



PRESIDIO
BANK

FINANCIAL STATEMENTS

December 31, 2015 and 2014

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Presidio Bank

Financial Statements Years Ended December 31, 2015 and 2014

Presidio Bank

Financial Statements
Years Ended December 31, 2015 and 2014

Presidio Bank

Contents

Independent Auditor's Report	3
Financial Statements	
Balance Sheets	5
Statements of Income	6
Statements of Comprehensive Income	7
Statements of Changes in Shareholders' Equity	8
Statements of Cash Flows	9
Notes to Financial Statements	10 - 43



Independent Auditor's Report

The Shareholders and Board of Directors
Presidio Bank
San Francisco, California

We have audited the accompanying financial statements of Presidio Bank, which comprise the balance sheets as of December 31, 2015 and the related statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

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

Other Matter

The 2014 financial statements of Presidio Bank were audited by other auditors, whose report dated March 16, 2015 expressed an unmodified opinion on those statements.

BDO USA, LLP

March 18, 2016

Financial Statements

Presidio Bank

Balance Sheets

<i>December 31,</i>	2015	2014
Assets		
Cash and due from banks	\$ 109,386,709	\$ 110,263,158
Available-for-sale investment securities, at fair value	10,626,905	10,640,544
Held-to-maturity investment securities, at amortized cost	631,450	664,223
Federal Reserve Bank stock, at cost	1,827,650	1,378,400
Federal Home Loan Bank stock, at cost	1,947,800	1,708,900
Loans, less allowance for loan losses of \$6,300,886 in 2015 and \$5,172,046 in 2014	517,513,593	410,568,585
Premises and equipment, net	1,230,695	1,476,630
Deferred tax assets, net	3,964,347	3,414,000
Accrued interest receivable and other assets	7,138,292	2,212,475
Total Assets	\$ 654,267,441	\$ 542,326,915
Liabilities and Shareholders' Equity		
Deposits:		
Non-interest bearing	\$ 210,998,103	\$ 164,353,390
Interest bearing	368,352,648	317,338,335
Total deposits	579,350,751	481,691,725
Subordinated debt	9,617,894	9,574,225
Accrued interest payable and other liabilities	7,745,752	3,243,579
Total Liabilities	596,714,397	494,509,529
Commitments and Contingencies (Note 10)		
Shareholders' Equity:		
Preferred stock, no par value; 10,000,000 shares authorized:		
Series A, noncumulative, \$1,000 per share liquidation preference 0 and 6,544 shares issued and outstanding in 2015 and 2014, respectively	-	6,544,000
Series B, noncumulative, \$1,000 per share liquidation preference; 0 and 325 shares issued and outstanding in 2015 and 2014, respectively	-	325,000
Common stock, no par value; 30,000,000 shares authorized; 5,476,695 and 4,203,391 shares issued and outstanding in 2015 and 2014, respectively	58,795,777	44,207,446
Accumulated deficit	(1,100,407)	(3,166,933)
Accumulated other comprehensive loss, net of tax	(142,326)	(92,127)
Total Shareholders' Equity	57,553,044	47,817,386
Total Liabilities and Shareholders' Equity	\$ 654,267,441	\$ 542,326,915

See accompanying notes to financial statements.

Presidio Bank
Statements of Income

<i>Years Ended December 31,</i>	2015	2014
Interest and Dividend Income:		
Interest and fees on loans	\$ 20,827,931	\$ 19,200,614
Interest on due from banks and other overnight deposits	291,630	173,334
Interest on investment securities	153,587	156,013
Dividend income	309,800	188,987
Total interest and dividend income	21,582,948	19,718,948
Interest Expense:		
Interest on deposits	818,858	796,526
Interest on subordinated debt	843,669	213,144
Total interest expense	1,662,527	1,009,670
Net interest income	19,920,421	18,709,278
Provision for loan losses	1,128,840	301,074
Net interest income after provision for loan losses	18,791,581	18,408,204
Non-Interest Income:		
Service charges and fees	599,397	619,073
Other non-interest income	101,744	82,084
Total non-interest income	701,141	701,157
Non-Interest Expenses:		
Salaries and employee benefits	9,667,905	8,550,036
Occupancy and equipment	1,764,787	1,583,202
Other	3,894,667	3,592,971
Total non-interest expenses	15,327,359	13,726,209
Income before income taxes	4,165,363	5,380,153
Provision for income taxes	1,623,343	2,234,079
Net Income	\$ 2,542,020	\$ 3,146,074
Basic Earnings Per Common Share	\$ 0.43	\$ 0.65
Diluted Earnings Per Common Share	\$ 0.41	\$ 0.63

See accompanying notes to financial statements.

Presidio Bank

Statements of Comprehensive Income

<i>Years Ended December 31,</i>	2015	2014
Net Income	\$ 2,542,020	\$ 3,146,074
Other comprehensive income (loss):		
Unrealized gains (losses) on available-for-sale securities:		
Unrealized holding gain (loss) arising during the year	(85,748)	127,772
Tax effect	35,549	(50,798)
Other comprehensive income (loss)	(50,199)	76,974
Comprehensive Income	\$ 2,491,821	\$ 3,223,048

See accompanying notes to financial statements.

Presidio Bank

Statements of Changes in Shareholders' Equity Years Ended December 31, 2015 and 2014

	Preferred Stock - Series A		Preferred Stock - Series B		Common Stock		Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity (Deficit)
	Shares	Amount	Shares	Amount	Shares	Amount			
Balance, December 31, 2013	6,544	\$ 6,486,222	325	\$ 325,000	4,169,744	\$ 43,540,149	\$ (5,898,579)	\$ (169,101)	\$ 44,283,691
Accretion of discount on Series A preferred stock	-	57,778	-	-	-	-	(57,778)	-	-
Preferred dividends	-	-	-	-	-	-	(356,650)	-	(356,650)
Restricted stock awards granted	-	-	-	-	29,247	-	-	-	-
Stock options exercises	-	-	-	-	4,400	42,748	-	-	42,748
Share-based compensation expense	-	-	-	-	-	624,549	-	-	624,549
Net income	-	-	-	-	-	-	3,146,074	-	3,146,074
Other comprehensive income	-	-	-	-	-	-	-	76,974	76,974
Balance, December 31, 2014	6,544	6,544,000	325	325,000	4,203,391	44,207,446	(3,166,933)	(92,127)	47,817,386
Preferred dividends	-	-	-	-	-	-	(475,494)	-	(475,494)
Redemption of preferred stock	(6,544)	(6,544,000)	(325)	(325,000)	-	-	-	-	(6,869,000)
Issuance of common stock	-	-	-	-	1,000,000	11,657,977	-	-	11,657,977
Restricted stock awards granted	-	-	-	-	42,804	-	-	-	-
Stock options exercises	-	-	-	-	230,500	2,194,613	-	-	2,194,613
Share-based compensation expense	-	-	-	-	-	661,905	-	-	661,905
Tax benefits of stock options	-	-	-	-	-	73,836	-	-	73,836
Net income	-	-	-	-	-	-	2,542,020	-	2,542,020
Other comprehensive income	-	-	-	-	-	-	-	(50,199)	(50,199)
Balance, December 31, 2015	-	\$ -	-	\$ -	5,476,695	\$ 58,795,777	\$ (1,100,407)	\$ (142,326)	\$ 57,553,044

See accompanying notes to financial statements.

Presidio Bank
Statements of Cash Flows

<i>Years Ended December 31,</i>	2015	2014
Cash Flows from Operating Activities:		
Net income	\$ 2,542,020	\$ 3,146,074
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of premiums on investment securities, net	38,401	12,688
Amortization of debt issuance costs	43,669	7,282
Depreciation and amortization	365,519	352,993
Provision for loan losses	1,128,840	301,074
Loss on disposal of equipment	-	5,475
Deferred loan origination fees (costs), net	281,637	92,003
Share-based compensation expense	661,905	624,549
(Benefit) provision for deferred income taxes	(550,347)	(326,000)
(Increase) decrease in accrued interest receivable and other assets	(4,010,464)	(484,340)
Increase in accrued interest payable and other liabilities	4,502,174	720,898
Net Cash Provided by Operating Activities	5,003,354	4,452,696
Cash Flows from Investing Activities:		
Purchases of available-for-sale investment securities	(5,821,667)	-
Proceeds from principal payments on investment securities	5,743,929	274,682
Redemption (purchases) of FRB stock	(449,250)	20,750
Purchases of FHLB stock	(238,900)	(342,700)
Net increase in loans	(108,355,484)	(42,407,571)
Cash invested in low income housing fund	(879,805)	-
Purchases of premises and equipment	(119,583)	(757,821)
Proceeds from sale of premises and equipment	-	1,530
Net Cash Used in Investing Activities	(110,120,760)	(43,211,130)
Cash Flows from Financing Activities:		
Net increase in demand, interest-bearing and savings deposits	109,183,502	72,562,593
Net increase (decrease) in time deposits	(11,524,477)	11,970,660
Issuance of subordinated debentures, net of debt issuance costs of \$436,696	-	9,563,304
Redemption of Series A and B preferred stock, net of discount	(6,869,000)	-
Payment of dividends on preferred stock	(475,494)	(356,650)
Proceeds from issuance of common stock	11,657,977	-
Excess tax benefits from exercised stock options	73,836	-
Proceeds from the exercise of stock options	2,194,613	42,748
Net Cash Provided by Financing Activities	104,240,957	93,782,655
Increase (Decrease) in Cash and Cash Equivalents	(876,449)	55,024,221
Cash and Cash Equivalents at Beginning of Year	110,263,158	55,238,937
Cash and Cash Equivalents at End of Year	\$ 109,386,709	\$ 110,263,158
Supplemental Disclosures of Cash Flow Information:		
Cash paid for interest expense	\$ 1,656,168	\$ 1,011,650
Cash paid for income taxes	\$ 1,710,000	\$ 2,535,000

See accompanying notes to financial statements.

Presidio Bank

Notes to Financial Statements

1. The Business of Presidio Bank

Presidio Bank (the "Bank") is a state-chartered bank and a member of the Federal Reserve System (the "Fed"). The Bank is subject to regulation by the Fed, the California Department of Business Oversight (the "DBO"), and the Federal Deposit Insurance Corporation (the "FDIC"). The Bank's deposits are insured by the FDIC up to applicable legal limits.

The Bank is headquartered in San Francisco, California and also has branch offices in Walnut Creek, San Rafael, San Mateo and Palo Alto, California. The Bank provides traditional commercial banking services to its target market throughout Northern California, consisting of small to medium sized businesses, along with the owners and executives of those firms.

2. Summary of Significant Accounting Policies

General

The accounting and reporting policies of the Bank conform with accounting principles generally accepted in the United States of America and prevailing practices within the banking industry.

Subsequent Events

Management has reviewed all events occurring from December 31, 2015 through March 18, 2016, the date the financial statements were available to be issued.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Operating Segments

While the Bank's executive officers monitor the revenue streams of the Bank's various products and services, operations are managed and financial performance is evaluated on a Bank-wide basis. Operating results are not reviewed by senior management to make resource allocation or performance decisions. Accordingly, all of the Bank's financial service operations are considered by management to be aggregated in one reportable operating segment.

Reclassifications

Certain reclassifications have been made to the prior year's balances in order to conform to the classifications used in the current year. None of the reclassifications had an impact on the prior year's net income or shareholder's equity.

Presidio Bank

Notes to Financial Statements

Cash and Cash Equivalents

For the purpose of the statement of cash flows, cash and cash equivalents consist of cash and due from banks as well as other overnight deposits. Net cash flows are reported for customer loan and deposit transactions.

Federal Reserve Bank Stock and Federal Home Loan Bank Stock

As a member of both the Federal Reserve Bank (the "FRB") and the Federal Home Loan Bank (the "FHLB"), the Bank is required to maintain a minimum level of investment in the capital stocks of the FRB and FHLB. These investments are considered restricted equity securities and are carried at par value. The Bank may request redemption at par value in excess of the amount required to be held. Stock redemptions are made at the discretion of the FRB and FHLB. Both cash and stock dividends are reported as income.

Investment Securities

Investment securities are classified into the following categories:

- Available-for-sale securities reported at fair value, with unrealized gains and losses excluded from earnings and reported, net of taxes, as accumulated other comprehensive income (loss) within shareholders' equity.
- Held-to-maturity securities, which management has the positive intent and ability to hold, reported at amortized cost, adjusted for the accretion of discounts and amortization of premiums.

Management determines the appropriate classification of its investments at the time of purchase and may only change the classification in certain limited circumstances. All transfers between categories are accounted for at fair value. There were no transfers between categories during the years ended December 31, 2015 and 2014.

Gains or losses on the sale of investment securities are computed using the specific identification method. Interest earned on investment securities is reported in interest income, net of applicable adjustments for accretion of discounts and amortization of premiums.

An investment security is impaired when its carrying value is greater than its fair value. Investment securities that are impaired are evaluated on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation to determine whether such a decline in their fair value is other than temporary. Management utilizes criteria such as the magnitude and duration of the decline and the intent and ability of the Bank to retain its investment in the securities for a period of time sufficient to allow for an anticipated recovery in fair value, in addition to the reasons underlying the decline, to determine whether the loss in value is other than temporary. The term "other than temporary" is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value is determined to be other than temporary, and management does not intend to sell the security or it is more likely than not that the Bank will not be required to sell the security before recovery, only the portion of the impairment loss representing credit exposure is recognized as a charge to earnings, with the balance

Presidio Bank

Notes to Financial Statements

recognized as a charge to other comprehensive income. If management intends to sell the security or it is more likely than not that the Bank will be required to sell the security before recovering its forecasted cost, the entire impairment loss is recognized as a charge to earnings.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are recorded at the principal balances outstanding, net of deferred loan origination fees and costs and the allowance for loan losses. Interest is accrued daily based upon outstanding loan balances. However, when in the opinion of management, loans are considered to be impaired and the future collectibility of interest and principal is in serious doubt, loans are placed on nonaccrual status and the accrual of interest income is suspended. Any interest accrued but unpaid is charged against income. Payments received are applied to reduce principal to the extent necessary to ensure collection. Subsequent payments on these loans, or payments received on nonaccrual loans for which the ultimate collectibility of principal is not in doubt, are applied first to earned but unpaid interest and then to principal. Generally, loans are placed on non-accrual status when they are 90 days past due. Past due status is based on the contractual terms of the loan. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. The Bank's policy for placing loans on nonaccrual status, recording payments received on nonaccrual loans resuming accrual of interest and determining past due or delinquency status does not differ by portfolio segment.

All loans are evaluated and considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due (including both principal and interest) in accordance with the contractual terms of the loan agreement. The policy for recognizing interest on impaired loans is the same as the policy described above and does not differ by portfolio segment.

Substantially all loan origination and commitment fees, net of direct loan origination costs, and purchase premiums and discounts on loans are deferred and recognized as an adjustment of yield, to be amortized to interest income over the contractual term of the loan. The unamortized balance of deferred fees and costs is reported as a component of net loans.

The Bank services loans that have been participated to other financial institutions totaling approximately \$20,198,000 and \$22,923,000 at December 31, 2015 and 2014, respectively.

Allowance for Loan Losses

The allowance for loan losses is an estimate of probable credit losses inherent in the Bank's loan portfolio that have been incurred as of the balance-sheet date. The allowance is established through a provision for loan losses which is charged to expense. Additions to the allowance are expected to maintain the adequacy of the total allowance after credit losses and loan growth. Credit exposures determined to be uncollectible are charged against the allowance. Cash received on previously charged off amounts is recorded as a recovery to the allowance. The policy for charging off loans and recording recoveries on previously charged off loans does not differ by portfolio segment. The overall allowance consists of two primary components, specific reserves related to impaired loans and general reserves related to loans that are not considered impaired.

Presidio Bank

Notes to Financial Statements

Loans determined to be impaired are individually evaluated for impairment. When a loan is impaired, the Bank measures impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate, except that as a practical expedient, it may measure impairment based on a loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. A loan is collateral dependent if the repayment of the loan is expected to be provided solely by the underlying collateral. The policy for measuring impaired loans does not differ by portfolio segment.

A restructuring of a debt constitutes a troubled debt restructuring ("TDR") if the Bank, for economic or legal reasons related to the debtor's financial difficulties, grants a concession to the debtor that it would not otherwise consider. TDR loans typically present an elevated level of credit risk as the borrowers are not able to perform according to the original contractual terms. Loans that are reported as TDRs are considered impaired and measured for impairment as described above.

The determination of the general reserve for loans that are not considered impaired is based on estimates made by management, to include, but not limited to, consideration of historical losses by portfolio segment experienced by the Bank since inception and a peer group for the trailing ten years, internal asset classifications, and qualitative factors to include economic trends in the Bank's service areas, industry experience and trends, geographic concentrations, estimated collateral values, the Bank's underwriting policies, the character of the loan portfolio, and probable losses inherent in the portfolio taken as a whole.

The Bank maintains a separate allowance for each loan type ("portfolio segment"). These portfolio segments include commercial, construction and land development, commercial real estate and consumer loans. The allowance for loan losses attributable to each portfolio segment, which includes both impaired loans and loans that are not impaired, is combined to determine the Bank's overall allowance, which is included on the balance sheet.

The Bank assigns a risk rating to all loans and periodically performs detailed reviews of all such loans over a certain threshold to identify credit risks and to assess the overall collectability of the portfolio. These risk ratings are also subject to examination by independent specialists engaged by the Bank and the Bank's regulators. During these internal reviews, management monitors and analyzes the financial condition of borrowers and guarantors, trends in the industries in which borrowers operate and the fair values of collateral securing these loans. These credit quality indicators are used to assign a risk rating to each individual loan. The risk ratings can be grouped into five major categories, defined as follows:

Pass - A pass loan is a strong, satisfactory or acceptable credit with no existing or known potential weaknesses deserving of management's close attention.

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

Presidio Bank

Notes to Financial Statements

Substandard - A substandard loan is not adequately protected by the current sound worth and paying capacity of the borrower or the value of the collateral pledged, if any. Loans classified as substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. Well defined weaknesses include a project's lack of marketability, inadequate cash flow or collateral support, failure to complete construction on time or the project's failure to fulfill economic expectations. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful- Loans classified doubtful have all the weaknesses inherent in those classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable.

Loss- Loans classified as loss are considered uncollectible and charged off immediately.

The general reserve component of the allowance for loan losses also consists of reserve factors that are based on management's assessment of the following for each portfolio segment: (1) inherent credit risk, (2) historical losses and (3) other qualitative factors. These reserve factors are inherently subjective and are driven by the repayment risk associated with each portfolio segment described below.

Commercial- Commercial loans generally possess a lower inherent risk of loss than real estate portfolio segments because these loans are generally underwritten to existing cash flows of operating businesses. Debt coverage is provided by business cash flows and economic trends influenced by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans.

Construction and land development- Construction and land development loans generally possess a higher inherent risk of loss than other real estate portfolio segments. A major risk arises from the necessity to complete projects within specified cost and time lines. Trends in the construction industry significantly impact the credit quality of these loans, as demand drives construction activity. In addition, trends in real estate values significantly impact the credit quality of these loans, as property values determine the economic viability of construction projects.

Commercial real estate - Commercial real estate loans generally possess a higher inherent risk of loss than other real estate portfolio segments, except land and construction loans. Adverse economic developments or an overbuilt market impact commercial real estate projects and may result in troubled loans. Trends in vacancy rates of commercial properties impact the credit quality of these loans. High vacancy rates reduce operating revenues and the ability for properties to produce sufficient cash flow to service debt obligations.

Consumer and other- The consumer and other category includes primarily residential real estate and home equity lines of credit. The degree of risk in this portfolio segment depends primarily on the loan amount in relation to collateral value, the interest rate and the borrower's ability to repay in an orderly fashion. These loans generally possess a lower inherent risk of loss than other real estate portfolio segments. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Weak economic trends indicate that the borrowers' capacity to repay their obligations may be deteriorating.

Presidio Bank

Notes to Financial Statements

Although management believes the allowance to be adequate, ultimate losses may vary from its estimates. At least quarterly, the Board of Directors reviews the adequacy of the allowance, including consideration of the relative risks in the portfolio, current economic conditions and other factors. If the Board of Directors and management determine that changes are warranted based on those reviews, the allowance is adjusted. In addition, the Bank's primary regulators, the FRB and DBO as an integral part of their examination process, review the adequacy of the allowance. These regulatory agencies may require additions to the allowance based on their judgment about information available at the time of their examinations.

Allowance for Credit Losses on Off-Balance Sheet Credit Exposures

The Bank also maintains a separate allowance for off-balance-sheet commitments. Management estimates anticipated losses using historical data and utilization assumptions. The allowance for off-balance-sheet commitments is included in accrued interest payable and other liabilities on the balance sheet.

Bank Premises and Equipment

Bank premises and equipment are carried at cost. Depreciation is determined using the straight-line method over the estimated useful lives of the related assets. The useful lives of furniture, fixtures and equipment are estimated to be 3 to 7 years. Leasehold improvements are amortized over the lesser of the respective lease term (including renewal periods that are reasonably assured) or their useful lives, which are generally 7 to 10 years.

Certain operating leases contain scheduled and specified rent increases or incentives in the form of tenant improvement allowances or credits. The scheduled rent increases are recognized on a straight-line basis over the lease term as an increase in the amount of rental expense recognized each period. Lease incentives are capitalized at the inception of the lease and amortized on a straight-line basis over the lease term as a reduction of rental expense. Amounts accrued in excess of amounts paid related to the scheduled rent increases are included in accrued interest payable and other liabilities on the balance sheet.

When assets are sold or otherwise disposed of, the cost and related accumulated depreciation or amortization are removed from the accounts, and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is charged to expense as incurred.

Income Taxes

Deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the reported amount of assets and liabilities and their tax basis. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. A valuation allowance is recognized if, based on the weight of available evidence, management believes it is more likely than not that some portion or all of the deferred tax assets will not be realized.

At December 31, 2015 and 2014, the Bank did not have a material reserve for uncertain tax positions. The Bank uses a comprehensive model for recognizing, measuring, presenting and disclosing in the financial statements tax positions taken or expected to be taken on a tax return. A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount

Presidio Bank

Notes to Financial Statements

recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded. Interest expense and penalties associated with unrecognized tax benefits, if any, are classified as income tax expense in the statement of operations. The Bank has not accrued for any interest or penalties as of December 31, 2015 or December 31, 2014 because it does not have any significant unrecognized tax benefits.

Earnings Per Share

Basic earnings per share, which excludes dilution, is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding for the period. Net income available to common shareholders differs from net income due to amounts for dividends paid on preferred stock, accretion of discounts on preferred stock and gain on settlement of preferred stock. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock, such as stock options, result in the issuance of common stock which share in the earnings of the Bank. The treasury stock method is applied to determine the dilutive effect of stock options in computing diluted earnings per share.

Share-Based Compensation

The Bank has one share-based compensation plan, the Presidio Bank 2006 Stock Option Plan (the "Plan"), which has been approved by its shareholders and permits the grant of stock options and restricted stock for up to 1,625,000 shares of the Bank's common stock, of which 5,011 shares were available for future grant at December 31, 2015. The Plan is designed to attract and retain employees and directors. The amount, frequency, and terms of share-based awards may vary based on competitive practices, the Bank's operating results and government regulations. New shares are issued upon option exercise of stock options and vesting of restricted stock. The Plan does not provide for the settlement of awards in cash. The Plan requires that the option price may not be less than the fair market value of the stock at the date the option is granted, and that the stock must be paid in full at the time the option is exercised.

The Bank has issued four types of awards under the plan: Organizer options, which were granted to founders and organizers and were fully vested upon the granting of the awards; service-based options, that generally vest over four or five year periods; restricted stock and restricted stock units, certain of which vest only if the Bank meets or exceeds certain pre-determined financial goals and objectives.

The Bank accounts for share-based compensation using a fair-value based method that requires that share-based compensation expense be recorded for all stock options and restricted stock awards and restricted stock units that are ultimately expected to vest as the requisite service is rendered.

Management estimates the fair value of each option award as of the date of grant using a Black-Scholes-Merton option pricing formula. Expected volatility is based on historical volatility of similar entities over a preceding period commensurate with the expected term of the option because the Bank's common stock has been publicly traded for a shorter period than the expected term for the options. The "simplified" method described in the Securities and Exchange Commission's Staff Accounting Bulletin No. 110 is used to determine the expected term of option awards. The risk-free rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Expected dividend yield was not considered in the option pricing formula because the Bank has not paid dividends and has no current plans to do so in the future.

Presidio Bank

Notes to Financial Statements

Option awards granted to employees and members of the Bank's board of directors are accounted for as stock compensation, whereby compensation expense is generally based on the grant date fair value of the option awards. Option awards granted to board advisory members are accounted for as equity-based payments to non-employees, whereby the fair value of the option awards is re-measured each reporting period and the expense recorded is ultimately based on the fair value of the option awards on the vesting date.

The fair values of restricted stock awards and restricted stock units are determined using the fair value of the underlying shares on the date of the grant. In addition to the assumptions discussed above, management makes estimates regarding pre-vesting forfeitures that will impact total compensation expense recognized under the Plan.

Adoption of New Financial Accounting Standards

In January 2014, the FASB amended existing guidance to clarify when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan such that the loan should be derecognized and the real estate recognized. These amendments clarify that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either: (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure, or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Amendments in this standard can be applied using a modified retrospective or prospective transition method. This amendment was effective for fiscal year ended, December 15, 2014. The adoption of this standard was not material to the Bank's operating results or financial condition.

In June 2014, the FASB amended existing guidance related to the accounting for share-based payments when the terms of an award provide that a performance target could be achieved after the requisite service period. These amendments require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. A reporting entity should apply existing guidance in Topic 718, Compensation - Stock Compensation, as it relates to awards with performance conditions that affect vesting to account for such awards. The total amount of compensation cost recognized during and after the requisite service period should reflect the number of awards that are expected to vest and should be adjusted to reflect those awards that ultimately vest. The requisite service period ends when the employee can cease rendering service and still be eligible to vest in the award if the performance target is achieved. These amendments are effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. Early adoption is permitted. Entities may apply the amendments in this amendment either: (a) prospectively to all awards granted or modified after the effective date; or (b) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. The adoption of this standard was not material to the Bank's operating results or financial condition.

Presidio Bank

Notes to Financial Statements

In August 2014, the FASB amended existing guidance related to the classification of certain government guaranteed mortgage loans, including those guaranteed by the FHA and the VA, upon foreclosure. It requires that a mortgage loan be derecognized and a separate other receivable be recognized upon foreclosure if the following conditions are met: 1) The loan has a government guarantee that is not separable from the loan before foreclosure; 2) At the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim; and 3) At the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. These amendments are effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. The amendments may be applied using a prospective transition method in which a reporting entity applies the guidance to foreclosures that occur after the date of adoption, or a modified retrospective transition using a cumulative-effect adjustment (through a reclassification to a separate other receivable) as of the beginning of the annual period of adoption. Prior periods should not be adjusted. A reporting entity must apply the same method of transition as elected under ASU 2014-04. The adoption of this standard did not have a material effect on the Bank's operating results or financial condition.

Newly Issued Not Yet Effective Accounting Standards

In May 2014 the FASB amended existing guidance related to revenue from contracts with customers. This amendment supersedes and replaces nearly all existing revenue recognition guidance, including industry specific guidance, establishes a new control-based revenue recognition model, changes the basis for deciding when revenue is recognized over time or at a point in time, provides new and more detailed guidance on specific topics and expands and improves disclosures about revenue. In addition, this amendment specifies the accounting for some costs to obtain or fulfill a contract with a customer. This amendment is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. Early adoption is not permitted. The amendments should be applied retrospectively to all periods presented or retrospectively with the cumulative effect recognized at the date of initial application. The Bank is currently evaluating the impact of this new accounting standard on the financial statements.

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update No. 2014-09 that created the new Topic 606 ("Topic 606") in the Accounting Standards Codification ("ASC"). Topic 606 also included numerous conforming additions and amendments to other Topics within the ASC. Topic 606 established new rules that affect the amount and timing of revenue recognition for contracts with customers, but does not affect lease accounting and reporting. As such, adoption of these provisions will not affect the Company's lease revenues but may affect the reporting of other of the Company's revenues. On August 12, 2015, the FASB deferred the effective date of the provisions included in Topic 606 to years commencing after December 15, 2017. Topic 606 can be adopted early for years commencing after December 15, 2016, and may be reflected using either a full retrospective method or a simplified method that does not recast prior periods but does disclose the effect of the adoption on the current period financial statements. The Company has not yet determined either the potential impact on its financial statements or the method it will elect to use in connection with the adoption of the changes included in Topic 606.

Presidio Bank

Notes to Financial Statements

In August 2014, the FASB issued ASU 2014-15, "Presentation of Financial Statements - Going Concern," which added Subtopic 205-40 to the ASC ("Subtopic 205-40"). Subtopic 205-40 requires management to determine whether substantial doubt exists concerning the reporting entity's ability to continue as a going concern, in which case certain disclosures will be required. Subtopic 205-40 affects financial statement presentation but not methods of accounting, and is effective on a prospective basis for annual periods ending after December 15, 2016 and each reporting period thereafter, although early adoption is permitted. The Company has not early adopted Subtopic 205-40.

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments - Overall - Recognition and Measurement of Financial Assets and Financial Liabilities," which added and amended several ASC Subtopics ("ASU 2016-01"). ASU 2016-01 affects recognition, measurement and disclosures concerning financial instruments, including changes to (i) accounting for equity investments, (ii) accounting for financial liabilities accounted for under the fair value option, (iii) measurement of fair value of financial assets and liabilities based on the exit price notion in ASC 820, and (iv) presentation and disclosure requirements for financial instruments. ASU 2016-01 is effective on a prospective basis for annual periods beginning after December 15, 2017 and each reporting period thereafter. The Company has not yet determined the impact of adopting ASU 2016-01 on its financial statements.

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)" ("ASU 2016-02"). ASU 2016-02 is effective for public companies for years beginning after December 15, 2018, although early adoption is permitted. ASU 2016-02 substantially modifies lessee accounting for leases, requiring that lessees recognize lease assets and liabilities for leases extending beyond one year. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement.

The new standard requires a lessor to classify leases as sales-type, finance or operating. A lease will be treated as a sale if it transfers all of the risks and rewards, as well as control of the underlying asset, to the lessee. If risks and rewards are conveyed without the transfer of control, the lease is treated as a financing. If the lessor doesn't convey risks and rewards or control, an operating lease results. A modified retrospective transition approach is required for lessors for sales-type, direct financing, and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company has not yet determined the effect of adopting ASU 2016-02 on its financial statements.

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Presidio Bank

Notes to Financial Statements

3. Investment Securities

Available-for-Sale Investment Securities

The following table summarizes the amortized cost and estimated fair value of available-for-sale investment securities at December 31, 2015 and 2014 and the corresponding amounts of gross unrealized gains and losses recognized in accumulated other comprehensive loss:

	2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
Mortgage-backed securities-residential	\$ 6,682,805	\$ -	\$ (116,702)	\$ 6,566,103
Asset-backed securities-student loan	4,188,688	-	(127,886)	4,060,802
	\$ 10,871,493	\$ -	\$ (244,588)	\$ 10,626,905

	2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
Mortgage-backed securities-residential	\$ 5,818,348	\$ 5,753	\$ (114,312)	\$ 5,709,789
Asset-backed securities-student loan	4,981,036	-	(50,281)	4,930,755
	\$ 10,799,384	\$ 5,753	\$ (164,593)	\$ 10,640,544

Net unrealized losses on available-for-sale investment securities totaling \$244,588 were recorded net of a related tax benefit of \$102,262 as accumulated other comprehensive loss at December 31, 2015. There were no sales or transfers of available-for-sale investment securities during the years ended December 31, 2015 and 2014. Available-for-sale residential mortgage-based securities with an amortized cost of \$5,929,127 and fair value of \$5,820,707 mature in 2019. Available-for-sale residential mortgage-based securities with an amortized cost of \$753,678 and fair value of \$745,396 mature in 2028. Available-for-sale student loan asset-backed securities mature in 2035. Expected maturities may differ from contractual maturities because the issuers of the securities may have the right to call or prepay obligations.

Presidio Bank

Notes to Financial Statements

Held-to-Maturity Investment Securities

The following table summarizes the amortized cost and fair value of held-to-maturity investment securities at December 31, 2015 and 2014 and the corresponding amounts of gross unrecognized gains and losses:

	2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
Mortgage-backed securities-residential	\$ 631,450	\$ -	\$ -	\$ 631,450

	2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
Mortgage-backed securities-residential	\$ 664,223	\$ -	\$ (199)	\$ 664,024

Held-to-maturity investment securities are recorded at amortized cost, adjusted for the amortization of premiums or accretion of discounts. There were no sales, calls or transfers of held-to-maturity investment securities for the years ended December 31, 2015 and 2014. Held-to-maturity investment securities mature in 2019.

At December 31, 2015 and 2014, the residential mortgage-backed securities held by the Bank were issued by a U.S. government-sponsored entities, Fannie Mae and Freddie Mac, institutions which the government has affirmed its commitment to support. At December 31, 2015, the student loan asset-backed security held by the Bank was guaranteed by eligible guarantee agencies and reinsured by the U.S. Department of Education for at least 97% of defaulted principal and accrued interest. The structure of this security also incorporates other forms of credit enhancement. Because management believes the declines in the fair values of its residential mortgage-backed securities and student loan asset backed security are attributable to changes in interest rates and not credit quality, and because the Bank does not have the intent to sell these securities and it is likely that it will not be required to sell the securities before their anticipated recovery, the Bank does not consider these securities to be other-than-temporarily impaired at December 31, 2015 and 2014.

At December 31, 2015, the Bank held available-for-sale asset backed securities with net unrealized losses of \$127,886 which had been in a continuous net unrealized loss position for more than 12 months. At December 31, 2014, the Bank held available-for-sale mortgage-backed securities and asset-backed securities with net unrealized losses of \$114,312 and \$50,281, respectively which had been in a continuous net unrealized loss position for more than 12 months. At December 31, 2015,

Presidio Bank

Notes to Financial Statements

the Bank held available-for-sale mortgage-backed securities with net unrealized losses of \$116,702 which had been in a continuous net unrealized loss position for less than 12 months. At December 31, 2014, the Bank held no securities with net unrealized losses which had been in a continuous net unrealized loss position for less than 12 months.

4. Loans

Outstanding loans at December 31, 2015 and 2014 are summarized below:

<i>December 31,</i>	2015	2014
Commercial	\$ 153,852,972	\$ 133,857,147
Construction and land development	42,492,983	14,100,301
Commercial real estate	224,219,589	195,777,189
Consumer and other	104,142,352	72,617,775
	524,707,896	416,352,412
Deferred loan origination fees, net	(893,417)	(611,781)
Allowance for loan losses	(6,300,886)	(5,172,046)
	\$ 517,513,593	\$ 410,568,585

Salaries and employee benefits totaling \$706,887 and \$592,800 were deferred as loan origination costs for the years ended December 31, 2015 and 2014, respectively.

As of December 31, 2015, the Bank had a recorded investment in a troubled debt restructuring of \$1,113,546, had no allocated specific reserves for that loan and had not committed to lend additional amounts on that loan. During 2015, payments applied to the balance of the loan reduced the balance to below the net liquidation value of the collateral, eliminating the need for any specific reserve.

As of December 31, 2014, the Bank had a recorded investment in a troubled debt restructuring of \$1,190,905, had allocated \$112,455 of specific reserves for that loan and had not committed to lend additional amounts on that loan. The modification occurred during the year ended December 31, 2014 and included an extension of the maturity date and reduced payments in the near term, but did not change the Bank's recorded investment in the loan or impact the allowance or provision for loan losses because the loan was already considered impaired before it was modified and the specific allowance did not change as a result of the modification.

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Presidio Bank

Notes to Financial Statements

5. Loans and Allowance for Loan Losses

The following table shows the allocation of the allowance for loan losses for the years ended December 31, 2015 and 2014 by portfolio segment and the allocation of the allowance for loan losses at December 31, 2015 and 2014 by portfolio segment and impairment methodology:

Allowance for Loan Losses 2015	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Unallocated	Total
Beginning balance allocated to portfolio segments	\$ 1,822,090	\$ 246,959	\$ 2,034,729	\$ 868,268	\$ 200,000	\$ 5,172,046
Provision for loan losses	493,011	411,438	81,789	342,602	(200,000)	1,128,840
Losses charged to allowance	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-
Ending balance allocated to portfolio segments	\$ 2,315,101	\$ 658,397	\$ 2,116,518	\$ 1,210,870	\$ -	\$ 6,300,886
Ending balance: individually evaluated for impairment	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Ending balance: collectively evaluated for impairment	\$ 2,315,101	\$ 658,397	\$ 2,116,518	\$ 1,210,870	\$ -	\$ 6,300,886

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Presidio Bank

Notes to Financial Statements

Allowance for Loan Losses 2014	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Unallocated	Total
Beginning balance allocated to portfolio segments	\$ 1,951,325	\$ 450,788	\$ 1,673,974	\$ 624,394	\$ 166,625	\$ 4,867,106
Provision for loan losses	80,232	(203,829)	148,116	243,180	33,375	301,074
Losses charged to allowance	-	-	-	-	-	-
Recoveries	3,172	-	-	694	-	3,866
Ending balance allocated to portfolio segments	\$ 2,034,729	\$ 246,959	\$ 1,822,090	\$ 868,268	\$ 200,000	\$ 5,172,046
Ending balance: individually evaluated for impairment	\$ 112,455	\$ -	\$ -	\$ -	\$ -	\$ 112,455
Ending balance: collectively evaluated for impairment	\$ 1,922,274	\$ 246,959	\$ 1,822,090	\$ 868,268	\$ 200,000	\$ 5,059,591

The following table shows the loan portfolio at December 31, 2014 and 2013 by portfolio segment and impairment methodology:

Loans 2015	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Total
Ending balance	\$ 153,852,972	\$ 42,492,983	\$ 224,219,589	\$ 104,142,352	\$ 524,707,896
Ending balance: individually evaluated for impairment	\$ 1,213,353	\$ -	\$ -	\$ -	\$ 1,213,353
Ending balance: collectively evaluated for impairment	\$ 152,639,619	\$ 42,492,983	\$ 224,219,589	\$ 104,142,352	\$ 523,494,543

Loans 2014	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Total
Ending balance	\$ 133,857,147	\$ 14,100,301	\$ 195,777,189	\$ 72,617,775	\$ 416,352,412
Ending balance: individually evaluated for impairment	\$ 1,330,906	\$ -	\$ -	\$ -	\$ 1,330,906
Ending balance: collectively evaluated for impairment	\$ 132,526,241	\$ 14,100,301	\$ 195,777,189	\$ 72,617,775	\$ 415,021,506

Presidio Bank

Notes to Financial Statements

As of December 31, 2015 the Bank had impaired commercial loans totaling \$1,213,353 with no related allowance. As of December 31, 2014 the Bank had impaired commercial loans totaling \$140,001 with no related allowance and impaired loans totaling \$1,190,905 with a related allowance of \$112,455. The average recorded investment in impaired loans totaled \$1,262,596 and \$1,738,057 for the years ended December 31, 2015 and 2014, respectively, and there was no interest income recognized on impaired loans for the years then ended.

The following table shows the loan portfolio allocated by management's internal risk ratings at December 31, 2015 and 2014:

Loans 2015	Credit Risk Profile by Internally Assigned Grade				Total
	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	
Grade:					
Pass	\$ 149,218,371	\$ 42,492,983	\$ 221,914,707	\$ 101,879,636	\$ 515,505,697
Special Mention	550,000	-	2,304,882	2,262,716	5,117,598
Substandard	4,084,601	-	-	-	4,084,601
Total	\$ 153,852,972	\$ 42,492,983	\$ 224,219,589	\$ 104,142,352	\$ 524,707,896

Loans 2014	Credit Risk Profile by Internally Assigned Grade				Total
	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	
Grade:					
Pass	\$ 126,196,096	\$ 12,803,619	\$ 194,713,901	\$ 71,268,185	\$ 404,981,901
Special Mention	5,245,662	1,296,682	1,063,288	1,349,590	8,955,222
Substandard	2,415,389	-	-	-	2,415,389
Total	\$ 133,857,147	\$ 14,100,301	\$ 195,777,189	\$ 72,617,775	\$ 416,352,389

The following table shows an aging analysis of the loan portfolio by the time past due at December 31, 2015 and 2014:

2015	30-89 Days Past Due	Nonaccrual	Total Past Due and Nonaccrual	Current	Total
Commercial:					
Commercial	\$ -	\$ 1,213,353	\$ 1,213,353	\$ 152,639,619	\$ 153,852,972
Construction and land- development	-	-	-	42,492,983	42,492,983
Commercial real estate	-	-	-	224,219,589	224,219,589
Consumer and other	-	-	-	104,142,352	104,142,352
Total	\$ -	\$ 1,213,353	\$ 1,213,353	\$ 523,494,543	\$ 524,707,896

Presidio Bank

Notes to Financial Statements

2014	30-89 Days Past Due	Nonaccrual	Total Past Due and Nonaccrual	Current	Total
Commercial:					
Commercial	\$ -	\$ 1,330,906	\$ 1,330,906	\$ 132,526,241	\$ 133,857,147
Construction and land- development	-	-	-	14,100,301	14,100,301
Commercial real estate	-	-	-	195,777,189	195,777,189
Consumer and other	-	-	-	72,617,775	72,617,775
Total	\$ -	\$ 1,330,906	\$ 1,330,906	\$ 415,021,506	\$ 416,352,412

6. Premises and Equipment

Premises and equipment consisted of the following:

<i>December 31,</i>	2015	2014
Furniture, fixtures and equipment	\$ 2,774,660	\$ 2,691,325
Leasehold improvements	1,408,855	1,372,606
	4,183,515	4,063,931
Less accumulated depreciation and amortization	(2,952,820)	(2,587,301)
	\$ 1,230,695	\$ 1,476,630

Depreciation and amortization included in occupancy and equipment expense totaled \$365,519 and \$352,993 for the years ended December 31, 2015 and 2014.

7. Interest Bearing Deposits

Interest-bearing deposits consisted of the following:

<i>December 31,</i>	2015	2014
Savings	\$ 2,747,814	\$ 2,620,220
Money market	247,127,554	193,429,810
Interest-bearing demand accounts	78,359,329	69,645,878
Time, \$100,000 or more	38,307,867	41,438,545
Other time	1,810,084	10,203,882
	\$ 368,352,648	\$ 317,338,335

Time deposits issued in denominations greater than or equal to \$250,000 totaled \$31,897,164 and \$34,194,245 at December 31, 2015 and 2014, respectively.

Presidio Bank

Notes to Financial Statements

Aggregate annual maturities of time deposits are as follows:

<i>Year Ending December 31,</i>	
2016	\$ 36,344,216
2017	2,146,489
2018	525,125
2019	156,013
2020	946,108
	\$ 40,117,951

Interest expense recognized on interest-bearing deposits for the years ended December 31, 2015 and 2014 consisted of the following:

<i>December 31,</i>	2015	2014
Savings	\$ 2,726	\$ 2,311
Money market	450,093	358,483
Interest-bearing demand accounts	152,468	159,266
Time, \$100,000 or more	187,693	99,935
Other time	25,878	176,531
	\$ 818,858	\$ 796,526

8. Income Taxes

Income taxes for the years ended December 31, 2015 and 2014 consisted of the following:

2015	Federal	State	Total
Current	\$ 1,534,154	\$ 605,189	\$ 2,139,343
Deferred	(376,000)	(140,000)	(516,000)
Income tax expense	\$ 1,158,154	\$ 465,189	\$ 1,623,343

2014	Federal	State	Total
Current	\$ 2,024,611	\$ 535,468	\$ 2,560,079
Deferred	(341,000)	15,000	(326,000)
Income tax expense	\$ 1,683,611	\$ 550,468	\$ 2,234,079

Presidio Bank

Notes to Financial Statements

The provision for income taxes differs from amounts computed by applying the statutory Federal income tax rate to income before income taxes. The items comprising these differences consisted of the following for the years ended December 31, 2015 and 2014:

	2015		2014	
	Amount	Rate	Amount	Rate
Federal income tax expense at statutory rate	\$ 1,425,267	34.0%	\$ 1,829,252	34.0%
State franchise tax, net of Federal benefit	306,900	7.3%	363,309	6.8%
Stock options	(94,364)	(2.2%)	50,000	0.9%
Low-income housing investments	(49,090)	(1.2%)	-	-
Other	34,630	0.8%	(8,482)	(0.2%)
Income tax expense	\$ 1,623,343	38.7%	\$ 2,234,079	41.5%

Deferred tax assets (liabilities) at December 31, 2015 and 2014 consisted of the following:

	2015	2014
Deferred tax assets:		
Organizational costs	\$ 208,057	\$ 245,886
Allowance for loan losses	2,684,509	2,177,352
Share-based compensation	251,188	310,808
Accrued expenses	776,749	663,201
Other	518,157	456,257
Total deferred tax assets	4,438,660	3,853,504
Deferred tax liabilities:		
FHLB stock dividends	(4,874)	(4,874)
Prepaid expenses	(4,825)	-
Change in accounting method	-	(71,446)
Fixed assets	(72,725)	-
Deferred loan costs	(391,889)	(363,184)
Total deferred tax liabilities	(474,313)	(439,504)
Net deferred tax assets	\$ 3,964,347	\$ 3,414,000

The determination of the amount of deferred income tax assets which are more likely than not to be realized is primarily dependent on projections of future earnings, which are subject to uncertainty and estimates that may change given economic conditions and other factors. The realization of deferred income tax assets is assessed and a valuation allowance is recorded if it is "more likely than not" that all or a portion of the deferred tax asset will not be realized. "More likely than not" is defined as greater than a 50% chance. All available evidence, both positive and negative is considered to determine whether, based on the weight of that evidence, a valuation allowance is needed. Based upon its analysis of available evidence, including recent profitability and the ability to realize net operating losses in the near term, management has determined that it is "more likely than not" that the Bank's deferred income tax assets as of December 31, 2015 were fully realized and therefore no valuation allowance was recorded.

Presidio Bank

Notes to Financial Statements

At December 31, 2015, the Bank had no Federal or State net operating loss carryforwards. The Bank files income tax returns in the United States and California jurisdictions. Federal and California tax returns are currently open for examination for tax years since 2011 and 2010, respectively. The total amount of unrecognized tax benefits, including interest and penalties, at December 31, 2015 was not material. The amount of tax benefits that would impact the effective rate, if recognized, is not expected to be material. The Bank does not anticipate any significant changes with respect to unrecognized tax benefits within the next 12 months.

9. Borrowing Arrangements

Lines of Credit

The Bank has unsecured Federal funds lines of credit with two of its correspondent banks under which it can borrow up to an aggregate of \$10,000,000. There were no borrowings outstanding under these arrangements at December 31, 2015 or 2014.

Federal Reserve Bank

The Bank has a borrowing arrangement with the Federal Reserve Bank of San Francisco secured by certain of the Bank's loans. At December 31, 2015, the amounts pledged and borrowing capacity under this arrangement totaled \$143,449,672 and \$117,072,179, respectively. At December 31, 2014, the amounts pledged and borrowing capacity under this arrangement totaled \$114,831,088 and \$97,477,166, respectively. There were no borrowings outstanding under this arrangement at December 31, 2015 or 2014.

Federal Home Loan Bank

The Bank has a borrowing arrangement with FHLB under which short-term and long term advances are secured by the Bank's loan portfolio. The Bank's credit limit varies according to the amount and composition of loans pledged as collateral. At December 31, 2015, the loans pledged and borrowing capacity under such limits were approximately \$83,180,995 and \$69,332,802, respectively. At December 31, 2014, the loans pledged and borrowing capacity under such limits were approximately \$104,356,631 and \$81,031,686, respectively. There were no borrowings outstanding under this arrangement at December 31, 2015 and 2014. Of the borrowing capacity at December 31, 2015 and 2014, \$22,000,000 was pledged as collateral in the form of a letter of credit to secure public deposits.

Subordinated Debentures

During 2014 the Bank issued \$10,000,000 of subordinated debentures in a private placement to accredited investors.

The subordinated debentures mature on September 30, 2024. The subordinated debentures are redeemable in whole or in part, from time to time, upon the occurrence of specific events defined within the notes. The subordinated debentures are also redeemable in whole or in part, on or after the fifth anniversary of the effective date of issuance, at prices ranging from 101% to 103% of the principal amount outstanding. Debt issuance costs totaling \$436,696 were capitalized as a discount to par value and are being amortized over the term of the debt as additional interest expense.

Presidio Bank

Notes to Financial Statements

The subordinated debentures may be included in Tier 2 capital (with certain limitations applicable) under current regulatory guidelines and interpretations. The subordinated debentures have a fixed rate of interest equal to 8%.

10. Commitments and Contingencies

Operating Leases

The Bank leases its San Francisco headquarters, branch offices in Walnut Creek, San Rafael, San Mateo and Palo Alto, and an office in Santa Rosa under non-cancelable operating leases. The leases expire on May 31, 2016, March 31, 2016, August 21, 2017, January 31, 2020, August 31, 2024 and May 30, 2016 respectively. The leases include annual rent adjustments of approximately 2.6%, 2%, 3%, 3%, 3% and 3%, respectively, each year during the lease terms. The San Francisco lease has two five year renewal options, the Walnut Creek, San Rafael, San Mateo and Palo Alto leases each have one five year renewal option and the Santa Rosa lease has one three year renewal option.

On January 6, 2016, the Bank extended its San Francisco headquarters lease to March 31, 2021. The lease includes annual rent adjustments of 3% each year during the lease term.

On January 15, 2016, the Bank extended its Walnut Creek lease to March 31, 2017.

On January 29, 2016, the Bank extended its Santa Rosa lease to May 31, 2019. The lease includes a rent adjustment of 2.6% during the final year of the lease term.

Approximate future minimum lease payments are as follows:

<i>Year Ending December 31,</i>	
2016	\$ 1,458,710
2017	1,476,047
2018	1,486,335
2019	1,504,196
2020	1,186,391
Thereafter	1,471,832
	<hr/>
	\$ 8,583,511

Rental expense included in occupancy and equipment expense totaled \$1,295,570 and \$1,098,374 for years ended December 31, 2015 and 2014, respectively.

Financial Instruments with Off-Balance-Sheet Risk

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business in order to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments consist of the following at December 31, 2015 and 2014:

	2015	2014
Commitments to extend credit	\$ 236,729,000	\$ 194,723,000
Standby letters of credit	\$ 11,405,000	\$ 8,084,000

Presidio Bank

Notes to Financial Statements

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

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, and deeds of trust on residential real estate and income-producing commercial properties.

Standby letters of credit are conditional commitments issued to guarantee the performance of a client to a third party. The credit risk involved in issuing standby letters of credit is essentially the same as that involved in extending loans to clients. The fair value of the liability related to these standby letters of credit, which represents the fees received for issuing the guarantees, was not significant at December 31, 2015. The Bank recognizes these fees as revenue over the term of the commitment or when the commitment is used.

Commercial loan commitments represent approximately 64% of total commitments and are generally unsecured or secured by collateral other than real estate and have variable interest rates. Consumer loan commitments represent approximately 6% of total commitments and are generally unsecured or secured by collateral other than real estate and have variable interest rates. Real estate loan commitments represent approximately 16% of total commitments and are generally secured by property with a loan-to-value ratio not to exceed 75%. The majority of real estate commitments also have variable interest rates. Letters of credit represent 5% of total commitments. Home equity lines of credit represent the remaining 9% of total commitments and are generally secured by residential real estate and have both variable and fixed interest rates.

Concentrations of Credit Risk

The Bank grants real estate mortgage, real estate construction and commercial loans to customers in San Francisco and surrounding counties. A substantial portion of its portfolio is secured by commercial and residential real estate at December 31, 2015 and 2014.

In management's judgment, a concentration of loans exists in real estate related loans with approximately 66% of the Bank's loans being real estate related. Although management believes the loans within this concentration have no more than the normal risk of collectibility, a substantial decline in the performance of the economy in general or a decline in real estate values in the Bank's primary market area, in particular, could have an adverse impact on the collectibility of these loans. Personal and business income represent the primary source of repayment for a majority of these loans.

Presidio Bank

Notes to Financial Statements

Correspondent Banking Agreements

The Bank maintains funds on deposit with other federally insured financial institutions under correspondent banking agreements. Bank balances totaling approximately \$572,848 and \$4,048 exceeded FDIC insurance limits as of December 31, 2015 and 2014, respectively.

11. Share-Based Compensation

The Bank grants stock options, restricted stock and restricted stock units to employees, directors and advisory board members in exchange for services, pursuant to the shareholder approved 2006 Stock Option Plan. The plan currently provides for 1,625,000 authorized shares.

Stock Option Awards

Stock option grants are granted with an exercise price equal to the fair market value of the related common stock on the grant date. Stock option grants generally become exercisable in equal annual installments over a four-year period with each installment vesting on the anniversary date of the grant. Each grant has a maximum ten-year term.

Stock option activity for the years ended December 31, 2015 and 2014 is summarized as follows:

	Number of Stock Options Outstanding	Weighted Average Exercise Price	Weighted Average Grant Date Fair Value	Weighted Average Remaining Contractual Life
Outstanding at December 31, 2013	1,010,425	\$ 9.24	\$ 2.09	4.5 years
Granted	173,500	10.52	3.67	
Exercised	(4,400)	9.72	3.07	
Cancelled or expired	(3,225)	9.02	2.32	
Outstanding at December 31, 2014	1,176,300	9.35	2.33	4.3 years
Granted	200,500	12.28	4.34	
Exercised	(230,500)	9.52	2.43	
Cancelled or expired	(28,500)	9.27	3.21	
Outstanding at December 31, 2015	1,117,800	9.85	2.65	4.6 years
Exercisable at December 31, 2015	740,650	9.38		2.7 years
Additional options expected to vest	315,755	\$ 10.61		8.1 years

At December 31, 2015, the aggregate intrinsic value of stock options outstanding was \$3,915,239, the aggregate intrinsic value of options exercisable was \$2,942,774, the aggregate intrinsic value of options exercised during the year was \$837,252 and the aggregate intrinsic value of additional options expected to vest was \$863,828.

Presidio Bank

Notes to Financial Statements

The weighted average exercise price and weighted average remaining contractual term by type of option award were as follows at December 31, 2015:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term
Organizer options	137,500	\$ 10.00	0.6 years
Service-based options	980,300	\$ 9.83	5.2 years

The unrecognized compensation cost related to non-vested service-based options totaled \$1,179,220 as of December 31, 2015. That cost is expected to be amortized on an accelerated basis over a weighted average period of 2.7 years and will be adjusted for subsequent changes in estimated forfeitures.

The following weighted average assumptions were used in the option pricing to value stock options granted in the periods indicated:

	2015	2014
Grant date fair value per share of options granted	\$ 4.34	\$ 3.65
Significant fair value assumptions:		
Expected term in years	8.3 years	7.2 years
Expected annual volatility	29.4%	29.6%
Expected annual dividend yield	0%	0%
Risk-free interest rate	1.85%	2.02%

The total compensation cost included in operating expenses was \$362,053 and \$236,752 for the years ended December 31, 2015 and 2014, respectively.

Restricted Stock Awards

The following restricted stock information is for the years ended December 31, 2015 and 2014.

	2015		2014	
	Number of Shares	Weighted Average Grant Date Fair Value Per Share	Number of Shares	Weighted Average Grant Date Fair Value Per Share
Nonvested, beginning of year	2,250	\$ 10.50	29,252	\$ 7.49
Granted	19,000	12.40	4,500	10.50
Vested	(11,750)	12.04	(31,502)	7.70
Forfeited	-	-	-	-
Nonvested, end of year	9,500	\$ 12.40	2,250	\$ 10.50

Presidio Bank

Notes to Financial Statements

Restricted Stock Units

The following restricted stock unit information is for the year ended December 31, 2015 and 2014.

	2015		2014	
	Number of Shares	Weighted Average Grant Date Fair Value Per Share	Number of Shares	Weighted Average Grant Date Fair Value Per Share
Nonvested, beginning of year	19,046	\$ 10.50	24,747	\$ 8.25
Granted	18,303	12.43	19,046	10.50
Incremental performance shares	4,758	12.43	-	-
Vested	(23,804)	10.50	(24,747)	8.25
Forfeited	(1,307)	12.40	-	-
Nonvested, end of year	16,996	\$ 12.43	19,046	\$ 10.50

Restricted stock units granted during 2015 and 2014 were earned as of December 31, 2015 and December 31, 2014, respectively, but are payable in shares to the holders as of May 15, 2015 and May 15, 2014, respectively. Units granted with these terms are, therefore, fully expensed as of the year-end but not reflected in shares outstanding until the payout date.

Compensation cost associated with the restricted stock and restricted stock units totaled \$299,853 and \$387,797 for the years ended December 31, 2015 and 2014, respectively. As of December 31, 2015 the unrecognized compensation cost related to the nonvested restricted stock and restricted stock units totaled approximately \$117,800. The unrecognized compensation cost at December 31, 2015 is expected to be amortized on a straight-line basis over a weighted average period of one year and will be adjusted for subsequent changes in estimated forfeitures.

12. Shareholders' Equity

Preferred Stock

On November 20, 2009, the Bank entered into a Letter Agreement (the "Purchase Agreement") with the United States Department of the Treasury (the "Treasury"), pursuant to which the Bank issued and sold (i) 10,800 shares of Fixed Rate Non-cumulative Perpetual Preferred Stock, Series A (the "Series A Preferred Stock") for a purchase price of \$10,800,000 and (ii) a warrant to purchase 325 shares of Fixed Rate Non-cumulative Perpetual Preferred Stock, Series B stock, (the "Warrant Preferred") for \$0.01 per share for an aggregate exercise price of \$3.25. The Treasury exercised the warrant immediately upon issuance. On December 11, 2012, the Treasury sold at auction all 10,800 shares of the Series A Preferred and all 325 shares of the Series B Preferred to private investors.

The Series A Preferred Stock qualifies as Tier 1 capital and pays non-cumulative dividends quarterly at a rate of 5% per annum for the first five years, and 9% per annum thereafter. The Warrant Preferred pays non-cumulative dividends at a rate of 9% per annum until redemption. Either series may be redeemed by the Bank after three years; however, the Warrant Preferred may not be redeemed until after all the Series A Preferred Stock has been redeemed.

Presidio Bank

Notes to Financial Statements

The Series A Preferred Stock and the Warrant Preferred were issued in a private placement exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended. Neither the Series A Preferred Stock nor the Warrant Preferred will be subject to any contractual restrictions on transfer, except that the Treasury and its transferees shall not effect any transfer of the Series A or Series B Preferred Stock which would require the bank to become subject to the periodic reporting requirements of Section 13 or 15(d) of the Exchange Act.

The Series A Preferred and Warrant Preferred shall be non-voting, other than class voting rights on (i) any authorization or issuance of shares ranking senior to the Series A Preferred and Warrant Preferred, (ii) any amendment to the rights of the Series A Preferred and Warrant Preferred, or (iii) any merger, exchange or similar transaction which would adversely affect the rights of the Series A Preferred and Warrant Preferred. If dividends on the Series A Preferred and Warrant Preferred are not paid in full for six dividend periods, whether or not consecutive, the holders of the Series A Preferred and Warrant Preferred will have the right to elect 2 directors. The right to elect directors will end when full dividends have been paid for all prior dividend periods.

Furthermore, for as long as any Series A Preferred Stock or Warrant Preferred is outstanding, no dividends may be declared or paid on junior preferred shares, preferred shares ranking pari passu with the Series A Preferred Stock or Warrant Preferred, or common shares (other than in the case of pari passu preferred shares or dividends on a pro rata basis with the Series A Preferred Stock or Warrant Preferred), nor may the Bank repurchase or redeem any junior preferred shares, preferred shares ranking pari passu with the Series A Preferred Stock or Warrant Preferred, unless the full dividend for the latest completed dividend period has been declared and paid in full.

The Bank recorded a discount on the Series A Preferred Stock at approximately the liquidation preference of the Series B Preferred. The discount recorded on the Series A Preferred Stock was amortized on the level-yield method over five years.

On November 22, 2013, the Bank repurchased 4,256 shares of the Series A Preferred Stock for \$4,074,920 from a private investor.

On September 30, 2015, the Bank repurchased all of the remaining 6,544 shares of Series A Preferred Stock and 325 shares of Series B Preferred Stock at par value of \$6,869,000 from private investors.

Dividends

Upon declaration by the Board of Directors, all shareholders of record will be entitled to receive dividends. The California Financial Code restricts the total dividend payment of any state banking association in any calendar year to the lesser of (1) the bank's retained earnings or (2) the Bank's net income for its last three fiscal years, less distributions made to shareholders during the same three-year period. At December 31, 2015, no amounts were free of such restrictions. The Bank received regulatory approval to pay the quarterly dividends on the Series A Preferred and the Series B Preferred during 2015 and 2014.

Presidio Bank

Notes to Financial Statements

Regulatory Capital

The Bank is subject to certain regulatory capital requirements administered by the FRB and the FDIC. Failure to meet these minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements.

Under capital adequacy guidelines, the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. These quantitative measures are established by regulation and require that minimum amounts and ratios of Total and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets be maintained. Capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

The Bank is also subject to additional capital guidelines under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum Total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table on the following page. As of December 31, 2015 and 2014, the most recent notification from the FDIC categorized the Bank as well capitalized under these guidelines. Management believes as of December 31, 2015 the Bank meets all capital adequacy requirements to which it is subject. There are no conditions or events since that notification that management believes have changed the Bank's category.

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Presidio Bank

Notes to Financial Statements

Management believes that the Bank met all of its capital adequacy requirements as of December 31, 2015 and 2014.

	2015		2014	
	Amount	Ratio	Amount	Ratio
<u>Leverage Ratio</u>				
Presidio Bank	\$ 57,696,000	9.0%	\$ 47,910,000	8.8%
Minimum requirement for "Well-Capitalized" institution	31,923,000	5.0%	27,194,000	5.0%
Minimum regulatory requirement	25,539,000	4.0%	21,755,000	4.0%
<u>Common Equity Tier 1 Risk-Based Capital Ratio</u>				
Presidio Bank	\$ 57,696,000	9.4%	N/A	N/A
Minimum requirement for "Well-Capitalized" institution	39,867,000	6.5%	N/A	N/A
Minimum regulatory requirement	27,600,000	4.5%	N/A	N/A
<u>Tier 1 Risk-Based Capital Ratio</u>				
Presidio Bank	\$ 57,696,000	9.4%	\$ 47,910,000	10.0%
Minimum requirement for "Well-Capitalized" institution	49,067,000	8.0%	28,751,000	6.0%
Minimum regulatory requirement	36,800,520	6.0%	19,167,000	4.0%
<u>Total Risk-Based Capital Ratio</u>				
Presidio Bank	\$ 74,533,000	12.2%	\$ 63,618,000	13.3%
Minimum requirement for "Well-Capitalized" institution	61,334,000	10.0%	47,918,000	10.0%
Minimum regulatory requirement	49,067,000	8.0%	38,334,000	8.0%

Earnings Per Share

The factors used in the earnings per share computation for the years ended December 31, 2015 and 2014 are as follows:

	2015	2014
Basic:		
Net income	\$ 2,542,020	\$ 3,146,074
Dividends on preferred stock	(475,494)	(356,650)
Gain on settlement of Series A Preferred Stock	-	-
Accretion of discount on Series A Preferred Stock	-	(57,778)
Net income available to common shareholders	\$ 2,066,526	\$ 2,731,646
Weighted average common shares outstanding	4,772,540	4,177,784
Basic earnings per common share	\$ 0.43	\$ 0.65

Presidio Bank

Notes to Financial Statements

	2015	2014
Diluted:		
Net income available to common shareholders	\$ 2,066,526	\$ 2,731,646
Weighted average common shares outstanding for basic earnings per common share	4,772,540	4,177,784
Add: Dilutive effects of assumed exercises of stock options	249,678	187,054
Average shares and dilutive potential common shares	5,022,218	4,364,838
Diluted earnings per common share	\$ 0.41	\$ 0.63

Stock options to purchase shares totaling 180,227 and 154,666 for the years ended December 31, 2015 and 2014 were excluded from the calculation of diluted earnings per share because they were considered anti-dilutive in that the assumed proceeds from exercise price, tax benefits, and average future compensation were greater than the average price of the Bank's common stock, but such stock options could become dilutive in the future.

13. Related Party Transactions

The Bank has entered into transactions with related parties, including Directors, executive officers and affiliates. The following is a summary of the aggregate activity involving related party borrowers during the years ended December 31, 2015 and 2014:

	2015	2014
Beginning balance	\$ 923,000	\$ 893,000
Disbursements	5,362,000	4,062,000
Amounts repaid	(5,105,000)	(4,032,000)
Ending balance	\$ 1,180,000	\$ 923,000
Undisbursed commitments to related parties	\$ 1,714,000	\$ 714,000

14. Employee Benefit Plans

Profit Sharing Plan

In 2006, the Bank adopted the Presidio Bank 401 (k) Profit Sharing Plan and Trust. All employees 21 years of age or older are eligible to participate in the plan. Eligible employees may elect to make tax deferred contributions up to the maximum amount allowed by law. The Bank may make additional contributions to the plan at the discretion of the Board of Directors. Bank contributions vest at a rate of 20% annually for all employees. The Bank made contributions to the Plan totaling approximately \$295,000 and \$242,000 for the years ended December 31, 2015 and 2014, respectively.

Presidio Bank

Notes to Financial Statements

15. Other Expenses

Other expenses for the years ended December 31, 2015 and 2014 consisted of the following:

	2015	2014
Data processing	\$ 1,151,711	\$ 1,063,871
Regulatory and insurance	433,505	393,944
Professional fees	531,426	429,258
Advertising and promotions	258,124	210,922
Stationery and supplies	168,012	161,543
Travel and entertainment	262,529	230,444
Correspondent bank charges	166,761	199,508
Directors fees and share-based compensation	342,480	424,047
Telephone	177,979	144,459
Other	402,140	334,975
	\$ 3,894,667	\$ 3,592,971

16. Fair Value Measurements

Fair Value Hierarchy

The Bank groups its assets and liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. Valuations within these levels are based upon:

Level 1 - Quoted market prices for identical instruments traded in active exchange markets.

Level 2 - Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable or can be corroborated by observable market data.

Level 3 - Model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect the Bank's estimates of assumptions that market participants would use on pricing the asset or liability. Valuation techniques include management judgment and estimation which may be significant.

Management monitors the availability of observable market data to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period. Management evaluates the significance of transfers between levels based upon the nature of the financial instrument and size of the transfer relative to total assets, total liabilities or total earnings.

Presidio Bank

Notes to Financial Statements

Fair Value of Financial Instruments

The estimated carrying and fair values of the Bank's financial instruments are as follows:

	Fair Value Measurements at December 31, 2015				
	Carrying Amount	Level 1	Level 2	Level 3	Total
Financial assets					
Cash and cash equivalents	\$ 109,386,709	\$ 109,386,709	\$ -	\$ -	\$ 109,386,709
Securities available-for-sale	10,626,905	-	10,626,905	-	10,626,905
Securities held-to-maturity	631,450	-	-	631,450	631,450
FRB and FHLB stock	3,775,450	N/A	N/A	N/A	3,775,450
Loans, net	517,513,593	-	-	517,513,593	517,513,593
Accrued interest receivable	1,281,758	-	18,589	1,263,169	1,281,758
Financial liabilities					
Deposits	579,350,751	526,824,731	40,155,236	-	566,979,967
Subordinated debt	10,000,000	-	-	10,000,000	10,000,000
Accrued interest payable	15,170	17	15,153	-	15,170

	Fair Value Measurements at December 31, 2014				
	Carrying Amount	Level 1	Level 2	Level 3	Total
Financial assets					
Cash and cash equivalents	\$ 110,263,158	\$ 110,263,158	\$ -	\$ -	\$ 110,263,158
Securities available-for-sale	10,640,544	-	10,640,544	-	10,640,544
Securities held-to-maturity	664,223	-	-	664,223	664,223
FRB and FHLB stock	3,087,300	N/A	N/A	N/A	3,087,300
Loans, net	410,568,585	-	-	413,876,721	413,876,721
Accrued interest receivable	1,089,133	-	18,309	1,070,824	1,089,133
Financial liabilities					
Deposits	481,691,725	421,947,557	51,756,504	-	473,704,061
Subordinated debt	10,000,000	-	-	10,000,000	10,000,000
Accrued interest payable	21,529	400	21,129	-	21,529

These estimates do not reflect any premium or discount that could result from offering the Bank's entire holdings of a particular financial instrument for sale at one time, nor do they attempt to estimate the value of anticipated future business related to the instruments. In addition, the tax ramifications related to the realization of unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of these estimates.

The methods and assumptions used to estimate the fair values of financial instruments are described as follows:

- a) *Cash and Cash Equivalents* - The carrying amounts of cash and short-term instruments approximate fair values and are classified as Level 1.
- b) *FRB and FHLB Stock* - It is not practical to determine the fair value of FRB and FHLB stock due to restrictions placed on its transferability.

Presidio Bank

Notes to Financial Statements

- c) *Investment Securities* - The fair value of investment securities available-for-sale is based on quoted market prices for similar securities in active markets resulting in a Level 2 classification. The fair value for investment securities held-to-maturity is based on a discounted cash flow model resulting in a Level 3 classification.
- d) *Loans* - Fair values of loans are estimated as follows: For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values resulting in a Level 3 classification. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality resulting in a Level 3 classification. Certain impaired loans are valued at the lower of cost or fair value of collateral. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.
- e) *Deposits* - The fair values disclosed for demand deposits (e.g., interest and non-interest checking, passbook savings, and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amount) resulting in a Level 1 classification. Fair values for fixed rate certificates of deposit are estimated using a discounted cash flows calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits resulting in a Level 2 classification.
- f) *Subordinated Debt* - The fair values for subordinated debt are estimated using a discounted cash flows calculation using a discount rate approximating the rate applicable at the balance sheet date for debt issued to institutions of similar credit worthiness resulting in a Level 3 classification.
- g) *Accrued Interest Receivable/Payable* - The carrying amounts of accrued interest approximate fair value resulting in Level 2 for accrued interest receivable on investment securities, Level 3 for accrued interest receivable on loans Level 1 for accrued interest payable on money market deposits and Level 2 for accrued interest payable on certificates of deposit.
- h) *Off-balance Sheet Instruments* - Fair values for off-balance sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value of commitments is not material.

Assets Recorded at Fair Value

The following tables present information about the Bank's assets measured at fair value on a recurring and nonrecurring basis. There were no liabilities measured at fair value on a recurring or nonrecurring basis.

Presidio Bank

Notes to Financial Statements

Recurring Basis

The Bank is required or permitted to record the following assets at fair value on a recurring basis at December 31, 2015 and 2014:

	December 31, 2015			
	Fair Value	Level 1	Level 2	Level 3
Available-for-sale investment securities				
Debt securities:				
Mortgage backed securities	\$ 6,566,103	\$ -	\$ 6,566,103	\$ -
Residential				
Asset backed securities				
Student loans	4,060,802	-	4,060,802	-
Total assets measured at fair value on a recurring basis	\$ 10,626,905	\$ -	\$ 10,626,905	\$ -

	December 31, 2014			
	Fair Value	Level 1	Level 2	Level 3
Available-for-sale investment securities				
Debt securities:				
Mortgage backed securities	\$ 5,709,789	\$ -	\$ 5,709,789	\$ -
Residential				
Asset backed securities				
Student loans	4,930,755	-	4,930,755	-
Total assets measured at fair value on a recurring basis	\$ 10,640,544	\$ -	\$ 10,640,544	\$ -

During the year ended December 31, 2015, there were no transfers in or out of Level 1 or Level 2 categories.

Presidio Bank

Notes to Financial Statements

Non-recurring Basis

The Bank may be required, from time to time, to measure certain assets at fair value on a non-recurring basis. These include assets that are measured at the lower of cost or market value that were recognized at fair value which was below cost at the reporting date.

	December 31, 2015			
	Fair Value	Level 1	Level 2	Level 3
Impaired loans:				
Commercial	\$ -	\$ -	\$ -	\$ -
Total assets measured at fair value on a non-recurring basis	\$ -	\$ -	\$ -	\$ -

	December 31, 2014			
	Fair Value	Level 1	Level 2	Level 3
Impaired loans:				
Commercial	\$ 1,078,450	\$ -	\$ -	\$ 1,078,450
Total assets measured at fair value on a non-recurring basis	\$ 1,078,450	\$ -	\$ -	\$ 1,078,450

The fair value of impaired loans included above is based on the fair value of the collateral less costs to sell. Impaired loans were categorized as Level 3 with unobservable inputs and assumptions in fair value measurements. Gains of \$112,455 were recognized as decreases in specific reserves on the above impaired commercial loans during the year ended December 31, 2015. Gains of \$168,813 were recognized as decreases in the specific reserves on the above impaired commercial loans for during the year ended December 31, 2014.

The following table presents quantitative information about level 3 fair value measurements for assets measured at fair value on a non-recurring basis at December 31, 2015 and 2014:

	December 31, 2015			
	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Input
Impaired loan - commercial	\$ -			

	December 31, 2014			
	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Input
Impaired loan - commercial	\$ 1,190,905	Sales comparison approach	Adjustment for differences between the comparable sales	13.4%

