

# 2017 ANNUAL REPORT

*We've got you covered!*



# Corporate Profile

Chino Commercial Bank (CCB) has become one of the Inland Empire's leading community banks, with three full-service banking offices operating in the diverse and growing economic regions of Chino, Ontario and Rancho Cucamonga, California. CCB provides small businesses and individuals with high-quality banking products and an unmatched personalized level of service.

Founded in September 2000, Chino Commercial Bank was established with an emphasis on the value of local ownership, community involvement and commitment to excellent personal service. The Bank's remarkable growth is a testimony to the broad acceptance of CCB's way of doing business. In 2006, Chino Commercial Bancorp was formed as the holding company of Chino Commercial Bank. The holding company's reorganization was completed in order to allow for more alternatives for raising capital and access to debt markets as well as increased structural alternatives for acquisitions, and greater flexibility with respect to engaging in non-banking activities.

At Chino Commercial Bank our goal is to provide customer service that sets us apart from other banks. The Bank has established standards that focus on an unsurpassed level of customer service, which help to achieve financial performance objectives that enhance shareholder value. In the future, the Bank will continue to implement new technologies, and increase collective knowledge, and thereby be able to maintain and expand a distinct competitive advantage.

The common stock of Chino Commercial Bancorp is traded on the Over-the-Counter Markets (OTC Markets) under the stock symbol "CCBC".

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### CHINO OFFICE

MAIN & CORPORATE OFFICES  
14245 Pipeline Avenue  
Chino, CA 91710  
Phone: (909) 393-8880  
Fax: (909) 465-1279



### ONTARIO OFFICE

1551 S. Grove Avenue  
Ontario, CA 91761  
Phone: (909) 230-7600  
Fax: (909) 230-5595



### RANCHO CUCAMONGA OFFICE

8229 Rochester Avenue  
Rancho Cucamonga, CA 91730  
Phone: (909) 204-7300  
Fax: (909) 204-7319

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[www.ChinoCommercialBank.com](http://www.ChinoCommercialBank.com)

# Financial Highlights

## As of and For the Years Ended December 31, 2017 2016 2015

(Dollars in Thousands, except per share data)

### SELECTED BALANCE SHEET DATA:

Total assets	\$ 192,801	\$ 175,092	\$ 161,384
Loans receivable	120,143	107,360	91,325
Deposits	149,126	137,562	130,349
Non-interest bearing deposits	74,767	68,614	74,431
Subordinated notes payable to subsidiary trust	3,093	3,093	3,093
Shareholders' equity	19,504	13,536	12,074

### SELECTED OPERATING DATA:

Interest income	\$ 6,353	\$ 5,768	\$ 5,139
Net income	1,571	1,453	1,327
Basic income per share	1.17	1.18	1.08
Diluted income per share	1.17	1.18	1.08

### PERFORMANCE RATIOS

Return on average assets	0.84%	0.85%	0.88%
Return on average equity	9.85%	11.28%	11.54%
Equity to total assets at the end of the period	10.12%	7.73%	7.48%
Core efficiency ratio	62.92%	64.82%	66.87%
Non-interest expense to average assets	2.66%	2.79%	2.95%

### REGULATORY RATIOS

Average equity to average assets	8.55%	7.57%	7.67%
Leverage capital	13.41%	10.24%	9.79%
Tier I Risk-based	19.76%	15.32%	15.82%
Risk-based capital	18.43%	15.37%	16.15%
Common Tier 1 (CET 1)	19.76%	15.32%	15.82%

## To Our Shareholders



We are very pleased to present you with Chino Commercial Bancorp and Chino Commercial Bank's annual report, for the year 2017. As you will read, this has been a very good year for the consolidated Company and the Bank, which posted record levels of Deposits, Loans, Revenue and Net Profits.

During 2017 the Bank was recognized by the American Bankers Association in their annual ranking of the **Top 200 Publicly Traded Community Banks** in the United States. The list was based upon the Bank's financial performance for the previous year's return on average equity.

The Bank was also recognized by the Findley Reports on Financial Institutions by receiving Findley's highest rating of **"Super Premier Performing Bank"** for the financial performance of the Bank for the previous year.

During 2017 we were able to achieve an increase in **Total Assets** from \$175 million to \$193 million, or an increase in assets of 10%. We were also fortunate in building **Deposits** from \$137 million to \$149 million, an increase of 9%; and in increasing **Loans** from \$107 million to \$120 million, or an increase of 12%. Perhaps equally important was the level of Loan quality attained, with the Bank suffering no credit losses during the year and ending the year with no loan delinquency and no non-accrual loans.

Similar to the increase in Assets, the Bank also realized an \$800 thousand, or 10% gain in gross revenue, up to \$8.5 million, yielding record net profits of \$1.5 million or \$1.17 per diluted share.

During 2017 the Company offered 307,883 shares of common stock to the general public at \$15.00 per share. The stock offering was fully subscribed, and provided a net increase to capital of \$4.4 million. This increase in common stock, if added to the Bank's capital, will allow the Bank to accept approximately 30% more deposits and thereby substantially increase the Bank's lending capacity going forward.

On the economic front, there has been a great deal of discussion lately regarding the trend and direction of interest rates, and the effects of rising interest rates on the banking industry. Fortunately, at year-end, 51% of your Bank's deposits were held in non-interest bearing accounts, a level well above many other banks. As a result, the Bank's net earnings are projected to increase with a moderate rise in interest rates, rather than decline.



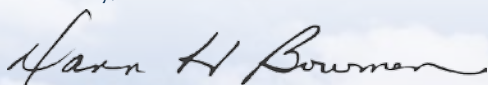
The Bank recently received approval from the Office of the Comptroller of the Currency to open the fourth branch office in Upland. The Bank has also signed a lease on a 3,125 sq. ft. building on Mountain Avenue in Upland, and plans to open the new **Upland branch** office in August of 2018.

Your management and staff are focused on building a solid foundation for future growth of the Bank, through the principles of consistent marketing efforts, sound, conservative credit policies and innovative solutions to our customers' financial needs. We believe that these core values are what set Chino Commercial Bank apart from the others.

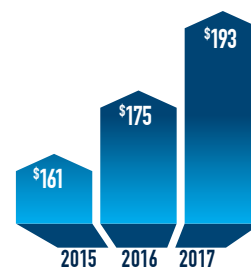
As a locally owned, locally managed independent bank, we feel that Chino Commercial Bank is truly a benefit to not only our customers, but also our shareholders and the community as a whole.

On behalf of your Board of Directors, Management, and Staff, I would like to thank you for your confidence and continued support of the Bank and look forward to another successful year.

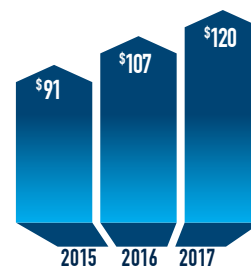
Sincerely,



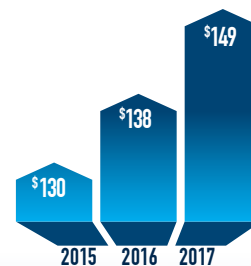
Dann H. Bowman  
President and Chief Executive Officer



*Total Assets*  
(in millions)



*Total Loans*  
(in millions)



*Total Deposits*  
(in millions)



*Shareholders' Equity*  
(in millions)

## Board of Directors



**Dann H. Bowman**  
*President and  
Chief Executive Officer*



**Bernard Wolfswinkel**  
*Chairman of the Board  
Retired*



**H. H. Corky Kindsvater**  
*Vice Chairman of the Board  
Chairman, Audit Committee  
Retired*



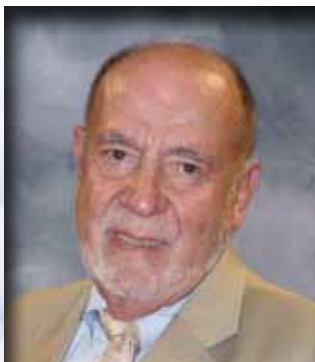
**Linda M. Cooper**  
*President, Inland Empire Escrow*



**Julio Cardenas**  
*President, Century 21 King Realtors*



**Jeanette L. Young**  
*Corporate Secretary  
Realtor, Windermere Real Estate  
Southern California*



**Richard G. Malooly**  
*Principal, RE/MAX Realty 100*



**Thomas A. Woodbury, D.O.**  
*Family Practice  
Physician and Surgeon*



**Michael Di Pietro, C.P.A.**

# 2017 ANNUAL REPORT

*Financial Statements*

# Independent Auditor's Report



**VAVRINEK, TRINE, DAY & CO., LLP**

*Certified Public Accountants*

VALUE THE *difference*

Board of Directors and Shareholders of  
Chino Commercial Bancorp  
Chino, California

We have audited the accompanying consolidated financial statements of Chino Commercial Bancorp and Subsidiary (the Company), which are comprised of the consolidated statements of financial condition as of December 31, 2017 and 2016, and the related consolidated statements of net 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 consolidated 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 the consolidated 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 consolidated financial statements based on our audits. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Chino Commercial Bancorp and Subsidiary as of December 31, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Vavrinek, Trine, Day & Co., LLP*

Rancho Cucamonga, California  
February 23, 2018

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# Consolidated Statements of Financial Condition

DECEMBER 31, 2017 AND 2016

	2017	2016
<b>ASSETS</b>		
Cash and due from banks	\$ 34,157,668	\$ 30,498,888
Interest-bearing deposits in other banks	1,240,000	2,480,000
Investment securities available for sale (Note 3)	3,131,027	3,924,102
Investment securities held-to-maturity (fair value approximates \$21,104,000 in 2017 and \$18,240,000 in 2016) (Note 3)	21,389,552	18,407,741
Loans held for investment, net of allowance for loan losses of \$2,094,723 in 2017, and \$1,845,447 in 2016, (Note 5)	120,142,757	107,359,980
Fixed assets, net (Note 6)	5,875,381	6,000,404
Accrued interest receivable	528,300	295,102
Stock investments, restricted, at cost (Note 4)	2,087,600	1,935,300
Bank owned life insurance	3,386,754	3,285,963
Other assets	861,968	904,338
Total Assets	<u>\$ 192,801,007</u>	<u>\$ 175,091,818</u>
<b>LIABILITIES</b>		
Deposits		
Noninterest-bearing	\$ 74,766,694	\$ 68,613,998
Interest-bearing	74,359,694	68,948,250
Total Deposits	149,126,388	137,562,248
Federal Home Loan Bank advances	20,000,000	20,000,000
Subordinated notes payable to subsidiary trust (Note 8)	3,093,000	3,093,000
Accrued interest payable	65,160	27,902
Other liabilities	1,012,535	872,374
Total Liabilities	<u>173,297,083</u>	<u>161,555,524</u>
Commitments and Contingent Liabilities (Notes 13 and 14)		
<b>SHAREHOLDERS' EQUITY</b>		
Common stock, no par value, 10,000,000 shares authorized, 1,549,420 and 1,231,332 shares issued and outstanding at December 31, 2017 and December 31, 2016, respectively	10,502,557	6,089,466
Retained earnings	9,024,637	7,449,608
Accumulated other comprehensive loss	(23,270)	(2,780)
Total Shareholders' Equity	<u>19,503,924</u>	<u>13,536,294</u>
Total Liabilities and Shareholders' Equity	<u>\$ 192,801,007</u>	<u>\$ 175,091,818</u>

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

# Consolidated Statements of Net Income

FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017	2016
<b>INTEREST INCOME</b>		
Interest and fees on loans	\$ 6,086,085	\$ 5,465,664
Interest on federal funds sold and FRB deposits	359,557	129,875
Interest on time deposits in other financial institutions	26,398	38,596
Interest on investment securities	552,510	545,109
Total Interest Income	7,024,550	6,179,244
<b>INTEREST EXPENSE</b>		
Interest on deposits	366,492	268,336
Interest on borrowings	305,524	142,676
Total Interest Expense	672,016	411,012
Net interest income	6,352,534	5,768,232
Provision for loan losses (Note 5)	204,400	199,950
Net interest income after provision for loan losses	6,148,134	5,568,282
<b>NONINTEREST INCOME</b>		
Service charges on deposit accounts	1,010,349	1,062,812
Other miscellaneous income	268,267	180,347
Dividend income from restricted stock	149,983	221,499
Income from bank-owned life insurance	100,791	102,716
Total Noninterest Income	1,529,390	1,567,374
<b>NONINTEREST EXPENSE</b>		
Salaries and employee benefits	3,051,474	2,882,535
Occupancy and equipment	424,856	416,781
Other expenses	1,483,013	1,455,299
Total Noninterest Expense	4,959,343	4,754,615
Income before income tax expense	2,718,181	2,381,041
Provision for income taxes	1,147,224	927,938
Net Income	\$ 1,570,957	\$ 1,453,103
Basic earnings per share	\$ 1.17	\$ 1.18
Diluted earnings per share	\$ 1.17	\$ 1.18

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

# Consolidated Statement of Comprehensive Income

FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
Net income	\$ 1,570,957	\$ 1,453,103
Other Comprehensive Income (Loss), Net of Tax Effects		
Net unrealized holding income (loss) on securities available-for-sale during the period (tax effects of \$7,428 and \$(9,578) in 2017 and 2016 respectively)	<u>(16,418)</u>	<u>13,700</u>
Total Comprehensive Income	<u>\$ 1,554,539</u>	<u>\$ 1,466,803</u>

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

# Consolidated Statements of Changes in Shareholders' Equity

FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	Number of Shares	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
<b>Balance at December 31, 2015</b>	1,026,349	\$ 6,089,466	\$ 6,000,577	\$ (16,480)	\$ 12,073,563
Net income	-	-	1,453,103	-	1,453,103
Change in unrealized gain on securities available for sale, net of tax	-	-	-	13,700	13,700
Cash in lieu of fractional stock dividends (Note 20)	-	-	(4,072)	-	(4,072)
Stock dividends (Note 20)	<u>204,983</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>Balance at December 31, 2016</b>	1,231,332	\$ 6,089,466	\$ 7,449,608	\$ (2,780)	\$ 13,536,294
Net income	-	-	1,570,957	-	1,570,957
Change in unrealized gain on securities available	-	-	-	(16,418)	(16,418)
Reclassification of stranded tax effects from change in tax rate	-	-	4,072	(4,072)	-
Issuance of common stock, net of offering costs (Note 21)	<u>318,088</u>	<u>4,413,091</u>	<u>-</u>	<u>-</u>	<u>4,413,091</u>
<b>Balance at December 31, 2017</b>	<u>1,549,420</u>	<u>\$ 10,502,557</u>	<u>\$ 9,024,637</u>	<u>\$ (23,270)</u>	<u>\$ 19,503,924</u>

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



# Consolidated Statements of Cash Flows

FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017	2016
<b>Cash Flows from Operating Activities</b>		
Net income	\$ 1,570,957	\$ 1,453,103
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	204,400	199,950
Depreciation and amortization	223,856	213,059
Proceeds from disposal of fixed assets	4,146	
Gain on disposition of fixed assets	(1,794)	-
Amortization of deferred loan fees	129,337	119,776
Net accretion of discount and amortization of premium on securities available-for-sale	27,118	40,120
Income from bank-owned life insurance	(100,791)	(102,716)
Deferred income tax	53,325	(80,232)
Net changes in:		
Accrued interest receivable	(233,198)	100,583
Other assets	(3,527)	(30,636)
Accrued interest payable	37,258	2,673
Other liabilities	144,211	28,683
Net Cash Provided by Operating Activities	2,055,298	1,944,363
<b>Cash Flows from Investing Activities</b>		
Net change in interest-bearing deposits in banks	1,240,000	2,480,000
Loan originations and principal collections, net	(13,116,514)	(16,354,742)
Purchase of fixed assets	(101,184)	(192,017)
Proceeds from principal payments received and maturities of available-for-sale securities	758,909	1,024,017
Purchase of securities held-to-maturity	(7,546,107)	(6,012,500)
Proceeds from principal payments received and maturities of securities held-to-maturity	4,543,447	10,670,972
Purchases of stock investments, restricted	(152,300)	(168,800)
Net Cash Used in Investing Activities	(14,373,749)	(8,553,070)
<b>Cash Flows from Financing Activities</b>		
Net increase in deposits	11,564,140	7,213,527
Proceeds from Federal Home Loan Bank advances	-	5,000,000
Cash paid in lieu of fractional stock dividends	-	(4,072)
Proceeds from issuance of common stock	4,413,091	-
Net Cash Provided by Financing Activities	15,977,231	12,209,455
<b>Net Increase in Cash and Cash Equivalents</b>	3,658,780	5,600,748
<b>Cash and Cash Equivalents at Beginning of Period</b>	30,498,888	24,898,140
<b>Cash and Cash Equivalents at End of Period</b>	\$ 34,157,668	\$ 30,498,888
<b>Supplemental Information</b>		
Interest paid	\$ 634,758	\$ 408,339
Income taxes paid	\$ 1,130,000	\$ 745,000
<b>Supplemental Disclosures of Noncash Investing and Financing Activities</b>		
Stock dividends issued	\$ -	\$ 2,931,257
Change in unrealized gain on securities available-for-sale	\$ 27,898	\$ 23,278

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

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### *Nature of Operations*

Chino Commercial Bank, N.A. (the Bank), a nationally chartered bank, was incorporated on December 8, 1999, and began operations on September 1, 2000, with the opening of its office in Chino, California. The Bank opened a branch office in Ontario, California in January 2006, and opened a branch office in Rancho Cucamonga, California in April 2010.

The Bank provides a variety of commercial banking services to individuals and small businesses primarily in the Inland Empire region of Southern California. Its primary lending products are real estate and commercial loans. Its primary deposit products are non-interest bearing deposits and money market accounts.

Chino Commercial Bancorp (the Company) is a California corporation registered as a bank holding company under the Bank Holding Company Act of 1956, as amended, and is headquartered in Chino, California. The Company was incorporated on March 2, 2006, and acquired all of the outstanding shares of Chino Commercial Bank, N.A. effective July 1, 2006. The Company's principal subsidiary is the Bank, and the Company exists primarily for the purpose of holding the stock of the Bank and of such other subsidiaries it may acquire or establish. The Company's only other direct subsidiary is Chino Statutory Trust I, which was formed on October 25, 2006, solely to facilitate the issuance of capital trust pass-through securities. Chino Commercial Bancorp and the Bank are collectively referred to herein as the Company unless otherwise indicated.

### *Basis of Presentation and Consolidation*

The consolidated financial statements include the accounts of Chino Commercial Bancorp and its subsidiary, Chino Commercial Bank. All significant intercompany balances and transactions have been eliminated in consolidation. The accounting and financial reporting policies the Company follows conform, in all material respects, to accounting principles generally accepted in the United States of America and to general practices within the financial services industry. In consolidating, the Company determines whether it has a controlling financial interest in an entity by first evaluating whether the entity is a voting interest entity or a variable interest entity under accounting principles generally accepted in the United States. Voting interest entities are entities in which the total equity investment at risk is sufficient to enable the entity to finance itself independently and provides the equity holders with the obligation to absorb losses, the right to receive residual returns, and the right to make decisions about the entity's activities. The Company consolidates voting interest entities in which it has all, or at least a majority of, the voting interest. As defined in applicable accounting standards, variable interest entities (VIEs) are entities that lack one or more of the characteristics of a voting interest entity. A controlling financial interest in an entity is present when an enterprise has a variable interest, or a combination of variable interests, that will absorb a majority of the entity's expected losses, receive a majority of the entity's expected residual returns, or both. The enterprise with a controlling financial interest, known as the primary beneficiary, consolidates the VIE. The Company's wholly-owned subsidiary, Chino Statutory Trust I, is a VIE for which the Company is not the primary beneficiary. Accordingly, the accounts of this entity are not included in the Company's consolidated financial statements.

### *Use of Estimates*

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the statement of financial condition and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation of the deferred tax asset.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## *Note 1* SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

### ***Cash and Cash Equivalents***

For purposes of reporting cash flows, cash and cash equivalents include cash, amounts due from banks and Federal funds sold on a daily basis.

### ***Interest-Bearing Deposits in Other Banks***

Interest-bearing deposits in other banks mature in less than two years and are carried at cost.

### ***Investment Securities***

In accordance with U.S. Generally Accepted Accounting Principles (GAAP), investment securities are classified in three categories and accounted for as follows: debt and equity that the Company has the positive intent and ability to hold to maturity are classified as held-to-maturity and are measured at amortized cost; debt and equity securities bought and held principally for the purpose of selling in the near term are classified as trading securities and are measured at fair value, with unrealized gains and losses included in earnings; debt and equity securities not classified as either held-to-maturity or trading securities are deemed as available-for-sale and are measured at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of stockholders' equity. Gains or losses on sales of investment securities are determined on the specific identification method. Premiums and discounts are amortized or accreted using the interest method over the expected lives of the related securities.

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

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

Declines in the fair value of "held-to-maturity" and "available-for-sale" securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the length of time and extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

### ***Loans Held for Sale***

Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value. Fair value is based on commitments on hand from investors or prevailing market prices. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income. There were no loans held for sale at December 31, 2017 and 2016.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

### **Loans**

The Company grants real estate, commercial and consumer loans to customers. A substantial portion of the loan portfolio is represented by real estate loans in the Inland Empire area. The ability of the Company's debtors to honor their contracts is dependent upon the general economic conditions in this area.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off generally are reported at their outstanding unpaid principal balances.

Loans, as reported, have been reduced by unfunded loan commitments, net deferred loan fees, and the allowance for loan losses.

Interest income is accrued daily, as earned, on all loans, except that interest is not accrued on loans that are generally 90 days or more past due. Loans are placed on non-accrual or charged off at an earlier date if collection of principal or interest is considered doubtful. Interest income previously accrued on non-accrual loans is reversed against current period interest income. Interest income on non-accrual loans may be recognized only if the loan is deemed to be fully collectible, and only to the extent of interest payments received. Otherwise, any interest payments received are applied against the loan balance. Loans are returned to accrual status after the borrower's financial condition has improved, when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. Interest recognition policies apply to all loans.

Loan origination fees and costs are deferred and amortized as an adjustment of the loan's yield over the life of the loan using the interest method.

### **Allowance for Loan Losses**

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

The allowance for loan losses is evaluated on a regular basis by management and is based on management's periodic review of the collectability of the loans in light of historical experience, the nature, and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific and general components. The specific component relates to loans that are individually evaluated for impairment. For impaired loans, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers unimpaired loans and is based on historical loss experience adjusted for qualitative factors.



# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

### *Allowance for Loan Losses, continued*

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral-dependent.

### *Troubled Debt Restructuring*

A troubled debt restructuring is a loan which the Company, for reasons related to a borrower's financial difficulties, grants a concession to a borrower that the Company would not otherwise consider. A loan restructuring may take the form of a reduction in the stated interest rate, an extension of the maturity at an interest rate below market, or a reduction in the face amount of the debt or accrued interest, among others. Loans that are renewed at below-market terms are considered to be troubled debt restructurings if the below-market terms represent a concession due to the borrower's troubled financial condition. Troubled debt restructurings are classified as impaired loans and are measured at the present value of estimated future cash flows using the loan's effective rate at inception of the loan. If the loan is considered to be collateral dependent, impairment is measured based on the fair value of the collateral.

### *Loan Portfolio Segments*

Management segregates the loan portfolio into portfolio segments for purposes of developing and documenting a systematic method for determining its allowance for loan losses. The portfolio segments are segregated based on loan types and the underlying risk factors present in each loan type. Such risk factors are periodically reviewed by management and revised as deemed appropriate.

The Company's loan portfolio is segregated into the following portfolio segments.

#### *One-to-Four Family Residential*

This portfolio segment consists of the origination of first mortgage loans and home equity second mortgage loans secured by one-to-four-family owner occupied residential properties located in the Company's market area. The Company has experienced no foreclosures on its owner occupied loan portfolio during recent periods and believes this is due mainly to its conservative lending strategies including its non-participation in "interest only", "Option ARM", "sub-prime" or "Alt-A" loans.

#### *Residential Income*

This portfolio segment consists of the origination of first mortgage loans secured by non-owner occupied residential properties in its market area. Such lending involves additional risks arising from the use of the properties by non-owners.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

### **Commercial Real Estate Loans**

This portfolio segment includes loans secured by commercial real estate, including multi-family dwellings. Loans secured by commercial real estate generally have larger loan balances and more credit risk than one-to-four-family mortgage loans. The increased risk is the result of several factors, including the concentration of principal in a limited number of loans and borrowers, the impact of local and general economic conditions on the borrower's ability to repay the loan, and the increased difficulty of evaluating and monitoring these types of loans.

### **Commercial and Industrial Loans**

This portfolio segment includes commercial business loans secured by assignments of corporate assets and personal guarantees of the business owners. Commercial business loans generally have higher interest rates and shorter terms than one-to-four-family residential loans, but they also may involve higher average balances, increased difficulty of loan monitoring and a higher risk of default since their repayment generally depends on the successful operation of the borrower's business.

### **Other Loans**

This portfolio segment includes loans to individuals for personal purposes, including but not limited to automobile loans. This portfolio segment also includes loans to individuals for overdraft protection and personal lines of credit.

### **Credit Quality Indicators**

The Company's policies, consistent with regulatory guidelines, provide for the classification of loans and other assets that are considered to be of lesser quality as substandard, doubtful, or loss assets. An asset is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets include those assets characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all of the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses make collection or liquidation in full highly questionable and improbable, based on currently existing facts, conditions, and values. Assets (or portions of assets) classified as loss are those considered uncollectible and of such little value that their continuation as assets is not warranted. Assets that do not expose the Company to risk sufficient to warrant classification in one of the aforementioned categories, but which possess potential weaknesses that deserve close attention, are required to be designated as special mention.

When assets are classified as special mention, substandard or doubtful, the Company allocates a portion of the related general loss allowances to such assets as the Company deems prudent. Determinations as to the classification of assets and the amount of loss allowances are subject to review by regulatory agencies, which can require that we establish additional loss allowances. Management regularly reviews the asset portfolio to determine whether any assets require classification in accordance with applicable regulations.

### **Transfer 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 Company, 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 Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

### ***Foreclosed Assets***

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value less cost to sell at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets.

### ***Company Premises and Equipment***

Company premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is provided for in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives. Building improvements are amortized over 39 years or the service lives of the improvements, whichever is shorter. The straight-line method of depreciation is followed for financial reporting purposes, while both accelerated and straight-line methods are followed for income tax purposes.

### ***Bank Owned Life Insurance***

The Company has purchased life insurance policies on certain officers. Company-owned life insurance is recorded at its cash surrender value (or the amount that can be realized).

### ***Income Taxes***

Deferred tax assets and liabilities are recognized for estimated future tax effects attributable to temporary differences between the book bases and tax bases of various assets and liabilities. Valuation allowances are established when necessary to reduce the deferred tax asset to the amount expected to be realized. The current and deferred taxes are based on the provisions of currently enacted tax laws and rates. As changes in tax laws are enacted, deferred tax assets and liabilities are adjusted accordingly through the provision for income taxes.

The Company uses a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Benefits from tax positions are recognized in the financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority that would have full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold are recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold are derecognized in the first subsequent financial reporting period in which that threshold is no longer met. Interest and penalties associated with uncertain tax positions are classified as income tax expense. At December 31, 2017 and 2016, the Company did not have a tax position that failed to meet the more-likely-than-not recognition threshold.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

### **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. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the statement of financial condition, such items, along with net income, are components of comprehensive income.

In February 2018, the FASB issued ASU 2018-02, *Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income* ("AOCI"). ASU 2018-02 allows entities to elect to reclassify stranded tax effects on items within AOCI, resulting from the new tax bill signed into law on December 22, 2017, to retained earnings. The Company/Bank elected to early adopt this new standard in 2017 and recorded a reclassification from AOCI to retained earnings in the amount of \$4,072.

### **Recent Accounting Guidance Not Yet Effective**

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers* (Topic 606). This Update requires an entity to recognize revenue as performance obligations are met, in order to reflect the transfer of promised goods or services to customers in an amount that reflects the consideration the entity is entitled to receive for those goods or services. The following steps are applied in the updated guidance: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when, or as, the entity satisfies a performance obligation. These amendments are effective for public business entities for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period and one year later for nonpublic business entities. Early adoption is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that period. The Company is currently evaluating the effects of ASU 2014-09 on its consolidated financial statements and disclosures, if any.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments-Overall: Recognition and Measurement of Financial Assets and Financial Liabilities* (Subtopic 825-10). Changes made to the current measurement model primarily affect the accounting for equity securities and readily determinable fair values, where changes in fair value will impact earnings instead of other comprehensive income. The accounting for other financial instruments, such as loans, investments in debt securities, and financial liabilities is largely unchanged. The Update also changes the presentation and disclosure requirements for financial instruments including a requirement that public business entities use exit price when measuring the fair value of financial instruments measured at amortized cost for disclosure purposes. This Update is generally effective for public business entities in fiscal years beginning after December 15, 2017, including interim periods within those fiscal years and one year later for nonpublic business entities. The Company is currently evaluating the effects of ASU 2016-01 on its consolidated financial statements and disclosures.



# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

### ***Recent Accounting Guidance Not Yet Effective, continued***

In February 2016, the FASB issued Accounting Standards Update (ASU) 2016-02, *Leases (Topic 842)*. The most significant change for lessees is the requirement under the new guidance to recognize right-of-use assets and lease liabilities for all leases not considered short-term leases, which is generally defined as a lease term of less than 12 months. This change will result in lessees recognizing right-of-use assets and lease liabilities for most leases currently accounted for as operating leases under current lease accounting guidance. The amendments in this Update are effective for interim and annual periods beginning after December 15, 2018, for public business entities and one year later for all other entities. The Company is currently evaluating the effects of ASU 2016-02 on its consolidated financial statements and disclosures.

In June 2016, the FASB issued ASU No. 2016-13, *Measurement of Credit Losses on Financial Instruments (Topic 326)*. This ASU significantly changes how entities will measure credit losses for most financial assets and certain other instruments that aren't measured at fair value through net income. In issuing the standard, the FASB is responding to criticism that today's guidance delays recognition of credit losses. The standard will replace today's "incurred loss" approach with an "expected loss" model. The new model, referred to as the current expected credit loss ("CECL") model, will apply to: (1) financial assets subject to credit losses and measured at amortized cost, and (2) certain off-balance sheet credit exposures. This includes, but is not limited to, loans, leases, held-to-maturity securities, loan commitments, and financial guarantees. The CECL model does not apply to available-for-sale ("AFS") debt securities. For AFS debt securities with unrealized losses, entities will measure credit losses in a manner similar to what they do today, except that the losses will be recognized as allowances rather than reductions in the amortized cost of the securities. As a result, entities will recognize improvements to estimated credit losses immediately in earnings rather than as interest income over time, as they do today. The ASU also simplifies the accounting model for purchased credit-impaired debt securities and loans. ASU 2016-13 also expands the disclosure requirements regarding an entity's assumptions, models, and methods for estimating the allowance for loan and lease losses. In addition, public business entities will need to disclose the amortized cost balance for each class of financial asset by credit quality indicator, disaggregated by the year of origination. ASU No. 2016-13 is effective for interim and annual reporting periods beginning after December 15, 2019, for SEC filers, one year later for non SEC filing public business entities and annual reporting periods beginning after December 15, 2020, for nonpublic business entities and interim periods within the reporting periods beginning after December 15, 2021. Early adoption is permitted for interim and annual reporting periods beginning after December 15, 2018. Entities will apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (i.e., modified retrospective approach). The Company is currently evaluating the provisions of ASU No. 2016-13 for potential impact on its consolidated financial statements and disclosures.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

### ***Recent Accounting Guidance Not Yet Effective, continued***

In January 2017, the FASB issued ASU No. 2017-04, *Intangibles – Goodwill and Other (Topic 350): Simplifying the Accounting for Goodwill Impairment*. This guidance removes Step 2 of the goodwill impairment test, which requires a hypothetical purchase price allocation, and goodwill impairment will simply 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. Entities will continue to have the option to perform a qualitative assessment to determine if a quantitative impairment test is necessary. The amendments in this Update are required for public business entities and other entities that have goodwill reported in their financial statements and have not elected the private company alternative for the subsequent measurement of goodwill. ASU No. 2017-04 is effective for interim and annual reporting periods beginning after December 15, 2021 for public business entities who are not SEC filers and one year later for all other entities. The Company is currently evaluating the effects of ASU 2017-04 on its consolidated financial statements and disclosures.

### ***Subsequent Events***

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued or are available to be issued. The Company 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 Company's financial statements do not reflect 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 issued or are available to be issued.

The Company has evaluated subsequent events through February 23, 2018, which is the date the financial statements were issued or the date the financial statements were available to be issued.

## Note 2 RESTRICTIONS ON CASH AND AMOUNTS DUE FROM BANKS

The Company is required to maintain average cash balances on hand or balances with the Federal Reserve Bank for balances in transaction accounts. The Company was able to maintain sufficient average cash balances to avoid the requirement for a reserve balance with the Federal Reserve Bank at December 31, 2017 and 2016.

The Company maintains cash that may exceed the Federal Deposit Insurance Corporation (FDIC) insured limits. The Company does not expect to incur losses in its cash accounts.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 3 INVESTMENT SECURITIES

The amortized cost and fair values of securities with gross unrealized gains and losses at December 31 are as follows:

<b>December 31, 2017</b>	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>
Securities available-for-sale:				
Mortgage-backed securities	<u>\$ 3,163,650</u>	<u>\$ 13,505</u>	<u>\$ (46,128)</u>	<u>\$ 3,131,027</u>
Securities held-to-maturity:				
Municipal bonds	\$ 330,000	\$ 861	\$ -	\$ 330,861
Federal agency	7,843,550	10,625	(114,794)	7,739,381
Mortgage-backed securities	13,216,002	16,230	(198,141)	13,034,091
	<u>\$ 21,389,552</u>	<u>\$ 27,716</u>	<u>\$ (312,935)</u>	<u>\$ 21,104,333</u>
<b>December 31, 2016</b>				
Securities available-for-sale:				
Mortgage-backed securities	<u>\$ 3,928,827</u>	<u>\$ 20,611</u>	<u>\$ (25,336)</u>	<u>\$ 3,924,102</u>
Securities held-to-maturity:				
Municipal bonds	\$ 330,000	\$ 865	\$ -	\$ 330,865
Federal agency	2,976,202	21,716	(75,994)	2,921,924
Mortgage-backed securities	15,101,539	43,470	(157,596)	14,987,413
	<u>\$ 18,407,741</u>	<u>\$ 66,051</u>	<u>\$ (233,590)</u>	<u>\$ 18,240,202</u>

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 3 INVESTMENT SECURITIES, continued

Unrealized losses and fair values, aggregated by investment category and length of time that individual securities have been in a continuous loss position, are summarized as follows as of December 31:

	Less than 12 Months		Over 12 Months	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
<b>December 31, 2017</b>				
Securities available-for-sale				
Mortgage-backed securities	\$ 1,226,754	\$ (16,247)	\$ 1,525,318	\$ (29,881)
Securities held to maturity				
Federal agency	\$ 4,947,050	\$ (32,232)	\$ 1,808,574	\$ (82,562)
Mortgage-backed securities	5,282,104	(44,775)	7,069,410	(153,366)
	<u>\$ 10,229,154</u>	<u>\$ (77,007)</u>	<u>\$ 8,877,984</u>	<u>\$ (235,928)</u>
<b>December 31, 2016</b>				
Securities available-for-sale				
Mortgage-backed securities	\$ -	\$ -	\$ 1,787,089	\$ (25,336)
Securities held to maturity				
Federal agency	\$ 1,936,124	\$ (75,994)	\$ -	\$ -
Mortgage-backed securities	11,179,167	(157,590)	2,123	(6)
	<u>\$ 13,115,291</u>	<u>\$ (233,584)</u>	<u>\$ 2,123</u>	<u>\$ (6)</u>

At December 31, 2017, the Company had three available-for-sale (AFS) mortgage-backed securities (MBS) with losses less than 12 months, and two AFS MBS with losses greater than 12 months. Also in 2017, the Company held three held-to-maturity (HTM) federal agency securities and seven HTM MBS with losses less than 12 months. In addition, in 2017 the Company held six held-to-maturity (HTM) federal agency securities and one HTM MBS with losses greater than 12 months. In 2016, the Company did not have any available-for-sale (AFS) mortgage-backed securities (MBS) with losses less than 12 months, but did have two AFS MBS with a loss greater than 12 months. Also in 2016, the Company held one security held-to-maturity (HTM) federal agency security and nine HTM MBS with losses less than 12 months. In addition, in 2016 the Company had one HTM MBS with a loss greater than 12 months.

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.



# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 3 INVESTMENT SECURITIES, continued

The unrealized losses at December 31, 2017 and 2016, are attributable to changes in interest rates and not credit quality. The Company has the ability to hold these investments until a recovery of fair value, which may be maturity. Thus, the Company does not consider these investments to be other-than-temporarily impaired as of December 31, 2017 and 2016.

The amortized cost and fair value of investment securities as of December 31, 2017, by contractual maturity are shown below:

	Available-for-Sale		Held-to-Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Within 1 year	\$ -	\$ -	\$ -	\$ -
After 1 year through 5 years	-	-	1,303,133	1,314,618
After 5 years through 10 years	-	-	6,870,417	6,755,624
After 10 years through 17 years	-	-	-	-
Mortgage-backed securities	3,163,650	3,131,027	13,216,002	13,034,091
	<u>\$ 3,163,650</u>	<u>\$ 3,131,027</u>	<u>\$ 21,389,552</u>	<u>\$ 21,104,333</u>

Investment securities with amortized cost totaling \$23,870,767 and estimated fair values totaling \$24,096,669 were pledged to secure borrowings with the Federal Home Loan Bank and the Federal Reserve Bank at December 31, 2017. Investment securities with amortized cost totaling \$18,804,043 and estimated fair values totaling \$18,669,944 were pledged to secure borrowings with the Federal Home Loan Bank at December 31, 2016.

## Note 4 STOCK INVESTMENTS, RESTRICTED

Restricted stock investments include the following at December 31 and are recorded at cost:

	2017	2016
Federal Home Loan (FHLB) stock	\$ 1,872,200	\$ 1,719,900
Federal Reserve Bank stock	165,400	165,400
Pacific Coast Banker's Bank stock	50,000	50,000
	<u>\$ 2,087,600</u>	<u>\$ 1,935,300</u>

As a member of the FHLB system, the Company is required to maintain an investment in FHLB stock in an amount equal to the greater of one percent of its outstanding mortgage loans or 2.7 percent of advances from the FHLB (See Note 10). No ready market exists for FHLB stock, and it has no quoted market value.

All restricted stock is evaluated for impairment based on an estimate of the ultimate recoverability of par value.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 5 LOANS AND ALLOWANCE FOR LOAN LOSSES

The composition of the Company's loans held for investment at December 31 is as follows:

	2017	2016
Real estate loans, commercial	\$ 98,644,472	\$ 85,135,319
Real estate loans, consumer	797,375	2,171,308
Commercial loans	22,819,882	21,816,870
Other loans	340,842	430,289
Total Gross Loans	122,602,571	109,553,786
Allowance for loan losses	(2,094,723)	(1,845,447)
Unearned income and deferred loan fees, net	(365,091)	(348,359)
Loans Held for Investment, Net	\$ 120,142,757	\$ 107,359,980

Changes in the allowance for loan losses by loan portfolio segment for the year ended December 31, 2017 and 2016, are summarized as follows:

	One-to-Four Residential	Residential Income	Commercial Real Estate	Commercial and Industrial	Other	Total
Beginning Balance, January 1, 2017	\$ 24,469	\$ 187,865	\$ 1,450,849	\$ 173,563	\$ 8,701	\$ 1,845,447
Provision (credit) for loan losses	(21,510)	(7,475)	230,131	15,320	(12,066)	204,400
Recoveries	4,532	-	12,862	17,587	9,895	44,876
Ending Balance, December 31, 2017	\$ 7,491	\$ 180,390	\$ 1,693,842	\$ 206,470	\$ 6,530	\$ 2,094,723
Beginning Balance, January 1, 2016	\$ 13,144	\$ 206,552	\$ 1,321,303	\$ 117,545	\$ 8,660	\$ 1,667,204
Provision (credit) for loan losses	11,325	(18,687)	114,185	96,191	(3,064)	199,950
Loans charged off	-	-	-	(63,830)	-	(63,830)
Recoveries	-	-	15,361	23,657	3,105	42,123
Ending Balance, December 31, 2016	\$ 24,469	\$ 187,865	\$ 1,450,849	\$ 173,563	\$ 8,701	\$ 1,845,447

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 5 LOANS AND ALLOWANCE FOR LOAN LOSSES, continued

The following tables present loans and the allowance for loan losses by segment as of December 31:

<u>December 31, 2017</u>	<u>One-to-Four Residential</u>	<u>Residential Income</u>	<u>Commercial Real Estate</u>	<u>Commercial and Industrial</u>	<u>Other</u>	<u>Total</u>
<b>Loans</b>						
Collectively evaluated for impairment	\$ 797,375	\$ 10,349,021	\$ 97,335,209	\$ 12,470,861	\$ 340,842	\$ 121,293,308
Individually evaluated for impairment	-	-	1,309,263	-	-	1,309,263
<b>Balance</b>	<u>\$ 797,375</u>	<u>\$ 10,349,021</u>	<u>\$ 98,644,472</u>	<u>\$ 12,470,861</u>	<u>\$ 340,842</u>	<u>\$ 122,602,571</u>
<b>Allowance for Loan Losses</b>						
Collectively evaluated for impairment	\$ 7,491	\$ 180,390	\$ 1,666,351	\$ 206,470	\$ 6,530	\$ 2,067,232
Individually evaluated for impairment	-	-	27,491	-	-	27,491
<b>Balance</b>	<u>\$ 7,491</u>	<u>\$ 180,390</u>	<u>\$ 1,693,842</u>	<u>\$ 206,470</u>	<u>\$ 6,530</u>	<u>\$ 2,094,723</u>
<u><b>December 31, 2016</b></u>						
<b>Loans</b>						
Collectively evaluated for impairment	\$ 1,649,612	\$ 11,054,996	\$ 83,674,796	\$ 10,761,874	\$ 430,289	\$ 107,571,567
Individually evaluated for impairment	521,696	-	1,460,523	-	-	1,982,219
<b>Balance</b>	<u>\$ 2,171,308</u>	<u>\$ 11,054,996</u>	<u>\$ 85,135,319</u>	<u>\$ 10,761,874</u>	<u>\$ 430,289</u>	<u>\$ 109,553,786</u>
<b>Allowance for Loan Losses</b>						
Collectively evaluated for impairment	\$ 14,818	\$ 187,865	\$ 1,426,285	\$ 173,563	\$ 8,701	\$ 1,811,232
Individually evaluated for impairment	9,651	-	24,564	-	-	34,215
<b>Balance</b>	<u>\$ 24,469</u>	<u>\$ 187,865</u>	<u>\$ 1,450,849</u>	<u>\$ 173,563</u>	<u>\$ 8,701</u>	<u>\$ 1,845,447</u>

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 5 LOANS AND ALLOWANCE FOR LOAN LOSSES, continued

The following tables summarize the loan portfolio at December 31, 2017 and 2016, by credit risk profiles based on internally assigned grades. Information has been updated for each credit quality indicator as of December 31, 2017 and 2016:

	Grade				
	Pass	Special Mention	Substandard	Doubtful	Total
<b>December 31, 2017</b>					
Residential One-to-Four	\$ 797,375	\$ -	\$ -	\$ -	\$ 797,375
Residential income	10,349,021	-	-	-	10,349,021
Commercial real estate	96,994,935	-	1,649,537	-	98,644,472
Commercial and industrial	12,470,861	-	-	-	12,470,861
Other	340,842	-	-	-	340,842
	<u>\$ 120,953,034</u>	<u>\$ -</u>	<u>\$ 1,649,537</u>	<u>\$ -</u>	<u>\$ 122,602,571</u>
<b>December 31, 2016</b>					
Residential One-to-Four	\$ 1,649,612	\$ -	\$ 521,696	\$ -	\$ 2,171,308
Residential income	11,054,996	-	-	-	11,054,996
Commercial real estate	83,339,873	-	1,795,446	-	85,135,319
Commercial and industrial	10,761,874	-	-	-	10,761,874
Other	430,289	-	-	-	430,289
	<u>\$ 107,236,644</u>	<u>\$ -</u>	<u>\$ 2,317,142</u>	<u>\$ -</u>	<u>\$ 109,553,786</u>

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 5 LOANS AND ALLOWANCE FOR LOAN LOSSES, continued

The following tables set forth certain information with respect to the Company's portfolio delinquencies by loan class and amount at December 31, 2017 and 2016:

### Age Analysis of Past Due Loans (by Class)

<b>December 31, 2017</b>	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90-Days	Total Past Due	Current	Total Loans	Non-accrual
Residential One-to-Four	\$ -	\$ -	\$ -	\$ -	\$ 797,375	\$ 797,375	\$ -
Residential income	-	-	-	-	10,349,021	10,349,021	-
Commercial real estate	-	340,375	-	340,375	98,304,097	98,644,472	-
Commercial and industrial	-	-	-	-	12,470,861	12,470,861	-
Other	-	-	-	-	340,842	340,842	-
	<u>\$ -</u>	<u>\$ 340,375</u>	<u>\$ -</u>	<u>\$ 340,375</u>	<u>\$ 122,262,196</u>	<u>\$ 122,602,571</u>	<u>\$ -</u>

<b>December 31, 2016</b>	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90-Days	Total Past Due	Current	Total Loans	Non-accrual
Residential One-to-Four	\$ -	\$ -	\$ 521,696	\$ 521,696	\$ 1,649,612	\$ 2,171,308	\$ 521,696
Residential income	-	-	-	-	11,054,996	11,054,996	-
Commercial real estate	-	262,433	-	262,433	84,872,886	85,135,319	-
Commercial and industrial	-	-	-	-	10,761,874	10,761,874	-
Other	-	-	-	-	430,289	430,289	-
	<u>\$ -</u>	<u>\$ 262,433</u>	<u>\$ 521,696</u>	<u>\$ 784,129</u>	<u>\$ 108,769,657</u>	<u>\$ 109,553,786</u>	<u>\$ 521,696</u>

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 5 LOANS AND ALLOWANCE FOR LOAN LOSSES, continued

The following tables are summaries of impaired loans by loan class at December 31, 2017 and 2016:

### Impaired Loans (by Class)

December 31, 2017	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
<b>With an Allowance Recorded:</b>					
Commercial real estate	\$ 1,309,263	\$ 1,309,263	\$ 27,491	\$ 1,323,587	\$ 79,457
<b>December 31, 2016</b>					
<b>With an Allowance Recorded:</b>					
Residential One-to-Four	\$ 521,696	\$ 521,696	\$ 9,651	\$ 529,812	\$ 11,546
Commercial real estate	1,460,523	1,460,523	24,564	1,464,317	90,792
	\$ 1,982,219	\$ 1,982,219	\$ 34,215	\$ 1,994,129	\$ 102,338

There were no non-accrual loans as of December 31, 2017. The Company had one loan on non-accrual status as of December 31, 2016.

There were no loans serviced for others at December 31, 2017 and 2016.

Certain loans are pledged as collateral for available borrowings with the FHLB. Pledged loans totaled \$73,004,172 and \$64,994,997 at December 31, 2017 and 2016, respectively.

### Troubled Debt Restructurings

No loans were modified in troubled debt restructuring during the years ended December 31, 2017 and 2016.

## Note 6 FIXED ASSETS

Company premises and equipment consisted of the following at December 31:

	2017	2016
Land	\$ 1,868,422	\$ 1,868,422
Building	3,212,729	3,212,729
Furniture, fixture and equipment	1,337,515	1,374,717
Building and leasehold improvements	1,423,981	1,423,981
Automobile	53,283	39,544
	<u>7,895,930</u>	<u>7,919,393</u>
Less accumulated depreciation and amortization	<u>2,020,549</u>	<u>1,918,989</u>
Total premises and equipment	<u>\$ 5,875,381</u>	<u>\$ 6,000,404</u>

Depreciation and amortization expense for years ended December 31, 2017 and 2016, amounted to \$223,856 and \$213,059, respectively.



# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 7 DEPOSITS

Interest-bearing and noninterest-bearing deposits consist of the following:

	2017	2016
NOW accounts	\$ 3,280,445	\$ 4,894,404
Savings and money market	51,647,670	53,144,332
Time certificate of deposit accounts under \$250,000	5,727,789	6,471,260
Time certificate of deposit accounts over \$250,000	13,703,790	4,438,254
Total interest-bearing deposits	74,359,694	68,948,250
Total noninterest-bearing deposits	74,766,694	68,613,998
Total Deposits	<u>\$ 149,126,388</u>	<u>\$ 137,562,248</u>

At December 31, 2017, the scheduled maturities of time deposits were as follows:

	2017
Within 1 year	\$ 19,325,113
After 1 year through 3 years	106,466
	<u>\$ 19,431,579</u>

## Note 8 SUBORDINATED NOTES PAYABLE TO SUBSIDIARY TRUST

On October 25, 2006, Chino Statutory Trust I (the Trust), a newly formed Connecticut statutory business trust and a wholly-owned subsidiary of the Company, issued an aggregate of \$3.0 million of principal amount of Capital Securities (the Trust Preferred Securities) and \$93,000 in Common Securities. The securities issued by the Trust are fully guaranteed by the Company with respect to distributions and amounts payable upon liquidation, redemption, or repayment. The entire proceeds to the Trust from the sale of the Trust Preferred Securities were used by the Trust to purchase \$3,000,000 in principal amount of the Junior Subordinated Deferrable Interest Debentures due December 15, 2036 issued by the Company (the Subordinated Debt Securities). The Company issued an additional \$93,000 in principal amount of the Junior Subordinated Deferrable Interest Debentures due December 15, 2036, in exchange for its investment in the Trust's Common Securities. During 2006 and 2007 the Company used approximately \$522,000 and \$2,478,000, respectively, from the proceeds of \$3.0 million to repurchase and retire Company stock. There was no cost to the Trust associated with the issuance.

The Subordinated Debt Securities bear interest equal to LIBOR (adjusted quarterly) plus 1.68 percent. At December 15, 2017, LIBOR rate was 1.32000 percent, resulting in an interest rate of 3.00000 percent from December 16, 2017 to March 14, 2018. At December 15, 2016, LIBOR rate was 0.96344 percent, resulting in an interest rate of 2.6434 percent from December 16, 2016 to March 16, 2017.

As of December 31, 2017 and 2016, accrued interest payable to the Trust amounted to \$4,358 and \$3,525, respectively. Interest expense for Trust Preferred Securities amounted to \$87,391 and \$72,035, for the years ended December 31, 2017 and 2016, respectively.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 9 RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Company has granted loans to certain officers, directors and companies with which it is associated. All such loans and commitments to lend were made under terms that are consistent with the Company's normal lending policies.

Aggregate related party loan transactions were as follows as of and for the years ended December 31:

	2017	2016
Balance, January 1	\$ 134,698	\$ 861,243
Advances	373,751	164,228
Repayments, net of borrowings	(353,375)	(890,773)
Balance as of December 31	<u>\$ 155,074</u>	<u>\$ 134,698</u>

Deposits from related parties held by the Company at December 31, 2017 and 2016, amounted to \$9,397,051 and \$7,906,510, respectively.

## Note 10 FEDERAL HOME LOAN BANK BORROWINGS

As a member of the FHLB, the Company may borrow funds collateralized by securities or qualified loans up to 35 percent of its asset base. The Company has a line of credit of \$49,338,850 and \$43,755,300 at December 31, 2017 and 2016, respectively. Total FHLB advances outstanding at December 31, 2017 and 2016 were \$20,000,000.

## Note 11 FEDERAL FUNDS LINE OF CREDIT

The Company had a total of \$5.5 million in Federal funds lines of credit with various banks at December 31, 2017 and 2016. There were no borrowings outstanding at December 31, 2017 and 2016.

Lines of Credit	2017	2016
PCBB	\$ 3,500,000	\$ 3,500,000
Zions	2,000,000	2,000,000
	<u>\$ 5,500,000</u>	<u>\$ 5,500,000</u>

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 12 INCOME TAXES

The asset and liability method is used in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax basis of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

The following is a summary of the provision for income taxes for the years ended December 31:

	2017	2016
Currently payable:		
Federal	\$ 829,407	\$ 747,311
State	264,492	260,859
	<u>1,093,899</u>	<u>1,008,170</u>
Deferred Taxes		
Federal	(92,030)	(65,531)
State	(28,416)	(14,701)
Deferred tax asset adjustment for enacted change in tax rate	<u>173,771</u>	<u>-</u>
	<u>53,325</u>	<u>(80,232)</u>
	<u>\$ 1,147,224</u>	<u>\$ 927,938</u>

Income tax expense for 2017 includes a downward adjustment of net deferred tax assets in the amount of \$173,771, recorded as a result of the enactment of H.R.1 Tax Cuts and Jobs Act on December 22, 2017. The Act reduced the corporate Federal tax rate from 34% to 21% effective January 1, 2018.

A comparison of the federal statutory income tax rates to the Company's effective income tax rates at December 31 follows:

	2017	2016
Statutory Federal tax rate	34.0%	34.0%
Increase (Decrease) Resulting From:		
State taxes, net of Federal tax benefit	7.2	7.2
Tax-exempt earnings on life insurance policies	(1.3)	(1.5)
Tax-exempt interest from municipal bonds	(0.2)	(0.4)
Tax impact from enacted change in tax rate	6.4	-
Other, net	<u>(3.9)</u>	<u>(0.3)</u>
Effective Tax Rate	<u>42.2%</u>	<u>39.0%</u>

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 12 INCOME TAXES, continued

The components of the net deferred tax asset, included in other assets on the statements of financial condition, were as follows at December 31:

	<u>2017</u>	<u>2016</u>
Deferred tax assets		
Allowance for loan losses	\$ 426,698	\$ 512,096
Start-up expense	1,877	3,359
State tax	56,141	91,646
Deferred compensation and benefits	137,824	190,658
Nonaccrual interest	-	12,411
Off balance sheet reserve	9,697	11,194
Unrealized loss on securities available for sale	9,352	1,924
	<u>641,589</u>	<u>823,288</u>
Deferred tax liabilities		
FHLB stock dividends	(18,423)	(25,645)
Depreciation and amortization	(110,395)	(132,822)
Deferred loan costs	(87,562)	(104,465)
Other	(21,311)	(114,633)
	<u>(237,691)</u>	<u>(377,565)</u>
	<u>\$ 403,898</u>	<u>\$ 445,723</u>

The Company records interest and penalties related to uncertain tax positions as part of income tax expense. There was no penalty or interest expense recorded as of December 31, 2017 and 2016. The Company does not expect the total amount of unrecognized tax benefits to significantly increase or decrease within the next twelve months.

Tax years ended December 31, 2014 through December 31, 2016; remain subject to examination by the Internal Revenue Service. Tax years ended December 31, 2013 through December 31, 2016, remain subject to examination by the California Franchise Tax Board.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 13 OFF BALANCE SHEET ACTIVITIES

### *Credit-Related Financial Instruments*

The Company is a party to credit-related 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 commitments to grant loans, undisbursed lines of credit, standby letters of credit, and commercial letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet.

The Company's exposure to credit loss is represented by the contractual amount of these commitments. The Company uses the same credit policies in making commitments as it does for on-balance-sheet instruments. At December 31, 2017 and 2016, the following financial instruments were outstanding:

	2017	2016
Undisbursed loans	\$ 13,098,363	\$ 10,073,137

Commitments to grant loans 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 may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Included in undisbursed commitments at December 31, 2017, was \$5,602,084 of commitments at fixed rates. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the customer. Collateral held varies but may include accounts receivable, inventory, equipment, income-producing commercial properties, residential properties, and properties under construction.

Undisbursed lines of credit are commitments for possible future extensions of credit to existing customers. These lines of credit are sometimes unsecured and may not necessarily be drawn upon to the total extent to which the Company is committed.

Standby and commercial letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. There were no standby letters of credit at December 31, 2017 and 2016.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 14 OTHER COMMITMENTS AND CONTINGENCIES

### *Operating Lease Commitments*

The Company signed a lease agreement for its Upland branch location on December 15, 2017. The agreement has a commencement date in 2018 and expires in 2023, and contains two 5 year options to renew. Future minimum lease payments are as follows:

December 31,	Amount
2018	\$ 40,873
2019	46,640
2020	50,448
2021	59,405
2022	61,187
Thereafter	5,112
Total	<u>\$ 263,665</u>

No rent expense was incurred in 2017 related to this lease agreement.

### *Employment Agreement*

The Company entered into a three-year employment agreement with a key officer expiring on June 30, 2018. The agreement provides for an annual base salary plus an incentive bonus equal to 5 percent of the Bank's net income. In addition, the key officer may receive a discretionary bonus determined by the Board of Directors. Employment may be terminated for cause, as defined, without incurring obligations. In the event of termination without cause, the key officer is entitled to severance compensation equal to at least six months' salary.

## Note 15 CONCENTRATION RISK

The Company grants commercial, real estate and installment loans to businesses and individuals primarily in the Inland Empire area. Most loans are secured by business assets, and commercial and residential real estate. Real estate and construction loans held for investment represented 94 percent and 84 percent of total loans held for investment at December 31, 2017 and 2016, respectively. The Company has no concentration of loans with any one customer or industry.

Deposits from escrow companies represented 8 percent and 9 percent of total deposits on December 31, 2017 and 2016, respectively. Four escrow companies accounted for 7 percent and 8 percent of total deposits for the years ended December 31, 2017 and 2016, respectively.

## Note 16 EMPLOYEE BENEFIT PLAN

The Company has a 401(k) savings and retirement plan (the Plan) that includes substantially all employees. Employees may contribute up to 100 percent of their compensation subject to certain limits based on Federal tax law. The Company has implemented the Plan based on safe harbor provisions. Under the Plan, the Company will match 100 percent of an employee's contribution up to the first 3 percent of compensation, and 50 percent of an employee's contribution up to the next 2 percent of compensation. Matching contributions will immediately be 100 percent vested. For the years ended December 31, 2017 and 2016, the Company matching contributions attributable to the Plan amounted to \$70,290 and \$69,951, respectively.



# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 17 SALARY CONTINUATION AGREEMENTS

The Company has entered into salary continuation agreements, which provide for payments to certain officers at the age of retirement. At December 31, 2017 and 2016, \$347,893 and \$347,795, respectively, of deferred compensation related to these agreements were included in other liabilities.

The plans are funded through life insurance policies that generate a cash surrender value to fund the future benefits.

## Note 18 REGULATORY MATTERS

*Minimum Regulatory Requirements* - The Company is subject to various regulatory capital requirements administered by the Federal banking regulators. 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 Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company must meet specific capital guidelines that involve quantitative measures of the Company's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Company on January 1, 2015, with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Under the Basel III rules, the Company must hold a capital conservation buffer above the adequately capitalized risk-based capital ratios. The capital conservation buffer is being phased in from 0.0 percent for 2015 to 2.50 percent by 2019. The capital conservation buffer for 2017 is 1.25 percent. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital.

Quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum capital ratios as set forth in the following table. The Company's actual capital amounts and ratios as of December 31, 2017 and 2016, are also presented in the table. Management believes, as of December 31, 2017 and 2016, that the Company met all capital adequacy requirements to which it is subject.

As of December 31, 2017 and 2016, the most recent notification from the OCC categorized the Company as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Company must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the following table.

There are no conditions or events since notification that management believes have changed the Company's category.

Federal and State banking regulations place certain restrictions on dividends and other capital distributions paid to shareholders. The total amount of dividends that may be paid at any date is generally limited to the lesser of the Bank's retained earnings or net income for the last three years, subject to minimum capital requirements.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 18 REGULATORY MATTERS, continued

Capital ratios for December 31, 2017 and 2016, are set forth below:

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in Thousands)						
<b>As of December 31, 2017:</b>						
Total Capital to Total Risk-Weighted Assets:						
Consolidated	\$ 24,268	18.43%	\$ 10,537	8.00%	\$ 13,171	10.00%
Bank	22,767	17.30%	10,531	8.00%	13,164	10.00%
Tier 1 Capital to Total Risk-Weighted Assets:						
Consolidated	\$ 26,031	19.76%	\$ 7,903	6.00%	\$ 10,537	8.00%
Bank	21,116	16.04%	7,898	6.00%	10,531	8.00%
Common Tier 1 (CET1)						
Consolidated	\$ 26,031	19.76%	\$ 5,927	4.50%	\$ 8,561	6.50%
Bank	21,116	16.04%	5,924	4.50%	8,556	6.50%
Tier 1 Capital to Average Assets:						
Consolidated	\$ 26,031	13.41%	\$ 7,762	4.00%	\$ 9,702	5.00%
Bank	21,116	10.89%	7,759	4.00%	9,699	5.00%
<b>As of December 31, 2016:</b>						
Total Capital to Total Risk-Weighted Assets:						
Consolidated	\$ 18,110	15.37%	\$ 9,427	8.00%	\$ 11,784	10.00%
Bank	17,722	15.05%	9,419	8.00%	11,773	10.00%
Tier 1 Capital to Total Risk-Weighted Assets:						
Consolidated	\$ 18,052	15.32%	\$ 7,070	6.00%	\$ 9,427	8.00%
Bank	16,245	13.80%	7,064	6.00%	9,419	8.00%
Common Tier 1 (CET1)						
Consolidated	\$ 18,052	15.32%	\$ 5,303	4.50%	\$ 7,659	6.50%
Bank	16,245	13.80%	5,298	4.50%	7,653	6.50%
Tier 1 Capital to Average Assets:						
Consolidated	\$ 18,052	10.24%	\$ 7,049	4.00%	\$ 8,811	5.00%
Bank	16,245	9.22%	7,045	4.00%	8,806	5.00%

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 19 EARNINGS PER SHARE

Basic earnings per share represent income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflect additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate solely to outstanding stock options, and are determined using the treasury stock method. There were no common stock equivalents that are dilutive at December 31, 2017 and 2016. The weighted-average number of shares for basic and diluted earnings was 1,347,358 in 2017 and 1,231,332 in 2016.

## Note 20 DIVIDENDS

During 2016, the Board of Directors declared and the Company issued a 20 percent stock dividend to shareholders of record on June 6, 2016. As a matter of accommodation, cash dividends were issued to holders of fractional shares. The stock dividend consisted of 204,983 shares of stock issued on June 27, 2016, at which time the trading price was \$14.20 per share. The 20 percent stock dividend was treated as a split for reporting purposes. The Company did not declare a dividend in 2017.

The Company's ability to declare dividends depends primarily upon dividends it receives from the Company, as a bank holding company that currently has no significant assets other than its equity interest in the Company. The Company's dividend practices in turn depend upon legal restrictions, the Company's earnings, financial position, current and anticipated capital requirements, and other factors deemed relevant by the Company's Board of Directors at that time.

## Note 21 CAPITAL OFFERING

During 2017 the Company completed a public offering with the sale of 307,883 shares of common stock at an offering price of \$15.00 per share. Total shares issued were 318,088, which includes 10,205 bonus shares. Proceeds of \$4,413,091, net of offering expenses of \$205,154, were received.

## Note 22 OTHER OPERATING EXPENSES

The following sets forth the breakdown of other operating expenses for the years ended December 31:

	2017	2016
Data processing fees	\$ 222,288	\$ 381,321
Deposit products and services	129,716	114,279
Professional fees	196,082	184,900
Regulatory assessments	150,753	141,000
Advertising and marketing	127,371	76,074
Directors' fees and expenses	120,214	108,013
Other expenses	536,589	449,712
Total Non-Interest Expenses	\$ 1,483,013	\$ 1,455,299

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 23 FAIR VALUE MEASUREMENTS

*Fair Value Measurements Using Fair Value Hierarchy* - Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The tables below present information about the Company's assets measured at fair value on a recurring and non-recurring basis as of December 31, 2017 and 2016, and indicate the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value. No liabilities were measured at fair value at December 31, 2017 and 2016.

The fair value hierarchy is as follows:

Level 1 Inputs - Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 Inputs - Quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 Inputs - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

The following section describes the valuation methodologies used for assets measured at fair value on a recurring basis, as well as the general classification of such instruments pursuant to the valuation hierarchy.

Financial assets measured at fair value on a recurring basis include the following:

*Securities Available for Sale* - The securities classified as available for sale are reported at fair value utilizing Level 2 inputs. For these securities, the Company 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.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 23 FAIR VALUE MEASUREMENTS, continued

The table below presents the balance of investment securities available for sale at December 31, 2017 and 2016, the fair value of which is measured on a recurring basis:

	Fair Value Measurements Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
<b>December 31, 2017</b>				
Securities Available-for-Sale				
Mortgage-backed securities	\$ -	\$ 3,131,027	\$ -	\$ 3,131,027
<b>December 31, 2016</b>				
Securities Available-for-Sale				
Mortgage-backed securities	\$ -	\$ 3,924,102	\$ -	\$ 3,924,102

Certain assets are measured at fair value on a nonrecurring basis; that is, the assets are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). There were no assets measured at fair value on a non-recurring basis as of December 31, 2017 and 2016.

**Impaired Loans** - Collateral-dependent impaired loans are carried at the fair value of the collateral less estimated costs to sell. The fair value of collateral is determined based on appraisals. In some cases, adjustments are made to the appraised values for various factors including age of the appraisal, age of comparables included in the appraisal, and known changes in the market and in the collateral. When significant adjustments were based on unobservable inputs, the resulting fair value measurement has been categorized as a Level 3 measurement. Otherwise, collateral-dependent impaired loans are categorized under Level 2.

There were no collateral dependent impaired loans at December 31, 2017 and 2016.

Impaired loans that are not collateral-dependent are carried at the present value of expected future cash flows discounted at the loan's effective interest rate. Troubled debt restructurings are also carried at the present value of expected future cash flows. However, expected cash flows for troubled debt restructurings are discounted using the loan's original effective interest rate rather than the modified interest rate. Since cash flows are not discounted to present value using a market interest rate, the measurement of impairment for these loans is not a fair value measurement.

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 23 FAIR VALUE MEASUREMENTS, continued

**Fair Value of Financial Instruments** - The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair value is based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Discount rates on loans can vary significantly depending on the risk profile of the loan and the borrower's deposit relationship with the Company. Accordingly, the fair value estimates may not be realized in the immediate settlement of the instrument. Accounting Standards Codification (ASC) 825, Financial Instruments, excludes certain financial instruments and all non-financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company.

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

**Cash and Cash Equivalents** - The carrying amounts reported in the balance sheet for cash and short-term instruments approximate their fair values.

**Interest-Bearing Deposits in Other Banks** - The fair value of interest-bearing deposits in other banks is estimated by discounting future cash flows using current offering rates for deposits with similar characteristics.

**Investment Securities** - Fair values for investment securities are based on quoted market prices.

**Stock Investments** - The carrying values of stock investments approximate fair value based on the redemption provisions of the stock.

**Loans** - The fair value of performing fixed rate loans is estimated by discounting future cash flows using the Company's current offering rate for loans with similar characteristics. The fair value of performing adjustable rate loans is considered to be the same as book value. The fair value of non-performing loans is estimated at the fair value of the related collateral or, when, in management's opinion, foreclosure upon the collateral is unlikely, by discounting future cash flows using rates that take into account management's estimate of excess credit risk.

**Bank Owned Life Insurance** - The fair values are based on current cash surrender values at each reporting date provided by the insurers.

**TruPS Common Securities** - Included in other assets are certain long-term investments carried at cost, which approximates estimated fair value, unless an impairment analysis indicates the need for adjustments.

**Commitments to Extend Credit and Standby Letters of Credit** - The Company does not generally enter into long-term fixed rate commitments or letters of credit. These commitments are generally at prices that are at currently prevailing rates. These rates are generally variable and, therefore, there is no interest rate risk exposure. Accordingly, the fair market value of these instruments is equal to the carrying amount of their net deferred fees. The net deferred fees associated with these instruments are not material. The Company has no unusual credit risk associated with these instruments.



# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 23 FAIR VALUE MEASUREMENTS, continued

**Deposits** - The fair value of deposits is determined as follows: (i) for saving accounts, money market accounts and other deposits with no defined maturity, fair value is the amount payable on demand; (ii) for variable-rate term deposits, fair value is considered to be the same as book value; and (iii) for fixed-rate term deposits, fair value is estimated by discounting future cash flows using current offering rates for deposits with similar characteristics.

**FHLB Advances** - The fair value of long-term debt is based on rates currently available to the Bank for debt with similar terms and remaining maturities.

**Accrued Interest** - The carrying amounts of accrued interest approximate fair value.

**Subordinated Debentures** - The fair values of subordinated debentures are determined based on the current market value for like instruments of a similar maturity and structure.

The estimated fair values and related carrying amounts of the Company's financial instruments at December 31, 2017, are as follows:

		Fair Value Measurements at December 31, 2017			
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Financial Assets:					
Cash and cash equivalents	\$ 34,157,668	\$ 34,157,668	\$ -	\$ -	\$ 34,157,668
Interest-bearing deposits with other banks	1,240,000	-	1,240,000	-	1,240,000
Investment securities available-for-sale	3,131,027	-	3,131,027	-	3,131,027
Investment securities held-to-maturity	21,389,552	-	21,104,333	-	21,104,333
Stock investments	2,087,600	-	-	2,087,600	2,087,600
Loans, net	120,142,757	-	-	120,113,277	120,113,277
Accrued interest receivable	528,300	-	528,300	-	528,300
Bank owned life insurance	3,386,754	-	3,386,754	-	3,386,754
Trups common securities	93,000	-	93,000	-	93,000
Financial Liabilities:					
Deposits					
Noninterest-bearing demand deposits	\$ 74,766,694	\$ 74,766,694	\$ -	\$ -	\$ 74,766,694
Interest-bearing deposits	74,359,694	-	69,947,000	-	69,947,000
FHLB advances	20,000,000	-	20,000,000	-	20,000,000
Accrued interest payable	65,160	-	65,160	-	65,160
Subordinated notes payable	3,093,000	-	3,093,000	-	3,093,000

# Notes to Consolidated Financial Statements

DECEMBER 31, 2017 AND 2016

## Note 23 FAIR VALUE MEASUREMENTS, continued

The estimated fair values and related carrying amounts of the Company's financial instruments at December 31, 2016, are as follows:

		Fair Value Measurements at December 31, 2016			
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Financial Assets:					
Cash and cash equivalents	\$ 30,498,888	\$ 30,498,888	\$ -	\$ -	\$ 30,498,888
Interest-bearing deposits with other banks	2,480,000	-	2,480,000	-	2,480,000
Investment securities available-for-sale	3,924,102	-	3,924,102	-	3,924,102
Investment securities held-to-maturity	18,407,741	-	18,240,202	-	18,240,202
Stock investments	1,935,300	-	-	1,935,300	1,935,300
Loans, net	107,359,980	-	-	107,643,553	107,643,553
Accrued interest receivable	295,102	-	295,102	-	295,102
Bank owned life insurance	3,285,963	-	3,285,963	-	3,285,963
Trups common securities	93,000	-	93,000	-	93,000
Financial Liabilities:					
Deposits					
Noninterest-bearing demand deposits	\$ 68,613,998	\$ 68,613,998	\$ -	\$ -	\$ 68,613,998
Interest-bearing deposits	68,948,250	-	63,780,000	-	63,780,000
FHLB advances	20,000,000	-	20,000,000	-	20,000,000
Accrued interest payable	27,902	-	27,902	-	27,902
Subordinated notes payable	3,093,000	-	3,093,000	-	3,093,000

## Branch Locations

*Coming Soon* – UPLAND OFFICE – 300 N Mountain Avenue, Upland, CA 91786



### CHINO OFFICE

MAIN & CORPORATE OFFICES  
14245 Pipeline Avenue  
Chino, CA 91710  
Phone: (909) 393-8880  
Fax: (909) 465-1279



### ONTARIO OFFICE

1551 S. Grove Avenue  
Ontario, CA 91761  
Phone: (909) 230-7600  
Fax: (909) 230-5595



### RANCHO CUCAMONGA OFFICE

8229 Rochester Avenue  
Rancho Cucamonga, CA 91730  
Phone: (909) 204-7300  
Fax: (909) 204-7319



*Business app*

[www.ChinoCommercialBank.com](http://www.ChinoCommercialBank.com)



*Personal app*

## Market Makers

### D.A. DAVIDSON

42605 Moonridge Road • P.O. Box 1688 • Big Bear Lake, California 92315  
(800) 288-2811

### ROBERT W. BAIRD & CO. INCORPORATED

1211 SW 5th Avenue, Suite 1400 • Portland, Oregon 97204  
(800) 754-2841

### STOCK SYMBOL: "CCBC"

Common Stock (OTC Markets)

We've got you covered!

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