PRESIDIO BANK

FINANCIAL STATEMENTS

December 31, 2017 and 2016

Presidio Bank

Financial Statements
Years Ended December 31, 2017 and 2016

Presidio Bank

Contents

INDEPENDENT AUDITOR'S REPORT

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

Report on the Financial Statements

We have audited the accompanying financial statements of Presidio Bank, which comprise the balance sheets as of December 31, 2017 and 2016 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, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Crowe Horwath LLP

Crowe Horwath LLP

San Francisco, California
March 12, 2018

Financial Statements

Presidio Bank

Balance Sheets

December 31,		**2017**		2016
Assets				
Cash and due from banks		**137,564,503**		156,194,325
Available-for-sale investment securities, at fair value		**7,073,633**		8,417,033
Held-to-maturity investment securities, at amortized cost		**595,674**		616,246
Federal Reserve Bank stock, at cost		**1,955,550**		1,884,200
Federal Home Loan Bank stock, at cost		**2,688,100**		2,331,300
Loans, less allowance for loan losses of $7,165,642 in 2017 and $6,867,658 in 2016		**619,115,610**		565,911,668
Premises and equipment, net		**2,627,349**		1,019,794
Deferred tax assets, net		**3,517,265**		4,382,463
Bank owned life insurance		**12,177,772**		-
Accrued interest receivable and other assets		**6,542,341**		6,745,620
Total Assets	**$**	**793,857,797**	$	747,502,649
Liabilities and Shareholders' Equity				
Deposits:				
Non-interest bearing	**$**	**295,069,565**	$	257,757,439
Interest bearing		**409,083,766**		405,726,109
Total deposits		**704,153,331**		663,483,548
Subordinated debt, net		**9,705,232**		9,661,563
Accrued interest payable and other liabilities		**5,237,025**		6,995,175
Total Liabilities		**719,095,588**		680,140,286
Commitments and Contingencies (Note 10)				
Shareholders' Equity:				
Preferred stock, no par value; 10,000,000 shares authorized, none outstanding		-		-
Common stock, no par value; 30,000,000 shares authorized; 6,084,059 and 5,957,265 shares issued and outstanding in 2017 and 2016, respectively		**65,959,682**		64,122,072
Retained earnings		**8,853,957**		3,377,073
Accumulated other comprehensive loss, net of tax		**(51,430)**		(136,782)
Total Shareholders' Equity		**74,762,209**		67,362,363
Total Liabilities and Shareholders' Equity	**$**	**793,857,797**	$	747,502,649

See accompanying notes to financial statements.

Presidio Bank

Statements of Income

Years Ended December 31,		**2017**		2016
Interest and Dividend Income:				
Interest and fees on loans	$	**29,186,955**	$	24,884,410
Interest on due from banks and other overnight deposits		**1,182,519**		591,929
Interest on investment securities		**128,089**		143,115
Dividend income		**301,899**		373,464
Total interest and dividend income		**30,799,462**		25,992,918
Interest Expense:				
Interest on deposits		**974,644**		912,209
Interest on subordinated debt		**843,669**		843,669
Interest on other borrowings		**580**		19,148
Total interest expense		**1,818,893**		1,775,026
Net interest income		**28,980,569**		24,217,892
Provision for loan losses		**297,984**		566,772
Net interest income after provision for loan losses		**28,682,585**		23,651,120
Non-Interest Income:				
Service charges and fees		**709,548**		641,450
Other non-interest income		**238,020**		56,842
Total non-interest income		**947,568**		698,292
Non-Interest Expenses:				
Salaries and employee benefits		**11,524,711**		10,671,111
Occupancy and equipment		**2,281,982**		2,124,473
Other		**4,487,412**		4,135,225
Total non-interest expenses		**18,294,105**		16,930,809
Income before income taxes		**11,336,048**		7,418,603
Provision for income taxes		**5,859,164**		2,941,123
Net Income	$	**5,476,884**	$	4,477,480
Basic Earnings Per Common Share	$	**0.91**	$	0.78
Diluted Earnings Per Common Share	$	**0.87**	$	0.75

See accompanying notes to financial statements.

Presidio Bank

Statements of Comprehensive Income

Years Ended December 31,		**2017**		2016
Net Income	**$**	5,476,884	$	4,477,480
Other comprehensive income:				
Unrealized gains on available-for-sale securities:				
Unrealized holding gain arising during the year		143,690		14,315
Tax effect		(58,338)		(8,771)
Other comprehensive income		85,352		5,544
Comprehensive Income	**$**	5,562,236	$	4,483,024

See accompanying notes to financial statements.

Presidio Bank

Statements of Changes in Shareholders' Equity
Years Ended December 31, 2017 and 2016

	Common Stock		Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
	Shares	Amount			
Balance, January 1, 2016	5,476,695	$ 58,795,777	$ (1,100,407)	$ (142,326)	$ 57,553,044
Restricted stock awards granted	40,500	-	-	-	-
Restricted stock units vested	12,745	-	-	-	-
Exercise of stock options	427,325	4,464,067	-	-	4,464,067
Share-based compensation expense	-	862,228	-	-	862,228
Net income	-	-	4,477,480	-	4,477,480
Other comprehensive income	-	-	-	5,544	5,544
Balance, December 31, 2016	**5,957,265**	**$ 64,122,072**	**$ 3,377,073**	**$ (136,782)**	**$ 67,362,363**
Restricted stock awards granted	38,000	-	-	-	-
Restricted stock units vested	14,952	-	-	-	-
Restricted stock forfeited	(4,125)	-	-	-	-
Restricted shares withheld to cover withholding taxes	(2,208)	(39,712)	-	-	(39,712)
Exercise of stock options	80,175	793,615	-	-	793,615
Share-based compensation expense	-	1,083,707	-	-	1,083,707
Net income	-	-	5,476,884	-	5,476,884
Other comprehensive income	-	-	-	85,352	85,352
Balance, December 31, 2017	**6,084,059**	**$ 65,959,682**	**$ 8,853,957**	**$ (51,430)**	**$ 74,762,209**

See accompanying notes to financial statements.

Presidio Bank
Statements of Cash Flows

Years Ended December 31,		2017		2016
Cash Flows from Operating Activities:				
Net income	$	5,476,884	$	4,477,480
Adjustments to reconcile net income to net cash provided by operating activities:				
Amortization of premiums on investment securities, net		12,082		23,656
Amortization of debt issuance costs		43,669		43,669
Amortization of tax credit investment		519,835		400,002
Depreciation and amortization		349,929		338,314
Provision for loan losses		297,984		566,772
Provision for unfunded commitments		195,965		29,046
Deferred loan origination (costs) fees, net		170,822		(45,183)
Share-based compensation expense		1,083,707		862,228
Deferred compensation expense		90,000		-
Deferred income tax expense (benefit)		806,860		(426,887)
Increase in surrender value of life insurance		(177,772)		-
Increase in accrued interest receivable and other assets		(316,556)		(7,330)
Increase (decrease) in accrued interest payable and other Liabilities		789,607		(70,758)
Net Cash Provided by Operating Activities		9,343,016		6,191,009
Cash Flows from Investing Activities:				
Purchases of available-for-sale investment securities		(500,000)		-
Proceeds from principal payments on investment securities		1,995,580		2,215,735
Purchases of FRB stock		(71,350)		(56,550)
Purchases of FHLB stock		(356,800)		(383,500)
Net increase in loans		(53,672,748)		(48,919,664)
Purchase of bank owned life insurance		(12,000,000)		-
Cash invested in low income housing fund		(2,833,722)		(708,865)
Purchases of premises and equipment		(1,957,484)		(127,413)
Net Cash Used in Investing Activities		(69,396,524)		(47,980,257)
Cash Flows from Financing Activities:				
Net increase in demand, interest-bearing and savings deposits		36,812,083		77,839,021
Net increase in time deposits		3,857,700		6,293,776
Proceeds from FHLB advances		-		53,500,000
Repayment of FHLB advances		-		(53,500,000)
Cash paid for withholding of taxes on share based awards		(39,712)		-
Proceeds from the exercise of stock options		793,615		4,464,067
Net Cash Provided by Financing Activities		41,423,686		88,596,864
(Decrease) Increase in Cash and Cash Equivalents		(18,629,822)		46,807,616
Cash and Cash Equivalents at Beginning of Year		156,194,325		109,386,709
Cash and Cash Equivalents at End of Year	$	137,564,503	$	156,194,325

Supplemental Disclosures of Cash Flow Information:				
Cash paid for interest expense	$	1,821,615	$	1,769,409
Cash paid for income taxes	$	4,255,000	$	2,515,221

See accompanying 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, 2017 through March 12, 2018, 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.

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, 2017 and 2016.

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 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 $31,093,000 and $21,518,000 at December 31, 2017 and 2016, 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.

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.

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.

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 Owned Life Insurance

The Bank has purchased life insurance policies on certain key executives. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or amounts due that are probable at settlement.

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, 2017 and 2016, 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 management believes the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount 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, 2017 or December 31, 2016 because it does not have any significant unrecognized tax benefits.

Earnings Per Share

Basic earnings per common share is net income divided by the weighted average number of common shares outstanding during the period. All outstanding unvested share-based payment awards that contain rights to nonforfeitable dividends are considered participating securities for this calculation. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable under stock options using the treasury stock method.

Share-Based Compensation

The Bank has two share-based compensation plan, the Presidio Bank 2006 Stock Option Plan (the "2006 Plan") and the Presidio Bank 2016 Equity Incentive Plan (the “2016 Plan”), which have been approved by its shareholders and permit the grant of stock options and restricted stock for up to 1,625,000 and 500,000 shares of the Bank's common stock, respectively. The 2006 Plan expired on July 18, 2016. There were 350,886 shares available for future grant in the 2016 Plan at December 31, 2017. The Plans are 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 Plans do not provide for the settlement of awards in cash. The Plans require 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 plans: 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.

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 Accounting Standards and 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. These amendments are effective for public business entities for annual reporting periods beginning after December 15, 2017, including interim reporting periods within that period. The amendments should be applied retrospectively to all periods presented or retrospectively with the cumulative effect recognized at the date of initial application. The majority of the Bank’s revenue consists of net interest income on financial assets and financial liabilities, which is explicitly excluded from the scope of ASU 2014-09. The Bank has completed its analysis for determining the extent ASU 2014-09 will affect its noninterest income, primarily in the area of fees and service charges on deposit accounts. Based on the analysis performed, the Bank did not have a material change in the timing or measurement of revenues related to noninterest income. The Bank will continue to evaluate the effect that this guidance will have on changes to financial statements disclosures which will be required to be included in the consolidated financial statements for the year ending December 31, 2018. However, the Bank does not expect this to have a material impact on its financial statements.

In January 2016, the FASB amended existing guidance that requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. It requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. It requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (i.e., securities or loans and receivables). It eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate fair value that is required to be disclosed for financial instruments measured at amortized cost. These amendments are effective for public business entities for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The adoption of this standard is not expected to have a material effect on the Bank’s operating results or financial condition, however the Bank is currently evaluating the impact to its disclosure of the fair value of financial instruments given the requirement to use the exit price notion described above.

In February 2016, the FASB amended existing guidance that requires lessees recognize the following for all leases (with the exception of short-term leases) at the commencement date (1) a lease liability, which is the lessee's obligation to make payments arising from a lease, measured on a discounted basis; and (2) A right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the lessee accounting model and Topic 606, Revenue from Contracts with Customers. These amendments are effective for public business entities for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application is permitted. Lessees (for capital and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. The Bank is currently evaluating the impact of this new accounting standard on the financial statements, and expects most of its significant leases will be required to be presented as assets on the balance sheet with corresponding liabilities for the lease obligations.

In June 2016, FASB issued guidance to replace the incurred loss model with an expected loss model, which is referred to as the current expected credit loss (CECL) model The CECL model is applicable to the measurement of credit losses on financial assets measured at amortized cost, including loan receivables, held-to maturity debt securities, and reinsurance receivables It also applies to off-balance sheet credit exposures not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in leases recognized by a lessor. For debt securities with other-than-temporary impairment (OTTI), the guidance will be applied prospectively. Existing purchased credit impaired (PCI) assets WIl grandfathered and classified as purchased credit deteriorated (PCD) assets at the date of adoption. The asset will be grossed up for the allowance for expected credit losses for all PCD assets at the date of adoption and will continue to recognize the discount in interest income based on the yield of such assets as of the adoption date Subsequent changes in expected credit losses will be recorded through the allowance. For all other assets within the scope of CECL a cumulative-effect adjustment will be recognized in retained earnings as of the beginning of the first reporting period in which the guidance is effective. These amendments are effective for public business entities that are not registered with the Securities and Exchange Commission for fiscal years beginning after December 15, 2020, including interim periods within those fiscal years. For calendar year-end companies such as the Bank, the standard is effective for March 31, 2021 interim financial statements. All entities may early adopt for fiscal years beginning after December 15, 2018, including interim periods in those fiscal years, which means that calendar year-end entities may adopt as early as the March 31, 2019 interim financial statements. The Bank is currently evaluating the impact of this new accounting standard on the financial statements and has not yet quantified an estimate of the expected impact.

In May 2017, the FASB provided guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. An entity should account for the effects of a modification unless all the following are met: (a) The fair value (or calculated value or intrinsic value, if such an alternative measurement method is used) of the modified award is the same as the fair value (or calculated value or intrinsic value, if such an alternative measurement method is used) of the original award immediately before the original award is modified. If the modification does not affect any of the inputs to the valuation technique that the entity uses to value the award, the entity is not required to estimate the value immediately before and after the modification. (b) The vesting conditions of the modified award are the same as the vesting conditions of the original award immediately before the original award is modified. (c) The classification of the modified award as an equity instrument or a liability instrument is the same as the classification of the original award immediately before the original award is modified. The amendments in this Update are effective for all entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2017. Early adoption is permitted, including adoption in any interim period, for reporting periods for which financial statements have not yet been issued. The amendments should be applied prospectively to an award modified on or after the adoption date. The adoption of this standard is not expected to have a material effect on the Bank's operating results or financial condition.

In March 2016, the FASB amended existing guidance to simply the accounting for share-based payment award transactions, including: (a) income tax consequences; (b) classification of awards as either equity or liabilities; (c) classification on the statement of cash flows; and (d) policy election to estimate the number of awards that are expected to vest (current GAAP) or account for forfeitures when they occur. The Bank adopted this standard effective January 1, 2017. The Bank made an accounting policy election upon adoption to account for forfeitures as they occur, and this change resulted in a cumulative adjustment that was immaterial to the periods presented. Changes to the statement of cash flows have been applied prospectively and the Company recorded excess tax benefits in its income tax expense. Adoption of all other changes under this update did not have a material impact on the Bank's operating results or financial condition.

In February 2018, the FASB amended existing guidance to allow the reclassification of certain tax effects from accumulated other comprehensive income. The amendments allow a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. Consequently, the amendments eliminate the stranded tax effects resulting from the change in tax rates and will improve the usefulness of information reported to financial statement users. However, because the amendments only relate to the reclassification of the income tax effects of the Tax Cuts and Jobs Act enacted on December 22, 2017 that reduced the Bank's tax rate from 34% to 21%, the underlying guidance that requires that the effect of a change in tax laws or rates be included in income from continuing operations is not affected. The amendments also require certain disclosures about stranded tax effects. The amendments are effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption of the amendments in this update is permitted. The effect of adoption of the standard will be to reclassify the stranded tax effects of the change in the federal corporate tax rate of the net unrealized gains on our available-for-sale investment securities from accumulated other comprehensive loss, net to retained earnings, which will be insignificant because the Bank's stranded tax effects are insignificant.

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, 2017 and 2016 and the corresponding amounts of gross unrealized gains and losses recognized in accumulated other comprehensive loss:

	2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
Mortgage-backed securities-residential	$ 4,533,409	$ -	$ (71,788)	$ 4,461,621
Asset-backed securities-student loan	2,626,807	-	(14,795)	2,612,012
	$ 7,160,216	$ -	$ (86,583)	$ 7,073,633

	2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
Mortgage-backed securities-residential	$ 5,313,453	$ -	$ (163,556)	$ 5,149,897
Asset-backed securities-student loan	3,333,853	-	(66,717)	3,267,136
	$ 8,647,306	$ -	$ (230,273)	$ 8,417,033

Net unrealized losses on available-for-sale investment securities totaling $86,583 and $230,373 were recorded net of related tax benefits of $35,153 and $93,491 as accumulated other comprehensive loss at December 31, 2017 and 2016, respectively. There were no sales or transfers of available-for-sale investment securities during the years ended December 31, 2017 and 2016. Available-for-sale residential mortgage-based securities with an amortized cost of $3,521,640 and fair value of $3,461,496 mature in 2023. Available-for-sale residential mortgage-based securities with an amortized cost of $470,890 and fair value of $465,592 mature in 2027. Available-for-sale residential mortgage-based securities with an amortized cost of $540,880 and fair value of $534,534 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.

At December 31, 2017 and 2016, 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, 2017, 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, 2017 and 2016.

At December 31, 2017, the Bank held available-for-sale asset backed securities with net unrealized losses of $14,795 which had been in a continuous net unrealized loss position for more than 12 months. At December 31, 2016, the Bank held available-for-sale asset-backed securities with net unrealized losses of $66,717 which had been in a continuous net unrealized loss position for more than 12 months. At December 31, 2017, the Bank held available-for-sale mortgage-backed securities with net unrealized totaling $71,788 which had been in a continuous net unrealized loss position for more than 12 months. At December 31, 2016, the Bank held available-for-sale mortgage-backed securities with net unrealized losses of $163,556 which had been in a continuous net unrealized loss position for less than 12 months.

Held-to-Maturity Investment Securities

The Bank held at amortized cost $595,674 and $616,246 of mortgage-backed held-to-maturity investment securities at December 31, 2017 and 2016, respectively, with estimated fair values substantially equivalent to amortized cost.

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, 2017 and 2016. Held-to-maturity investment securities mature in 2019.

4. Loans

Outstanding loans at December 31, 2017 and 2016 are summarized below:

December 31,		**2017**		2016
Commercial	$	**197,747,782**	$	180,412,055
Construction and land development		**44,714,219**		12,297,957
Commercial real estate		**271,345,626**		263,462,889
Consumer and other		**113,492,681**		117,454,659
		627,300,308		573,627,560
Deferred loan origination fees, net		**(1,019,056)**		(848,234)
Allowance for loan losses		**(7,165,642)**		(6,867,658)
	$	**619,115,610**	$	565,911,668

Salaries and employee benefits totaling $773,979 and $680,682 were deferred as loan origination costs for the years ended December 31, 2017 and 2016, respectively.

As of December 31, 2017, the Bank had no recorded investments in a troubled debt restructurings. There were no loans modified as troubled debt restructurings during the year ended December 31, 2017.

As of December 31, 2016, the Bank had a recorded investment in a troubled debt restructuring of $1,054,850, and had allocated $85,694 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, 2016 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.

There were no loans modified as troubled debt restructurings during the previous twelve months that defaulted during the years ended December 31, 2017 and 2016. The Bank generally considers a delinquency in excess of 90 days to constitute a default.

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, 2017 and 2016 by portfolio segment and the allocation of the allowance for loan losses at December 31, 2017 and 2016 by portfolio segment and impairment methodology:

Allowance for Loan Losses 2017	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Unallocated	Total
Beginning balance allocated to portfolio segments	$ 2,840,021	$ 197,640	$ 2,472,583	$ 1,357,414	$ -	$ 6,867,658
Provision for loan losses	(316,585)	505,037	109,586	(142,386)	142,332	297,984
Losses charged to allowance	51,006	-	-	-	-	51,006
Recoveries	(51,006)	-	-	-	-	(51,006)
Ending balance allocated to portfolio segments	$ 2,523,436	$ 702,677	$ 2,582,169	$ 1,215,028	$ 142,332	$ 7,165,642
Ending balance: individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ -
Ending balance: collectively evaluated for impairment	$ 2,523,436	$ 702,677	$ 2,582,169	$ 1,215,028	$ 142,332	$ 7,165,642

Allowance for Loan Losses 2016	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Unallocated	Total
Beginning balance allocated to portfolio segments	$ 2,315,101	$ 658,397	$ 2,116,518	$ 1,210,870	$ -	$ 6,300,886
Provision for loan losses	524,920	(460,757)	356,065	146,544	-	566,772
Losses charged to allowance	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-
Ending balance allocated to portfolio segments	$ 2,840,021	$ 197,640	$ 2,472,583	$ 1,357,414	$ -	$ 6,867,658
Ending balance: individually evaluated for impairment	$ 85,694	$ -	$ -	$ -	$ -	$ 85,694
Ending balance: collectively evaluated for impairment	$ 2,754,327	$ 197,640	$ 2,472,583	$ 1,357,414	$ -	$ 6,781,964

The following table shows the loan portfolio at December 31, 2017 and 2016 by portfolio segment and impairment methodology:

Loans 2017	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Total
Ending balance	$ 197,747,782	$ 44,714,219	$ 271,345,626	$ 113,492,681	$ 627,300,308
Ending balance: individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -
Ending balance: collectively evaluated for impairment	$ 197,747,782	$ 44,714,219	$ 271,345,626	$ 113,492,681	$ 627,300,308

Loans 2016	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Total
Ending balance	$ 180,412,055	$ 12,297,957	$ 263,462,889	$ 117,454,659	$ 573,627,560
Ending balance: individually evaluated for impairment	$ 1,054,850	$ -	$ -	$ -	$ 1,054,850
Ending balance: collectively evaluated for impairment	$ 179,357,205	$ 12,297,957	$ 263,462,889	$ 117,454,659	$ 572,572,710

As of December 31, 2017 the Bank had no impaired loans. As of December 31, 2016 the Bank had impaired commercial loans totaling $1,054,850 with $85,694 of related allowance. The average recorded investment in impaired loans totaled $659,706 and $1,083,185 for the years ended December 31, 2017 and 2016, 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, 2017 and 2016:

	Credit Risk Profile by Internally Assigned Grade				
Loans 2017	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Total
Grade:					
Pass	$ 185,220,516	$ 44,714,219	$ 262,178,346	$ 110,875,548	$ 602,988,629
Special Mention	11,130,125	-	8,167,280	2,002,133	21,299,538
Substandard	1,397,141	-	1,000,000	615,000	3,012,141
Total	$ 197,747,782	$ 44,714,219	$ 271,345,626	$ 113,492,681	$ 627,300,308

	Credit Risk Profile by Internally Assigned Grade				
Loans 2016	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Total
Grade:					
Pass	$ 176,356,388	$ 12,297,957	$ 263,133,728	$ 115,845,534	$ 567,633,607
Special Mention	300,000	-	329,161	994,125	1,623,286
Substandard	3,755,666	-	-	615,000	4,370,666
Total	$ 180,412,055	$ 12,297,957	$ 263,462,889	$ 117,454,659	$ 573,627,560

The following table shows an aging analysis of the loan portfolio by the time past due at December 31, 2017 and 2016:

2017	30-89 Days Past Due	Nonaccrual	Total Past Due and Nonaccrual	Current	Total
Commercial:					
Commercial	$ -	$ -	$ -	$ 197,747,782	$ 197,747,782
Construction and land-development	-	-	-	44,714,219	44,714,219
Commercial real estate	-	-	-	271,345,626	271,345,626
Consumer and other	-	-	-	113,492,681	113,492,681
Total	$ -	$ -	$ -	$ 627,300,308	$ 627,300,308

2016	30-89 Days Past Due	Nonaccrual	Total Past Due and Nonaccrual	Current	Total
Commercial:					
Commercial	$ -	$ 1,054,850	$ 1,054,850	$ 179,357,205	$ 180,412,055
Construction and land-development	-	-	-	12,297,957	12,297,957
Commercial real estate	-	-	-	263,462,889	263,462,889
Consumer and other	-	-	-	117,454,659	117,454,659
Total	$ -	$ 1,054,850	$ 1,054,850	$ 572,572,710	$ 573,627,560

6. Premises and Equipment

Premises and equipment consisted of the following:

December 31,	**2017**	2016
Furniture, fixtures and equipment	**$ 3,337,635**	$ 2,859,548
Leasehold improvements	**2,809,504**	1,408,855
	6,147,139	4,268,403
Less accumulated depreciation and amortization	**(3,519,790)**	(3,248,609)
	$ 2,627,349	$ 1,019,794

Depreciation and amortization included in occupancy and equipment expense totaled $349,929 and $338,314 for the years ended December 31, 2017 and 2016.

7. Interest Bearing Deposits

Interest-bearing deposits consisted of the following:

December 31,	**2017**	2016
Savings	**$ 4,092,828**	$ 3,074,276
Money market	**234,612,892**	256,636,447
Interest-bearing demand accounts	**120,108,619**	99,603,659
Time, $100,000 or more	**48,807,689**	44,515,341
Other time	**1,461,738**	1,896,386
	$ 409,083,766	$ 405,726,109

Time deposits issued in denominations greater than or equal to $250,000 totaled $43,685,947 and $37,998,740 at December 31, 2017 and 2016, respectively.

Aggregate annual maturities of time deposits are as follows:

Year Ending December 31,	
2018	$ 40,219,335
2019	8,981,019
2020	501,336
2021	567,737
	$ 50,269,427

Interest expense recognized on interest-bearing deposits for the years ended December 31, 2017 and 2016 consisted of the following:

December 31,	**2017**	2016
Savings	**$ 4,370**	$ 3,732
Money market	**515,429**	540,692
Interest-bearing demand accounts	**182,618**	172,795
Time, $100,000 or more	**266,656**	160,865
Other time	**5,571**	34,125
	$ 974,644	$ 912,209

8. Income Taxes

Income taxes for the years ended December 31, 2017 and 2016 consisted of the following:

2017	Federal	State	Total
Current	$ 3,714,913	$ 1,337,391	$ 5,052,304
Deferred	928,958	(122,098)	806,860
Income tax expense	$ 4,643,871	$ 1,215,293	$ 5,859,164

2016	Federal	State	Total
Current	$ 2,473,882	$ 894,128	$ 3,368,010
Deferred	(339,249)	(87,638)	(426,887)
Income tax expense	$ 2,134,633	$ 806,490	$ 2,941,123

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, 2017 and 2016:

	2017		2016	
	Amount	Rate	Amount	Rate
Federal income tax expense at statutory rate	$ 3,854,256	34.0%	$ 2,522,325	34.0%
State franchise tax, net of Federal benefit	802,093	7.1%	532,203	7.2%
Impact of tax reform	1,417,174	12.5%	-	-
Stock options	(40,691)	(0.4%)	25,764	0.3%
Earnings from bank owned life insurance	(60,442)	(0.5%)	-	-
Low-income housing investments	(48,157)	(0.4%)	(88,184)	(1.2%)
Other	(67,069)	(0.6%)	(50,985)	(0.7%)
Income tax expense	$ 5,859,164	51.7%	$ 2,941,123	39.6%

Deferred tax assets (liabilities) at December 31, 2017 and 2016 consisted of the following:

	2017	2016
Deferred tax assets:		
Allowance for loan losses	**$ 2,293,999**	$ 2,938,342
Organizational costs	**95,111**	170,229
Share-based compensation	**268,048**	218,896
Accrued expenses	**652,332**	783,846
Deferred rent	**211,110**	242,104
Current state tax	**262,730**	265,237
Other	**73,293**	229,185
Total deferred tax assets	**3,856,623**	4,847,839
Deferred tax liabilities:		
FHLB stock dividends	**(3,502)**	(4,874)
Prepaid expenses	**(2,224)**	(3,596)
Fixed assets	**-**	(35,741)
Deferred loan costs	**(333,632)**	(421,165)
Total deferred tax liabilities	**(339,358)**	(465,376)
Net deferred tax assets	**$ 3,517,265**	$ 4,382,463

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, 2017 will be fully realized and therefore no valuation allowance was recorded.

At December 31, 2017, 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 2014 and 2013, respectively. The total amount of unrecognized tax benefits, including interest and penalties, at December 31, 2017 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.

On December 22, 2017, H.R. 1, originally known as the "Tax Cuts and Jobs Act" was enacted into law. The legislation provides for significant changes to the Internal Revenue Code that impact corporate taxation requirements, such as the reduction of the federal income tax rate for corporations from 34 percent to 21 percent and changes or limitations to certain tax deductions. The Company remeasured its deferred tax assets and liabilities based on the reduced federal corporate income tax rate of 21 percent. This remeasurement resulted in an income tax impact of $1,417,174, which is included as a component of income tax expense.

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, 2017 or 2016.

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, 2017, the amounts pledged and borrowing capacity under this arrangement totaled $56,255,311 and $48,532,492, respectively. At December 31, 2016, the amounts pledged and borrowing capacity under this arrangement totaled $60,691,985 and $49,681,047, respectively. There were no borrowings outstanding under this arrangement at December 31, 2017 or 2016.

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, 2017, the loans pledged and borrowing capacity under such limits were approximately $305,605,617 and $186,749,156, respectively. At December 31, 2016, the loans pledged and borrowing capacity under such limits were approximately $265,234,123 and $160,873,200, respectively. There were no borrowings outstanding under this arrangement at December 31, 2017 and 2016. Of the borrowing capacity at December 31, 2017 and 2016, $22,000,000 was pledged as collateral in the form of a letter of credit to secure public deposits.

Subordinated Debt

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 recorded as a discount to par value and are being amortized over the term of the debt as additional interest expense. The unamortized balance of debt issuance costs totaled $294,768 and $338,437 at December 31, 2017 and 2016, respectively, and is recorded as part of the carrying amount of the subordinated debt. 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% and require quarterly interest-only payments until maturity.

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, under non-cancelable operating leases. The leases expire on March 31, 2021, December 31, 2027, December 31, 2022, August 31, 2024 and January 31, 2020 respectively. Each lease includes an annual rent adjustment of approximately 3.0% each year during the lease terms and each lease has one five-year renewal option. The bank leases an office in Santa Rosa on a month to month basis.

Approximate future minimum lease payments are as follows:

Year Ending December 31,	
2018	$ 1,753,905
2019	1,806,449
2020	1,516,813
2021	972,672
2022	795,277
Thereafter	2,356,510
	$ 9,201,626

Rental expense included in occupancy and equipment expense totaled $1,804,969 and $1,646,121 for years ended December 31, 2017 and 2016, 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, 2017 and 2016:

	2017	2016
Commitments to extend credit	**$ 353,192,000**	$ 276,883,000
Standby letters of credit	**$ 8,478,000**	$ 8,982,000

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, 2017. The Bank recognizes these fees as revenue over the term of the commitment or when the commitment is used.

Commercial loan commitments represent approximately 49% 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 23% 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 2% of total commitments. Home equity lines of credit represent the remaining 20% 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, 2017 and 2016.

In management's judgment, a concentration of loans exists in real estate related loans with approximately 63% 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.

Correspondent Banking Agreements

The Bank maintains funds on deposit with other federally insured financial institutions under correspondent banking agreements. Bank balances totaling approximately $501,569 and $433,232 exceeded FDIC insurance limits as of December 31, 2017 and 2016, respectively.

11. Share-Based Compensation

The Bank grants stock options, restricted stock awards and restricted stock units to employees, directors and advisory board members in exchange for services, pursuant to the shareholder approved 2006 Stock Option Plan and 2016 Equity Incentive Plan. During the year ended December 31, 2017 the 2006 Stock Option Plan expired and has no shares available for future grant. The 2016 Equity Incentive Plan provides for 500,000 authorized shares and at December 31, 2017 had 350,886 shares available for future grant.

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, 2017 and 2016 is summarized as follows:

	Number of Stock Options Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life
Outstanding at December 31, 2015	1,117,800	$ 9.85	5.6 years
Granted	36,000	13.61	
Exercised	(427,325)	9.75	
Forfeited	(13,500)	11.11	
Expired	(1,400)	9.88	
Outstanding at December 31, 2016	711,575	10.07	5.6 years
Granted	25,500	17.52	
Exercised	(80,175)	9.90	
Forfeited	(20,875)	13.03	
Expired	(2,000)	10.31	
Outstanding at December 31, 2017	634,025	$ 10.29	5.1 years
Exercisable at December 31, 2017	466,900	$ 9.43	4.3 years
Additional options expected to vest	167,125	$ 12.71	7.5 years

At December 31, 2017, the aggregate intrinsic value of stock options outstanding was $8,849,205, the aggregate intrinsic value of options exercisable was $6,921,155 and the aggregate intrinsic value of additional options expected to vest was $1,928,050. The aggregate intrinsic value of options exercised during the years ended December 31, 2017 and 2016 totaled $656,661 and $1,633,099, respectively.

During the years ended December 31, 2017 and 2016, the Bank received $793,615 and $4,168,352 of cash from the exercise of stock options and realized tax benefits of $229,279 and $94,657, respectively.

The unrecognized compensation cost related to non-vested service-based options totaled $595,521 as of December 31, 2017. That cost is expected to be amortized on an accelerated basis over a weighted average period of 2.2 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:

		2017		2016
Grant date fair value per share of options granted	$	6.67	$	5.03
Significant fair value assumptions:				
Expected term in years		8.4 years		8.1 years
Expected annual volatility		27.08%		29.4%
Expected annual dividend yield		0%		0%
Risk-free interest rate		2.24%		1.85%

The total compensation cost included in operating expenses was $566,139 and $458,270 for the years ended December 31, 2017 and 2016, respectively.

Restricted Stock Awards

The following restricted stock information is for the years ended December 31, 2017 and 2016.

	2017			2016		
	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	40,500	$	13.60	9,500	$	12.40
Granted	38,000		16.60	40,500		13.60
Vested	(9,875)		13.60	(9,500)		12.40
Forfeited	(4,125)		15.01	-		-
Nonvested, end of year	64,500	$	15.28	40,500	$	13.60

Restricted Stock Units

The following restricted stock unit information is for the year ended December 31, 2017 and 2016.

	2017			2016		
	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	14,952	$	13.37	16,996	$	12.43
Granted	12,120		16.50	14,952		13.37
Vested	(14,952)		13.37	(12,745)		12.43
Forfeited	-		-	(4,251)		12.43
Nonvested, end of year	12,120	$	16.50	14,952	$	13.37

Restricted stock units granted during 2017 and 2016 were earned as of December 31, 2017 and December 31, 2016, respectively, but are payable in shares to the holders as of May 15, 2018 and May 15, 2017, 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 awards and restricted stock units totaled $517,568 and $403,958 for the years ended December 31, 2017 and 2016, respectively. As of December 31, 2017 the unrecognized compensation cost related to the nonvested restricted stock and restricted stock units totaled approximately $766,886. The unrecognized compensation cost at December 31, 2017 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

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, 2017, $8,853,957 was free of such restrictions.

Regulatory Capital

Banks and bank holding companies are subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Under the Basel III rules, the Bank must hold a capital conservation buffer above the adequately capitalized risk-based capital ratios. The capital conservation buffer is being phased in from 0.625% for 2016 to 2.50% by 2019. The capital conservation buffer for 2017 is 1.25%. The net unrealized gain or loss on available for sale securities not included in computing regulatory capital. Management believes as of December 31, 2017, the Bank meets all capital adequacy requirements to which they are subject.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At year-end 2017 and 2016, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the Bank's category.

	2017		2016	
	Amount	Ratio	Amount	Ratio
Leverage Ratio				
Presidio Bank	$ 74,814,000	9.7%	$ 67,499,000	9.1%
Minimum requirement for "Well-Capitalized" institution	38,701,000	5.0%	36,915,000	5.0%
Minimum regulatory requirement	30,961,000	4.0%	29,532,000	4.0%
Common Equity Tier 1 Risk-Based Capital Ratio				
Presidio Bank	$ 74,814,000	9.8%	67,499,000	10.1%
Minimum requirement for "Well-Capitalized" institution	49,646,000	6.5%	43,368,000	6.5%
Minimum regulatory requirement	34,370,000	4.5%	30,024,000	4.5%
Tier 1 Risk-Based Capital Ratio				
Presidio Bank	$ 74,814,000	9.8%	$ 67,499,000	10.1%
Minimum requirement for "Well-Capitalized" institution	61,102,000	8.0%	53,376,000	8.0%
Minimum regulatory requirement	45,827,000	6.0%	40,032,000	6.0%
Total Risk-Based Capital Ratio				
Presidio Bank	$ 92,446,000	12.1%	$ 84,594,000	12.7%
Minimum requirement for "Well-Capitalized" institution	76,378,000	10.0%	66,720,000	10.0%
Minimum regulatory requirement	61,102,000	8.0%	53,376,000	8.0%

Earnings Per Share

The factors used in the earnings per share computation for the years ended December 31, 2017 and 2016 are as follows:

	2017	2016
Basic:		
Net income	$ **5,476,884**	$ 4,477,480
Dividends on preferred stock	**-**	-
Less: Undistributed earnings allocated to participating securities	**(61,227)**	(19,653)
Net income available to common shareholders	$ **5,415,657**	$ 4,457,827
Weighted average common shares outstanding including participating securities	**6,046,183**	5,773,075
Less: Participating securities	**(67,591)**	(25,340)
Average shares	**5,978,592**	5,747,735
Basic earnings per common share	$ **0.91**	$ 0.78

	2017	2016
Diluted:		
Net income available to common shareholders	$ **5,415,657**	$ 4,457,827
Weighted average common shares outstanding for basic earnings per common share	**5,978,592**	5,747,735
Add: Dilutive effects of assumed exercises of stock options	**280,509**	199,616
Average shares and dilutive potential common shares	**6,259,101**	5,947,351
Diluted earnings per common share	$ **0.87**	$ 0.75

Stock options to purchase shares totaling 29,660 and 226,466 for the years ended December 31, 2017 and 2016 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, 2017 and 2016:

	2017	2016
Beginning balance	$ 1,420,000	$ 1,180,000
Disbursements	9,562,000	9,133,000
Amounts repaid	(9,270,000)	(8,893,000)
Ending balance	$ 1,712,000	$ 1,420,000
Undisbursed commitments to related parties	$ 1,590,000	$ 2,236,000

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. Employees vest into the plan at a rate of 20% annually. The Bank made contributions to the Plan totaling $319,642 and $308,367 for the years ended December 31, 2017 and 2016, respectively.

Post Retirement Plans

The Board of Directors approved a salary continuation plan for certain executives during 2017. Under the plan, once executives reach retirement age, the Bank is obligated to provide executives with annual benefits after retirement. The estimated present value of these future benefits is accrued from the effective date of the plan based on a discount rate of 3.6%.

The expense recognized under this plan for the year ended December 31, 2017 totaled $90,000. Accrued compensation payable under the salary continuation plan totaled $90,000, and is included in accrued interest payable and other liabilities on the Bank's balance sheet.

15. Other Expenses

Other expenses for the years ended December 31, 2017 and 2016 consisted of the following:

	2017	2016
Data processing	$ **1,365,651**	$ 1,286,728
Regulatory and insurance	**453,666**	488,730
Professional fees	**573,639**	538,875
Advertising and promotions	**206,870**	277,050
Stationery and supplies	**172,600**	154,835
Travel and entertainment	**261,263**	255,436
Correspondent bank charges	**121,636**	121,753
Directors fees and share-based compensation	**560,110**	411,532
Telephone	**198,755**	185,638
Other	**573,222**	414,648
	$ **4,487,412**	$ 4,135,225

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.

Fair Value of Financial Instruments

The carrying amounts and estimated fair values of the Bank's financial instruments at December 31, 2017 and 2016 were as follows:

	Carrying Amount	Fair Value Measurements at December 31, 2017 Using: Level 1	Level 2	Level 3	Total
Financial assets					
Cash and cash equivalents	$ 137,564,503	$ 137,564,503	$ -	$ -	$ 137,564,503
Securities available-for-sale	7,073,633		7,073,633	-	7,073,633
Securities held-to-maturity	595,674	-	-	595,674	595,674
FRB and FHLB stock	4,643,650	N/A	N/A	N/A	N/A
Loans, net	619,115,610	-	-	612,133,320	612,133,320
Accrued interest receivable	1,733,181	-	17,610	1,715,571	1,733,181
Financial liabilities					
Deposits	704,153,331	653,883,905	50,364,515	-	704,248,420
Subordinated debt, net	9,705,232	-	-	9,495,606	9,495,606
Accrued interest payable	18,065	9	18,056	-	18,065

	Carrying Amount	Fair Value Measurements at December 31, 2016 Using: Level 1	Level 2	Level 3	Total
Financial assets					
Cash and cash equivalents	$ 156,194,325	$ 156,194,325	$ -	$ -	$ 156,194,325
Securities available-for-sale	8,417,033		8,417,033	-	8,417,033
Securities held-to-maturity	616,246	-	-	616,246	616,246
FRB and FHLB stock	4,215,500	N/A	N/A	N/A	N/A
Loans, net	565,911,668	-	-	566,887,402	566,887,402
Accrued interest receivable	1,733,181	-	18,324	1,376,647	1,394,971
Financial liabilities					
Deposits	663,438,548	653,883,905	50,364,515	-	704,248,420
Subordinated debt, net	9,661,563	-	-	9,530,784	9,530,784
Accrued interest payable	20,787	7	20,780	-	20,787

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 their transferability.*

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.

Recurring Basis

The Bank is required or permitted to record the following assets at fair value on a recurring basis at December 31, 2017 and 2016:

	December 31, 2017			
	Fair Value	Level 1	Level 2	Level 3
Available-for-sale investment securities				
Debt securities:				
Mortgage backed securities Residential	$ 4,461,621	$ -	$ 4,461,621	$ -
Asset backed securities				
Student loans	2,612,012	-	2,612,012	-
Total assets measured at fair value on a recurring basis	$ 7,073,633	$ -	$ 7,073,633	$ -

	December 31, 2016			
	Fair Value	Level 1	Level 2	Level 3
Available-for-sale investment securities				
Debt securities:				
Mortgage backed securities Residential	$ 5,149,897	$ -	$ 5,149,897	$ -
Asset backed securities				
Student loans	3,267,136	-	3,267,136	-
Total assets measured at fair value on a recurring basis	$ 8,417,033	$ -	$ 8,417,033	$ -

During the years ended December 31, 2017 and 2016, there were no transfers in or out of Level 1 or Level 2 categories.

Non-recurring Basis

The Bank may be required, from time to time, to measure certain assets or liabilities 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. There were no assets measured at fair value on a non-recurring basis at December 31, 2017. Assets measured at fair value on a non-recurring basis at December 31, 2016 were as follows:

	December 31, 2016			
	Fair Value	Level 1	Level 2	Level 3
Impaired loans:				
Commercial	$ 969,156	$ -	$ -	$ 969,156
Total assets measured at fair value on a non-recurring basis	$ 969,156	$ -	$ -	$ 969,156

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. Losses of $85,694 were recognized as increases in specific reserves on the above impaired commercial loans during the year ended December 31, 2016.

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, 2016:

	December 31, 2016			
	Fair Value	Valuation Technique(s)	Unobservable Inputs	Range (Weighted Average)
Impaired loan - commercial	$ 969,156	Sales Comparison Approach	Adjustments for differences between the comparable sales	(50)% - 80% (3%)