of the operation associated with the asset. If the evaluation of the forecasted cash flows indicates that the carrying value of the asset is not recoverable, the asset is written down to fair value.

Other real estate owned and repossessed assets – Other real estate owned and repossessed assets represent real estate or other assets that have been recognized upon foreclosure or repossession of property securing an outstanding loan. At the time of foreclosure or repossession, these assets are initially recorded at fair value, which becomes the new cost basis in the asset. Any write-downs based on the asset's fair value at the date of acquisition are charged to the allowance for loan losses. Subsequently, management periodically performs valuations such that these assets are carried at the lower of the new cost basis or fair value, net of estimated costs to sell. Fair value adjustments, including gains and losses, impairments or write-downs, are recognized within other non-interest expense.

Cash surrender value of bank-owned life insurance – The cash surrender value of the contract reflects the Bank's investment in the recorded asset, net of surrender charges. Changes in the cash surrender value of the contract are included in earnings as gains or losses in the period they arise.

Advertising expenses – Advertising costs are generally expensed as incurred.

Note 1 – Organization and Summary of Significant Accounting Policies (continued)

Income taxes – Income taxes are accounted for using an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the financial statement and tax basis of assets and liabilities at currently enacted tax rates applicable to the period in which the deferred income tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred income tax assets and liabilities are adjusted through the provision for income taxes. A valuation allowance is provided through a provision for income taxes when it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Bank evaluates the probability of the realization of its deferred tax assets by assessing its valuation allowance and by adjusting the amount of such allowance, if necessary.

The Bank recognizes the tax benefit from uncertain tax positions only if it is more likely than not that the tax positions will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefit is measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The Bank recognizes interest and penalties related to income tax matters in income tax expense, however there were none in 2016. The Bank is no longer subject to U.S. federal or state and local income tax examinations by tax authorities for years before 2013.

Share-based compensation – The Bank applies fair value recognition provisions in accounting for share-based compensation. Under this accounting standard, share-based awards that do not require future service are expensed immediately. Share-based employee awards that require future service are expensed over the requisite service period, net of forfeitures of such awards, on a straight-line basis.

The fair value of each option granted is estimated on the date of grant using the Black-Scholes option-pricing model, based on several assumptions. Expected volatility is based on the historical volatility of the price of the Bank's stock for a period consistent with the expected life of the option. The Bank uses historical data to estimate option exercise and employee termination rates within the valuation model. The expected term of options represents the period of time that stock options are expected to be outstanding and is estimated based on historical exercise and forfeiture activity within the banking industry. Expected dividends are estimated to be zero due to the Bank's historical practice of not paying dividends. The risk-free rate of return for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the grant date.

Earnings per common share – Basic earnings per common share is computed by dividing net income by the weighted average number of common shares outstanding during the period, after giving retroactive effect to any stock dividends and splits. Diluted earnings per common share is computed similar to basic earnings per common share except that the denominator is increased to include the number of additional common shares that would have been outstanding if potential dilutive common shares had been issued.

Note 1 – Organization and Summary of Significant Accounting Policies (continued)

Off-balance sheet financial instruments – The Bank holds no derivative financial instruments. However, in the ordinary course of business, the Bank enters into off-balance sheet financial instruments consisting of commitments to extend credit, commercial letters of credit, and standby letters of credit. These financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received.

Fair value of assets and liabilities – Fair value is defined as the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date. The Bank determines fair value based upon quoted prices when available or through the use of alternative approaches, such as matrix or model pricing, when market quotes are not readily accessible or available. The valuation techniques used are based on observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Bank's market assumptions.

These two types of inputs create the following fair value hierarchy:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset or liability. Unobservable inputs are used to measure fair value to the extent that observable inputs are not available. The Bank's own data used to develop unobservable inputs shall be adjusted for market consideration when reasonably available.

The Bank used the following methods and significant assumptions to estimate fair value for its assets measured and carried at fair value on a recurring or nonrecurring basis in the accompanying financial statements:

Investment securities available-for-sale – For these investments, the Bank obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things. When market quotes are not readily accessible or available, alternative approaches are utilized, such as matrix or model pricing.

Impaired loans – Impaired loans are measured and adjusted to fair value on a nonrecurring basis. Impaired loans are measured for impairment at the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's market price, or the fair value of the collateral based on independent appraisals, less costs to sell, if the loan is collateral dependent.

Note 1 – Organization and Summary of Significant Accounting Policies (continued)

Other real estate owned and repossessed – These assets are measured and adjusted to fair value, less costs to sell, on a nonrecurring basis based on recent appraisals.

The following methods and assumptions were used by the Bank in estimating fair values of other assets and liabilities for disclosure purposes:

Cash and cash equivalents – For these short-term instruments, the carrying amount is a reasonable estimate of fair value.

Investment securities available-for-sale – For these securities, the Bank obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and bond terms and conditions, among other things. When market quotes are not readily accessible or available, alternative approaches are utilized, such as matrix or model pricing.

Time deposits with other financial institutions – Fair value for time certificates with other banks are based on the market values for comparable investments.

Restricted equity securities – Due to significant restrictions on these securities, it is impractical to estimate the fair value. As a result, the fair value has been determined to approximate cost.

Loans – For certain variable rate loans, fair value is estimated at carrying value, as these loans frequently re-price to market. The fair value of other types of loans is estimated by discounting future cash flows, using current rates at which similar loans would be made to borrowers with similar credit risk and for the same remaining maturities.

Deposit liabilities – The fair value of demand deposits, savings deposits, and money market accounts is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated by discounting future cash flows, using the rates currently offered for deposits of similar remaining maturities.

Borrowed funds – Rates currently available to the Bank for such borrowings with similar terms and remaining maturities are used to estimate the fair values using discounted cash flow analysis.

Accrued interest receivable and payable – The fair values of accrued interest receivable and payable are based on the amounts to be received or paid, which approximates carrying value at the reporting date.

Commitments to extend credit and commercial and standby letters of credit – The fair values of these off-balance sheet commitments to extend credit and commercial and standby letters of credit are not considered practicable to estimate because of the lack of quoted market prices and the inability to estimate fair value without incurring excessive costs.

Note 1 – Organization and Summary of Significant Accounting Policies (continued)

Subsequent events – Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. The Bank recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing the financial statements. The Bank's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date and before financial statements are available to be issued. The Bank has evaluated subsequent events through February 24, 2017, which is the date the financial statements became available to be issued.

Note 2 – Investment Securities

The amortized cost and estimated fair value of investment securities available-for-sale are as follows:

	December 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Mortgage-backed securities	$ 13,644,626	$ 2,180	$ (303,192)	$ 13,343,614
Collateralized mortgage obligations	6,334,987	-	(135,151)	6,199,836
Municipal securities	1,971,347	-	(59,249)	1,912,098
Agency securities	499,938	-	(3,380)	496,558
	$ 22,450,898	$ 2,180	$ (500,972)	$ 21,952,106

	December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Mortgage-backed securities	$ 11,150,101	$ 26,155	$ (93,409)	$ 11,082,847
Collateralized mortgage obligations	533,037	2,588	(16,149)	519,476
Municipal securities	554,790	-	(4,715)	550,075
Agency securities	2,499,785	-	(5,329)	2,494,456
	$ 14,737,713	$ 28,743	$ (119,602)	$ 14,646,854

Note 2 – Investment Securities (continued)

At December 31, 2016, the Bank had 40 investment securities in a loss position for less than twelve months, and 11 in an unrealized loss position for greater than twelve months, and at December 31, 2015, the Bank had 12 investment securities in a loss position for less than twelve months, and 9 in an unrealized loss position for greater than twelve months as shown in the following table. The Bank evaluated the unrealized losses and determined that the declines in value were temporary and related to the change in market interest rates since the date of purchase.

	December 31, 2016					
	Less than 12 Months		Greater than 12 Months		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
Mortgage-backed securities	$ 9,993,228	$ (236,835)	$ 2,994,433	$ (66,357)	$ 12,987,661	$ (303,192)
Collateralized mortgage obligations	5,967,359	(127,700)	232,477	(7,451)	6,199,836	(135,151)
Municipal securities	1,912,097	(59,249)	-	-	1,912,097	(59,249)
Agency securities	496,558	(3,380)	-	-	496,558	(3,380)
	$ 18,369,242	$ (427,164)	$ 3,226,910	$ (73,808)	$ 21,596,152	$ (500,972)

	December 31, 2015					
	Less than 12 Months		Greater than 12 Months		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
Mortgage-backed securities	$ 4,392,989	$ (39,665)	$ 2,403,547	$ (53,744)	$ 6,793,536	$ (93,409)
Collateralized mortgage obligations	-	-	298,823	(16,149)	298,823	(16,149)
Municipal securities	550,075	(4,715)	-	-	550,075	(4,715)
Agency securities	2,494,456	(5,329)	-	-	2,494,456	(5,329)
	$ 7,437,520	$ (49,709)	$ 2,702,370	$ (69,893)	$ 10,136,890	$ (119,602)

Note 2 – Investment Securities (continued)

The amortized cost and estimated fair value of available-for-sale investment securities and held to maturity securities as of December 31, 2016, by contractual maturity, are shown below. The amortized cost and fair value of mortgage-backed securities are presented by expected average life, rather than contractual maturity. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-sale	
	Amortized Cost	Estimated Fair Value
Due in one year or less	$ -	$ -
Due after one year through five years	17,799,816	17,467,167
Due after five years through ten years	4,651,082	4,484,939
Thereafter	-	-
	$ 22,450,898	$ 21,952,106

During 2016, the Bank received $3,741,558 and realized a gain of $35,118 and $5,025, respectively, from the sale of securities available-for-sale. During 2015, the Bank received $4,907,965 and realized a gain and loss of $52,320 and $7,846, respectively, from the sale of securities available-for-sale. As of December 31, 2016 and 2015, investment securities with fair values of $4,002,451 and $3,287,015, respectively, were pledged to secure FHLB borrowings and public deposits.

Note 3 – Loans, Net of Allowance for Loan Losses and Net Deferred Loan Fees

The loan portfolio consists of the following loan categories as of December 31:

	2016	2015
Commercial real estate	$ 35,145,677	$ 33,683,888
Commercial	5,575,770	5,918,828
Construction	3,912,229	3,191,810
Residential real estate	8,880,815	6,727,677
Consumer	1,396,550	1,880,270
	54,911,041	51,402,473
Deferred loan fees, net	(117,138)	(49,570)
Allowance for loan losses	(615,616)	(623,477)
Loans, net of allowance for loan losses and net deferred loan fees	$ 54,178,287	$ 50,729,426

Note 4 – Allowance for Loan Losses

The following table displays the allocation of the allowance for loan losses to significant segments of the loan portfolio at December 31, along with activity in the allowance for loan losses for the years then ended:

2016	Commercial Real Estate	Commercial	Construction	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses							
Beginning balance	$ 92,418	$ 116,133	$ 166,497	$ 54,416	$ 10,474	$ 183,539	$ 623,477
Charge-offs	-	-	-	-	(11,010)	-	(11,010)
Recoveries	-	-	-	-	3,149	-	3,149
Provision for loan losses	27,141	(59,655)	(3,319)	9,781	6,545	19,507	-
Ending balance	$ 119,559	$ 56,478	$ 163,178	$ 64,197	$ 9,158	$ 203,046	$ 615,616
Ending balance Individually evaluated for impairment	$ -	$ 7,472	$ -	$ -	$ -	$ -	$ 7,472
Ending balance Collectively evaluated for impairment	$ 119,559	$ 49,006	$ 163,178	$ 64,197	$ 9,158	$ 203,046	$ 608,144
Loans							
Ending balance Individually evaluated for impairment	$ 240,492	$ 7,472	$ -	$ 44,022	$ -	$ -	$ 291,986
Ending balance Collectively evaluated for impairment	$ 34,905,185	$ 5,568,298	$ 3,912,229	$ 8,836,793	$ 1,396,550	$ -	$ 54,619,055

2015	Commercial Real Estate	Commercial	Construction	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses							
Beginning balance	$ 93,818	$ 53,675	$ 300,966	$ 82,252	$ 9,169	$ 64,121	$ 604,001
Charge-offs	-	(2,141)	(1,208)	-	-	-	(3,349)
Recoveries	-	22,825	-	-	-	-	22,825
Provision for loan losses	(1,400)	41,774	(133,261)	(27,836)	1,305	119,418	-
Ending balance	$ 92,418	$ 116,133	$ 166,497	$ 54,416	$ 10,474	$ 183,539	$ 623,477
Ending balance Individually evaluated for impairment	$ -	$ 9,567	$ -	$ -	$ -	$ -	$ 9,567
Ending balance Collectively evaluated for impairment	$ 92,418	$ 106,566	$ 166,497	$ 54,416	$ 10,474	$ 183,539	$ 613,910
Loans							
Ending balance Individually evaluated for impairment	$ 255,366	$ 9,567	$ -	$ -	$ -	$ -	$ 264,933
Ending balance Collectively evaluated for impairment	$ 33,428,522	$ 5,909,261	$ 3,191,810	$ 6,727,677	$ 1,880,270	$ -	$ 51,137,540

Note 4 – Allowance for Loan Losses (continued)

Credit quality indicators – The Bank's risk rating methodology assigns risk ratings ranging from 1 to 9, where a higher rating represents higher risk. Assignment of a risk rating is done on the individual loan rather than at the borrower level. Loans are graded from inception and on a continuing basis until the debt is repaid.

Pass/Watch – An acceptable asset carrying a normal degree of credit risk exhibiting the capacity to perform according to the repayment terms. There are five grades within this category.

Special mention – A special mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in a deterioration of the repayment prospects for the asset or in the institution's credit position at some future date. Special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

Substandard – A substandard asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged. Assets so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt.

Doubtful – Any asset classified doubtful has all the weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and value, highly questionable and improbable.

Loss – Assets classified loss are considered uncollectible and of such minimal value that the continuance as bankable assets are not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value but that it is not practical or desirable to defer writing off this presumed worthless asset even though a partial recovery may occur in the future.

Note 4 – Allowance for Loan Losses (continued)

The following table represents loan portfolio information by loan type and credit grade as of December 31, 2016 and 2015:

	Commercial Real Estate		Commercial		Construction	
	2016	2015	2016	2015	2016	2015
Grade						
Pass	$ 35,145,677	$ 33,683,888	$ 5,575,770	$ 5,240,253	$ 3,912,229	$ 3,191,810
Special mention	-	-	-	-	-	-
Substandard	-	-	-	678,575	-	-
Total	$ 35,145,677	$ 33,683,888	$ 5,575,770	$ 5,918,828	$ 3,912,229	$ 3,191,810

	Residential Real Estate		Consumer		Total Loans	
	2016	2015	2016	2015	2016	2015
Grade						
Pass	$ 8,836,793	$ 6,727,677	$ 1,396,550	$ 1,880,270	$ 54,867,019	$ 50,723,898
Special mention	-	-	-	-	-	-
Substandard	44,022	-	-	-	44,022	678,575
Total	$ 8,880,815	$ 6,727,677	$ 1,396,550	$ 1,880,270	$ 54,911,041	$ 51,402,473

The following table presents an aging analysis of past due loans as of December 31, 2016 and 2015:

	2016						
	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Recorded Investment > 90 Days and Accruing
Commercial real estate	$ -	$ -	$ -	$ -	$ 35,145,677	$ 35,145,677	$ -
Commercial	-	-	-	-	5,575,770	5,575,770	-
Construction	-	-	-	-	3,912,229	3,912,229	-
Residential real estate	363,697	-	-	363,697	8,517,118	8,880,815	-
Consumer	-	-	-	-	1,396,550	1,396,550	-
	$ 363,697	$ -	$ -	$ 363,697	$ 54,547,344	$ 54,911,041	$ -

	2015						
	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Recorded Investment > 90 Days and Accruing
Commercial real estate	$ -	$ -	$ -	$ -	$ 33,663,283	$ 33,683,888	$ -
Commercial	-	-	-	-	5,918,828	5,918,828	-
Construction	-	-	-	-	3,191,810	3,191,810	-
Residential real estate	-	-	-	-	6,727,677	6,727,677	-
Consumer	-	-	-	-	1,880,270	1,880,270	-
	$ -	$ -	$ -	$ -	$ 51,381,868	$ 51,402,473	$ -

Note 4 – Allowance for Loan Losses (continued)

The following table shows impaired loans and the related specific allowance for loan losses as of December 31, 2016 and 2015 along with the average recorded investment and interest income recognized on impaired loans for the years then ended:

	2016				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded					
Construction	$ -	$ -	$ -	$ -	$ -
Commercial real estate	240,492	240,492	-	251,259	18,595
Residential real estate	44,022	44,022	-	44,645	1,431
Commercial	-	-	-	8,920	596
	$ 284,514	$ 284,514	$ -	$ 304,824	$ 20,622
With an allowance recorded					
Construction	$ -	$ -	$ -	$ -	$ -
Commercial real estate	-	-	-	-	-
Residential real estate	-	-	-	-	-
Commercial	7,472	7,472	7,472	9,158	596
	$ 7,472	$ 7,472	$ 7,472	$ 9,158	$ 596
Total					
Construction	$ -	$ -	$ -	$ -	$ -
Commercial real estate	240,492	240,492	-	251,259	18,595
Residential real estate	44,022	44,022	-	44,645	1,431
Commercial	7,472	7,472	7,472	18,078	1,192
Total impaired loans	$ 291,986	$ 291,986	$ 7,472	$ 313,982	$ 21,218

	2015				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded					
Construction	$ -	$ -	$ -	$ 31,524	$ -
Commercial real estate	255,366	255,366	-	266,755	19,718
Residential real estate	-	-	-	28,873	-
Commercial	-	-	-	60,033	-
	$ 255,366	$ 255,366	$ -	$ 387,185	$ 19,718
With an allowance recorded					
Construction	$ -	$ -	$ -	$ -	$ -
Commercial real estate	-	-	-	-	-
Residential real estate	-	-	-	-	-
Commercial	9,567	9,567	9,567	8,248	-
	$ 9,567	$ 9,567	$ 9,567	$ 8,248	$ -
Total					
Construction	$ -	$ -	$ -	$ 31,524	$ -
Commercial real estate	255,366	255,366	-	266,755	19,718
Residential real estate	-	-	-	28,873	-
Commercial	9,567	9,567	9,567	68,281	-
Total impaired loans	$ 264,933	$ 264,933	$ 9,567	$ 395,433	$ 19,718

Note 4 – Allowance for Loan Losses (continued)

The following table shows loans on nonaccrual status as of December 31:

	2016	2015
Commercial	$ -	$ -
Construction	-	-
Residential real estate	-	9,567
	$ -	$ 9,567

As of December 31, 2016 and December 31, 2015, the Bank identified troubled debt restructurings in the amount of $7,472 and $11,523, respectively. The loans have been performing under their restructured terms.

Note 5 – Premises, Equipment, and Leasehold Improvements

The composition of premises, equipment, and leasehold improvements as of December 31, 2016 and 2015 is summarized as follows:

	2016	2015
Building	$ 1,472,763	$ 1,472,736
Land	952,021	952,021
Furniture and fixtures	621,422	621,422
Equipment	563,599	556,204
Software	92,911	92,911
Leasehold improvements	53,024	46,461
Total furniture, equipment, and leasehold improvements	3,755,740	3,741,755
Less accumulated depreciation and amortization	(1,282,521)	(1,152,297)
Premises, equipment, and leasehold improvements, net of accumulated depreciation and amortization	$ 2,473,219	$ 2,589,458

Depreciation and amortization expense for the years ended December 31, 2016 and 2015 was $130,224 and $135,140, respectively.

Note 6 – Time Deposits

Time certificates of deposit of $250,000 and over aggregated $2,697,532 and $4,191,026 as of December 31, 2016 and 2015, respectively. At December 31, 2016, the scheduled maturities of all time certificates of deposit were as follows:

Years ending December 31,	2017	$ 5,530,148
	2018	2,271,840
	2019	1,090,859
	2020	544,239
	2021	361,447
	2022 and beyond	-
		$ 9,798,533

Note 7 – Lines of Credit and Borrowed Funds

As a member of the Federal Home Loan Bank of Seattle (FHLB), the Bank has entered into an "Advances, Security and Deposit Agreement" with the FHLB. Borrowings under the credit arrangement are collateralized by the Bank's FHLB stock as well as loans or other instruments, which may be pledged. As of December 31, 2016 and December 31, 2015, loans and securities in the amount of $36,331,294 and $31,758,632, respectively, were pledged to secure borrowings. The Bank had $2,500,000 in outstanding borrowings with the FHLB carrying interest rates between 0.86% and 0.96% as of December 31, 2016. There were no outstanding borrowings with the FHLB as of December 31, 2015. At December 31, 2016, borrowings outstanding with FHLB were scheduled to mature in 2017.

The Bank had federal funds lines of credit agreement with two financial institutions as of December 31, 2016. The maximum borrowing available under these lines was $3,700,000. The lines are intended to support short-term liquidity needs, and the agreements may restrict consecutive day usage. There was no balance outstanding as of December 31, 2016 or 2015.

Note 8 – Income Taxes

Income taxes consist of the following for the years ended December 31, 2016 and 2015:

	2016	2015
Current tax provision		
Federal	$ -	$ -
State and local	2,015	2,498
	2,015	2,498
Deferred tax provision		
Federal	191,185	193,902
State and local	8,800	38,600
	199,985	232,502
Change in valuation allowance	-	-
Provision for income taxes	$ 202,000	$ 235,000

The components of the net deferred tax assets at December 31, 2016 and 2015 were as follows:

	2016	2015
Deferred tax assets		
Net operating loss carryforward	$ 777,805	$ 1,042,100
Unamortized preopening start-up costs	110,700	128,100
Reserve for loan losses	204,700	204,700
Unrealized losses on securities available-for-sale	189,500	34,500
Nonaccrual loan interest	-	200
Share-based compensation	68,200	42,200
Accrued compensation	9,800	15,500
Total deferred tax assets	1,360,705	1,467,300
Deferred tax liabilities		
Accumulated depreciation	83,800	89,400
Prepaid expenses	14,500	42,200
Loan origination costs	107,000	107,900
Other	1,240	28,650
Total deferred tax liabilities	206,540	268,150
Net deferred tax assets	$ 1,154,165	$ 1,199,150

Note 8 – Income Taxes (continued)

At December 31, 2016 and 2015, the Bank had federal net operating loss carryforwards of approximately $2,163,600 and $2,805,000, and unamortized pre-opening expenses, capitalized for tax purposes, of approximately $283,700 and $328,400, respectively. The carryforwards will be available to offset future taxable income. Unless utilized in earlier tax years, the carryforwards will expire beginning in 2027. The pre-opening expenses are being amortized and deducted for tax purposes over a 180 month period and will be fully amortized in 2022.

The following summarizes the difference between the provision for income taxes for financial statement purposes and the federal statutory rate of 34.00% for the years ended December 31, 2016 and 2015:

	2016		2015	
Federal, at statutory rate	$ 243,685	34.00%	$ 266,326	34.00%
State and local, net of federal benefit	37,451	5.23%	40,791	5.21%
Tax-exempt interest, net of expenses	(42,121)	-5.88%	(51,546)	-6.64%
Bank-owned life insurance	(27,388)	-3.82%	(27,742)	-3.57%
Other	(9,627)	-1.34%	7,171	-4.40%
Provision for income taxes, at effective rate	$ 202,000	28.19%	$ 235,000	24.60%

The Bank does not anticipate that the amount of unrecognized tax benefits will significantly increase or decrease in the next 12 months. There were no interest or penalties accrued for the year ended December 31, 2016 or 2015. The Bank files U.S. federal and Oregon state income tax returns, which are subject to examination by the taxing authorities for years 2013 and later.

Note 9 – Transactions with Related Parties

Certain directors, executive officers, and principal shareholders are customers of and have had banking transactions with the Bank in the ordinary course of business, and the Bank expects to have such transactions in the future. Management believes loans and commitments to loan included in such transactions are made in compliance with applicable laws on substantially the same terms (including interest rates and collateral) as those prevailing at the time for comparable transactions with other persons and, in the opinion of the management of the Bank, do not involve more than the normal risk of collection or present any other unfavorable features.

Note 9 – Transactions with Related Parties (continued)

An analysis of the activity with respect to loans outstanding to directors and executive officers of the Bank and its affiliates for the years ended December 31 is as follows:

	2016	2015
Beginning balance	$ 1,364,887	$ 1,506,428
Additions	-	-
Repayments	(122,735)	(141,541)
Ending balance	$ 1,242,152	$ 1,364,887

Related party deposits held by the Bank at December 31, 2016 and 2015, were $1,256,879 and $739,306, respectively.

Note 10 – Financial Instruments with Off-Balance Sheet Risk

In the normal course of business to meet the financing needs of its customers, the Bank becomes a party to financial instruments with off-balance sheet risk. These financial instruments include commitments to extend credit and the issuance of letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The contract amounts of those instruments reflect the extent of involvement the Bank has in particular classes of financial instruments.

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

Commitments to extend credit are agreements to lend to customers, 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, total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property and equipment, and income-producing properties.

Letters of credit written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank may hold cash, marketable securities, or real estate as collateral supporting those commitments for which collateral is deemed necessary.

Note 10 – Financial Instruments with Off-Balance Sheet Risk (continued)

The notional amount of the Bank's financial instruments with off-balance sheet risk as of December 31, 2016 and 2015 consisted of commitments to extend credit totaling $6,565,493 and $6,086,241, respectively. No letters of credit were outstanding as of December 31, 2016 and 2015.

Note 11 – Concentrations of Credit Risk

The Bank maintains balances in correspondent bank accounts that at times may exceed federally insured limits. Management believes that its risk of loss associated with such balances is minimal due to the financial strength of the correspondent banks.

A majority of the Bank's loans and commitments have been granted to customers in the Bank's market area. The distribution of commitments to extend credit is expected to approximate the distribution of loans outstanding. Concentrations of credit by type of loan are set forth in Note 3. The Bank's loan policies do not allow the extension of credit to any single borrower or group of related borrowers in excess of the Bank's legal lending limit, as defined in state banking regulations.

Note 12 – Commitments and Contingencies

Operating leases – The Bank leases a branch facility set to expire December 2020 and certain equipment with various expiration dates under agreements accounted for as operating leases.

Following are the future minimum contractual lease payments as of December 31, 2016.

Years ending December 31,	2017	$ 31,500
	2018	32,100
	2019	32,700
	2020	28,125
	2021 and beyond	-
		$ 124,425

Rent expense was $31,187 and $39,492 for the years ended December 31, 2016 and 2015, respectively.

Legal contingencies – The Bank, in the ordinary course of business, may become a defendant in certain claims and legal actions. In the opinion of management, after consultation with legal counsel, there are no matters or potential claims presently known to the Bank that are expected to have a material adverse effect on the financial condition or results of operations of the Bank.

Note 12 – Commitments and Contingencies (continued)

Employment agreements – The Bank has entered into employment agreements with certain officers of the Bank. Such agreements provide for termination benefits upon a change in control or the occurrence of other specified events. The payments to the officers required under the agreements are generally based off of a multiple of the individual's annual compensation.

Note 13 – Share-Based Awards

The Bank has an active share-based compensation plan (the Plan) that provides for the granting of stock options and restricted stock awards to eligible employees and directors. The Plan allows for the granting of both incentive and nonqualified stock options as well as restricted stock awards. There are 250,000 shares authorized for issuance under the Plan. In the event a share-based award expires, terminates or is cancelled without having been exercised in full, the shares subject to the award return to the authorized pool of available shares. As of December 31, 2016, 57,215 shares are available for future grant under the Plan. All options granted and outstanding under the Plan are exercisable at purchase prices which approximate the fair value of the Bank's common stock on the date of grant. The options expire ten years from the date of grant. Option exercise prices, vesting period, number of shares granted to recipients, and durations for stock options are determined and approved by the Board of Directors.

The following assumptions were used to determine the fair value of option grants:

	2016
Dividend yield	0%
Expected life (years)	5.5
Expected volatility	41.59%
Risk-free rate	1.84%
Weighted average fair value per share	$ 2.70

Note 13 – Share-Based Awards (continued)

The following summarizes stock option activity under the Plan for the years ended December 31, 2016 and 2015:

	Total Options	Incentive Options	Non-statutory Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Weighted Average Grant-date Fair Value
Options outstanding – January 1, 2015	95,275	44,395	50,880	$ 6.00	$ 5.00	$ 3.00
Options granted	5,000	-	5,000	7.00	10.00	3.00
Options forfeited	-	-	-	-	-	-
Options outstanding – January 1, 2016	100,275	44,395	55,880	6.00	5.00	3.00
Options granted	12,500	-	12,500	7.00	9.00	3.00
Options forfeited	(7,260)	(7,260)	-	7.00	-	3.00
Options outstanding – December 31, 2016	105,515	37,135	68,380	7.00	4.00	3.00
Options exercisable – December 31, 2016	76,015	36,135	39,880	6.00	3.00	3.00
December 31, 2015	82,275	43,395	38,880	7.00	4.00	3.00

As of December 31, 2016, there was $102,856 of intrinsic value of shares exercisable and outstanding. Unrecognized compensation expense related to unvested stock options totaled $46,522 as of December 31, 2016, which will be recognized over a weighted average period of 1.11 years.

Note 13 – Share-Based Awards (continued)

The following table summarizes restricted stock award activity under the Plan:

	Number of Shares	Weighted Average Grant-date Fair Value
Restricted stock awards unvested at January 1, 2015	17,097	$ 5.86
Awards granted	5,000	7.00
Awards vested	(4,200)	5.75
Restricted stock awards unvested at December 31, 2015	17,897	4.63
Awards granted	3,000	7.00
Awards vested	(4,500)	5.90
Awards forfeited	(1,100)	5.65
Restricted stock awards unvested at December 31, 2016	15,297	4.64

The fair value of restricted stock awards vesting during 2016 and 2015 was approximately $25,987 and $24,733, respectively.

The Bank recognized $83,281 and $44,500 of stock-based compensation expense for restricted stock awards and stock options for the years ended December 31, 2016 and 2015, respectively. As of December 31, 2016, there was $25,987 of unrecognized stock-based compensation expense related to non-vested restricted stock awards, which will be recognized over a period of approximately three years. As of December 31, 2016, there were 57,215 shares available for future awards under the Plan.

Note 14 – Earnings per Share

The following is a computation of basic and diluted earnings per share for the years ended December 31, 2016 and 2015:

	2016	2015
Net income	$ 514,580	$ 548,311
Weighted average number of common shares outstanding – basic	1,053,362	1,049,134
Effects of potentially dilutive common shares	25,426	26,836
Weighted average number of common shares outstanding – diluted	1,078,788	1,075,970
Earnings per common share		
Basic	$ 0.49	$ 0.52
Diluted	0.48	0.51

There were approximately 100,000 and 103,000 shares of weighted average stock options, unvested restricted stock awards outstanding, and stock warrants outstanding for the years ended December 31, 2016 and 2015, respectively, which were excluded from the diluted earnings per share calculation due to their effect being anti-dilutive.

Note 15 – Stock Warrants and Options in Lieu of Warrants

In its initial stock offering, the Bank issued warrants and options in lieu of warrants to the individuals who provided at-risk funds to meet organizational expenses. All warrants and options in lieu of warrants allow for the purchase of additional common shares at $10 per share and were fully vested at the grant date. As of December 31, 2016 and 2015, warrants and options in lieu of warrants for the purchase of 82,000 shares were outstanding and fully exercisable. No warrants have been exercised and they expire in 2018.

Note 16 – Defined Contribution Employee Benefit Plan

The Bank sponsors a defined contribution and profit sharing plan under the provisions of Section 401(k) of the Internal Revenue Code, whereby eligible employees may defer a portion of their gross wages. Employees eligible to participate in the plan must be over 18 years of age and may contribute up to the maximum allowable by IRS statute. The Bank may make matching and discretionary contributions to the plan. Matching contributions vest over a five year vesting schedule. Discretionary contributions vest over a period of five years. During 2016, the Bank made a matching contribution up to 3% of eligible compensation totaling $28,529. During 2015, the Bank made a matching contribution up to 2% of eligible compensation totaling $20,429. No discretionary contributions were made for 2016 or 2015.

Note 17 – Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by federal and state banking agencies. Failure to meet minimum requirements can initiate certain mandatory – and possibly additional discretionary – actions by regulators that, if undertaken, could have a direct material effect on a bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, banks 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. Capital amounts and classification are also subject to qualitative judgments by 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 Tier 1, common equity Tier 1, and total capital to risk-weighted assets (as defined in the regulations), and of Tier 1 capital to average assets (as defined in the regulations).

Note 17 – Regulatory Matters (continued)

The Bank's capital amounts and ratios as of December 31, 2016 and 2015 are as follows:

	Actual		Capital Adequacy Purposes		To Be Well-Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(dollars in thousands)						
December 31, 2016						
Total capital to risk-weighted assets	$ 10,334	15.9%	$ 5,186	>8.0%	$ 6,483	>10.0%
Common equity Tier 1 capital to risk-weighted assets	9,718	15.0%	2,917	>4.5%	4,214	>6.5%
Tier 1 capital to risk-weighted assets	9,718	15.0%	3,890	>6.0%	5,186	>8.0%
Tier 1 capital to average assets	9,718	11.2%	3,456	>4.0%	4,320	>5.0%
December 31, 2015						
Total capital to risk-weighted assets	$ 10,434	16.8%	$ 4,972	>8.0%	$ 6,215	>10.0%
Common equity Tier 1 capital to risk-weighted assets	9,811	15.8%	2,797	>4.5%	4,040	>6.5%
Tier 1 capital to risk-weighted assets	9,811	15.8%	3,729	>6.0%	4,972	>8.0%
Tier 1 capital to average assets	9,811	12.3%	3,197	>4.0%	3,996	>5.0%

As of the most recent notification from its regulatory agencies, the Bank was categorized as well-capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the Bank's regulatory capital category. Management believes, as of December 31, 2016, that the Bank and the Company meet all capital adequacy requirements to which they are subject.

The Bank is required to establish and phase-in a "conservation buffer," consisting of a common equity Tier 1 capital amount equal to 2.5% of risk-weighted assets by 2019. An institution that does not meet the conservation buffer requirement will be subject to restrictions on certain activities including payment of dividends, stock repurchases, and discretionary bonuses to executive officers. The phase-in began in 2016 and increases 0.625% annually until fully phased-in by 2019.

Note 18 – Fair Value of Assets and Liabilities

The following tables disclose the estimated fair value and the related carrying value of the Bank's financial assets and liabilities:

	Carrying Value	Fair Value at December 31, 2016 Total	Level 1	Level 2	Level 3
Financial assets					
Cash and cash equivalents	$ 2,211,276	$ 2,211,276	$ 2,211,276	$ -	$ -
Time deposits with other financial institutions	978,417	984,173	-	984,173	-
Investment securities available-for-sale	21,952,106	21,952,106	-	21,952,106	-
Restricted equity securities	293,700	293,700	-	293,700	-
Loans	54,911,041	56,374,000	-	-	56,374,000
Accrued interest receivable	229,081	229,081	-	72,709	156,372
Financial liabilities					
Demand deposits, money market accounts, and savings deposits	63,143,409	63,143,409	63,143,409	-	-
Time deposits	9,798,533	9,855,000	-	-	9,855,000
Accrued interest payable	4,696	4,696	-	-	4,696

	Carrying Value	Fair Value at December 31, 2015 Total	Level 1	Level 2	Level 3
Financial assets					
Cash and cash equivalents	$ 5,918,954	$ 5,918,954	$ 5,918,954	$ -	$ -
Time deposits with other financial institutions	490,000	490,071	-	490,071	-
Investment securities available-for-sale	14,646,854	14,646,854	-	14,646,854	-
Restricted equity securities	85,500	85,500	-	85,500	-
Loans	51,402,473	53,202,000	-	-	53,202,000
Accrued interest receivable	168,124	168,124	-	37,852	130,272
Financial liabilities					
Demand deposits, money market accounts, and savings deposits	55,866,418	55,866,418	55,866,418	-	-
Time certificates of deposits	12,199,168	12,265,000	-	-	12,265,000
Accrued interest payable	3,046	3,046	-	-	3,046

While estimates of fair value are based on management's judgment of the most appropriate factors, there is no assurance that were the Bank to dispose of such items, the estimated fair values would necessarily be achieved at that date, since market values may differ depending on various circumstances. The estimated fair values should not necessarily be relied upon at subsequent dates.

In addition, other assets and liabilities of the Bank that are not defined as financial instruments are not included in the above disclosures, such as property and equipment. Also nonfinancial instruments typically not recognized in the consolidated financial statements nevertheless may have value but are not included in the above disclosures. These include, among other items, the estimated earnings power of core deposit accounts, the trained work force, customer goodwill, and similar items.