Report of Independent Auditors
and Financial Statements for

Mountain Pacific Bank

December 31, 2016 and 2015

MOSS-ADAMS LLP

Certified Public Accountants | Business Consultants

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NOTE: This annual report serves as Mountain Pacific Bank’s annual disclosure statement under the requirements of the Federal Deposit Insurance Corporation (FDIC). This statement has not been reviewed or confirmed for accuracy or relevance by the FDIC.

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Stockholders
Mountain Pacific Bank

Report on the Financial Statements

We have audited the accompanying financial statements of Mountain Pacific Bank (the Bank), which comprise the balance sheets as of December 31, 2016 and 2015, and the related statements of income, comprehensive income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

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

Moss Adams LLP

Everett, Washington
February 28, 2017

ASSETS

	December 31, 2016	December 31, 2015
Cash and due from banks	$ 4,570,028	$ 4,220,884
Federal funds sold and excess balance account - Federal Reserve Bank	14,789,000	16,012,000
Total cash and cash equivalents	19,359,028	20,232,884
Interest-bearing deposits in banks	2,000,000	3,000,000
Investment securities available-for-sale	12,543,358	8,886,060
Investment securities held-to-maturity	-	999,745
Loans	191,469,441	152,599,701
Less allowance for loan losses	2,974,275	2,555,069
Total loans, net	188,495,166	150,044,632
Leaseholds and equipment, net	449,373	658,446
Accrued interest receivable	814,698	587,824
Federal Home Loan Bank (FHLB) stock and Pacific Coast Bankers' Bank (PCBB) stock, at cost	503,200	576,600
Other real estate owned (OREO), net	4,930,275	5,340,420
Deferred tax asset, net	3,350,000	3,525,000
Other assets	479,845	427,412
Total assets	$ 232,924,943	$ 194,279,023

LIABILITIES AND STOCKHOLDERS' EQUITY

	2016	2015
Deposits		
Noninterest-bearing	$ 35,096,445	$ 31,088,351
Interest-bearing	169,209,948	132,760,509
Total deposits	204,306,393	163,848,860
FHLB advances	2,000,000	5,000,000
Accrued interest payable	85,390	71,315
Other liabilities	921,229	599,609
Total liabilities	207,313,012	169,519,784
Stockholders' equity		
Common stock, $1 par value, 10,000,000 shares authorized; 6,231,451 and 6,212,541 issued and outstanding at December 31, 2016 and 2015, respectively	6,231,451	6,212,541
Additional paid-in capital	26,927,921	26,794,351
Accumulated deficit	(7,404,393)	(8,244,393)
Accumulated other comprehensive loss	(143,048)	(3,260)
Total stockholders' equity	25,611,931	24,759,239
Total liabilities and stockholder's equity	$ 232,924,943	$ 194,279,023

See accompanying notes.

MOUNTAIN PACIFIC BANK
STATEMENTS OF INCOME

	Years Ended December 31, 2016	2015
INTEREST AND DIVIDEND INCOME		
Loans, including fees	$ 8,588,871	$ 7,113,657
Federal funds sold and excess balance account - Federal Reserve Bank and interest-bearing deposits in banks	41,878	26,067
Investment securities	190,595	175,764
Dividends from FHLB and PCBB	19,517	12,620
Total interest and dividend income	8,840,861	7,328,108
INTEREST EXPENSE		
Deposits	874,645	647,025
FHLB advances and other borrowings	29,225	39,634
Total interest expense	903,870	686,659
Net interest income	7,936,991	6,641,449
PROVISION FOR LOAN LOSSES	400,000	100,000
Net interest income after provision for loan losses	7,536,991	6,541,449
NONINTEREST INCOME		
Service fees	382,731	378,087
Gain on sale of investment securities available-for-sale	27,624	-
Gain on sale of loans	54,436	303,982
Total noninterest income	464,791	682,069
NONINTEREST EXPENSES		
Salaries and employee benefits	3,710,667	3,113,802
Occupancy and equipment	933,182	892,445
Data processing	430,695	424,472
Advertising and business development	248,745	205,926
Professional fees and state taxes	446,886	498,745
Regulatory assessments	225,450	206,400
Other real estate owned, net	155,560	167,797
Other	480,597	463,931
Total noninterest expenses	6,631,782	5,973,518
NET INCOME BEFORE PROVISION FOR INCOME TAXES	1,370,000	1,250,000
PROVISION FOR FEDERAL INCOME TAXES	530,000	425,000
NET INCOME	$ 840,000	$ 825,000

See accompanying notes.

	Years Ended December 31, 2016	2015
NET INCOME	$ 840,000	$ 825,000
OTHER COMPREHENSIVE INCOME		
Unrealized loss on securities		
Unrealized holding loss	(187,164)	(22,988)
Tax effect on unrealized holding loss	65,354	-
Reclassification adjustments for realized gains on sales	(27,624)	-
Tax effect on adjustments for realized gains on sales	9,646	-
Other comprehensive loss	(139,788)	(22,988)
COMPREHENSIVE INCOME	$ 700,212	$ 802,012

MOUNTAIN PACIFIC BANK
STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

	Common Stock		Additional Paid-In	Accumulated	Accumulated Other Comprehensive	Total Stockholders'
	Shares	Amount	Capital	Deficit	Income (Loss)	Equity
BALANCE, December 31, 2014	6,184,206	$ 6,184,206	$ 26,690,434	$ (9,069,393)	$ 19,728	$ 23,824,975
Net income	-	-	-	825,000	-	825,000
Other comprehensive loss, net	-	-	-	-	(22,988)	(22,988)
Stock awards vested	6,885	6,885	(6,885)	-	-	-
Stock options exercised	15,200	15,200	30,400	-	-	45,600
Common stock issued	6,250	6,250	12,500	-	-	18,750
Stock-based compensation expense	-	-	67,902	-	-	67,902
BALANCE, December 31, 2015	6,212,541	6,212,541	26,794,351	(8,244,393)	(3,260)	24,759,239
Net income	-	-	-	840,000	-	840,000
Other comprehensive loss, net	-	-	-	-	(139,788)	(139,788)
Stock awards vested	6,630	6,630	(6,630)	-	-	-
Stock options exercised	11,780	11,780	23,741	-	-	35,521
Stock warrants exercised	500	500	4,500	-	-	5,000
Stock-based compensation expense	-	-	111,959	-	-	111,959
BALANCE, December 31, 2016	6,231,451	$ 6,231,451	$ 26,927,921	$ (7,404,393)	$ (143,048)	$ 25,611,931

See accompanying notes.

	Years Ended December 31, 2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 840,000	$ 825,000
Adjustments to reconcile net income to net cash flows from operating activities		
Provision for loan losses	400,000	100,000
Stock-based compensation expense including stock in lieu of compensation	111,959	67,902
Depreciation and amortization	294,737	276,786
Amortization on investment securities	87,774	64,454
Gain on sale of investment securities	(27,624)	-
Gain on sale of loans	(54,436)	(303,982)
Proceeds from sale of loans	554,023	3,179,367
Deferred federal income taxes	250,000	425,000
Changes in operating assets and liabilities		
Accrued interest receivable	(226,874)	66,932
Other assets	(52,433)	(117,139)
Accrued interest payable	14,075	16,537
Other liabilities	321,620	22,585
Net cash from operating activities	2,512,821	4,623,442
CASH FLOWS FROM INVESTING ACTIVITIES		
Net change in interest-bearing deposits in banks	1,000,000	725,000
Net change in loans made to customers	(39,350,121)	(29,811,979)
Purchases of investment securities available-for-sale	(8,158,528)	(3,858,104)
Proceeds from principal paydowns of mortgage-backed securities	1,998,675	1,258,649
Proceeds from sale of investments available-for-sale	593,571	-
Proceeds from maturities and calls of investments available-for-sale	1,634,046	-
Proceeds from maturities and calls of investments held to maturity	999,745	-
Proceeds from sales of other real estate owned	539,110	269,578
Capitalized costs for other real estate owned	(128,965)	-
Redemption of FHLB stock	73,400	62,400
Additions to premises and equipment, net	(85,664)	(284,104)
Net cash used in investing activities	(40,884,731)	(31,638,560)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in noninterest-bearing deposits	4,008,094	6,901,770
Net increase in interest-bearing deposits	36,449,439	33,342,825
Proceeds from exercise of stock options	35,521	45,600
Proceeds from exercise of stock warrants	5,000	18,750
Repayment of FHLB borrowings	(3,000,000)	(2,425,000)
Net cash from financing activities	37,498,054	37,883,945
NET CHANGE IN CASH AND CASH EQUIVALENTS	(873,856)	10,868,827
CASH AND CASH EQUIVALENTS, beginning of year	20,232,884	9,364,057
CASH AND CASH EQUIVALENTS, end of year	$ 19,359,028	$ 20,232,884
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid during the period for interest	$ 889,795	$ 670,122
Cash paid during the period for federal income taxes	$ 260,000	$ -
SUPPLEMENTAL DISCLOSURE OF NONCASH ITEMS		
Unrealized (loss) on securities available-for-sale	$ (214,788)	$ (22,988)

Note 1 - Organization and Summary of Significant Accounting Policies

Nature of operations - Mountain Pacific Bank (the Bank) provides a full range of banking services to individual and corporate customers through its headquarters in Everett, Washington, and full-service branches in Lynnwood, Washington, and the Ballard neighborhood of Seattle, Washington. The Bank's primary deposit products are checking and term certificate accounts, and its primary lending products are commercial loans and commercial real estate loans. The Bank is subject to significant competition from other financial institutions.

MPB Directors Buildout LLC (the Related Entity) was formed during 2010, and is a related party entity that, at December 31, 2016 and 2015, has common controlling ownership with the Bank through one of its directors. The Related Entity was formed to enter into project-specific buildouts of certain Bank-owned lots without providing further risk to the Bank. The Bank has no direct ownership in the Related Entity. There was no activity or amounts outstanding for the years ended December 31, 2016 or 2015.

At periodic intervals, the state of Washington and the Federal Deposit Insurance Corporation (FDIC) routinely examine the Bank's financial statements as part of their legally prescribed oversight of the banking system. Based on these examinations, the regulators can direct the Bank's financial statements to be adjusted in accordance with their findings.

Financial statement presentation and use of estimates - The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and reporting practices applicable to the banking industry. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheets, and revenues and expenses for the period. Actual results could differ from estimated amounts. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, the valuation of impaired loans and other real estate owned, and deferred tax assets.

Subsequent events - Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. The Bank recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing the financial statements. The Bank's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date and before the financial statements are available to be issued. The Bank has evaluated subsequent events through February 28, 2017, which is the date the financial statements are issued.

Cash and cash equivalents - For purposes of reporting cash flows, cash and cash equivalents include cash on hand, noninterest-bearing amounts due from banks, federal funds sold, and the excess balance account at the Federal Reserve Bank (FRB), all with maturities of three months or less. Generally, federal funds are purchased and sold for one-day periods. The amounts on deposit fluctuate and, at times, may exceed the insured limit by the Federal Deposit Insurance Corporation (FDIC), which potentially subjects the Bank to credit risk. Investments in federal funds sold are made with major banks as approved by the board of directors.

Interest-bearing deposits in banks - Interest-bearing deposits in banks include interest-bearing deposits and certificates of deposit in federally insured financial institutions located throughout the United States and territories. The amounts on deposit fluctuate and, at times, may exceed the insured limit by the FDIC, which potentially subjects the Bank to credit risk.

Investment securities - Investment securities are classified into one of three categories: (1) held-to-maturity, (2) available-for-sale, or (3) trading. The Bank had no trading securities at December 31, 2016 or 2015. Investment securities are categorized as held-to-maturity when the Bank has the positive intent and ability to hold those securities to maturity. Securities that are held-to-maturity are stated at cost and adjusted for amortization of premiums and accretion of discounts, which are recognized as adjustments to interest income. Interest income includes amortization of premiums and discounts. Premiums and discounts are recognized in interest income using the interest method over the period to maturity.

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

Investment securities categorized as available-for-sale are generally held for investment purposes (to maturity), although unanticipated future events may result in the sale of some securities. Available-for-sale securities are recorded at estimated fair value, with the net unrealized gain or loss reported as "accumulated other comprehensive loss" within the statements of changes in stockholders' equity. Realized gains or losses on dispositions are based on the net proceeds and the adjusted carrying amount of securities sold, using the specific identification method, and are included in earnings.

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

Federal Home Loan Bank (FHLB) stock - As a member of the FHLB system, the Bank is required to maintain a minimum investment level in FHLB stock based on specific percentages of the Bank's outstanding loans, total assets, or FHLB advances. This security is classified at cost, classified as a restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income. Management determined there was no impairment at December 31, 2016 and 2015. The Bank had $313,200 and $386,600 of FHLB stock at December 31, 2016 and 2015, respectively.

Pacific Coast Bankers' Bank (PCBB) stock - PCBB stock represents an investment by the Bank in the capital stock of PCBB of $190,000 at both December 31, 2016 and 2015, and is carried at cost, classified as a restricted security, and periodically evaluated for impairment.

Loans held-for-sale - Loans originated and intended for sale in secondary markets are carried at the lower of cost or estimated market value in the aggregate. Net unrealized losses are recognized through a valuation allowance by charges to income. Gains or losses on the sale of such loans are based on the specific identification method. Loans are generally sold with servicing retained.

Loans - Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off generally are reported at their outstanding principal adjusted for any charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method.

The accrual of interest on loans is discontinued at the time the loan is 90 days delinquent unless the credit is well secured and in process of collection. Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash basis or cost-recovery method until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably ensured.

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

Significant concentrations of credit risk - Most of the Bank's business activity is with customers located within Snohomish and King Counties, Washington. The Bank originates commercial, real estate, construction, and consumer loans. Generally, loans are secured by accounts receivable, inventory, deposit accounts, personal property, or real estate. Rights to collateral vary and are legally documented to the extent practicable. Local economic conditions may affect borrowers' ability to meet the stated repayment terms. Approximately 72% of the Bank's loan portfolio is secured by real estate (Note 3). The Bank does not have any significant concentrations to one customer.

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

The allowance for credit losses is maintained at a level sufficient to provide for probable loan losses based on evaluating known and inherent risks in the loan portfolio and is evaluated on a regular basis by management. The allowance is provided based upon management's continuing analysis of the pertinent factors underlying the quality of the loan portfolio. These factors include changes in the size and composition of the loan portfolio, delinquency levels, actual loan loss experience, current economic conditions, and detailed analysis of individual loans for which full collectability may not be ensured. The detailed analysis includes techniques to estimate the fair value of loan collateral and the existence of potential alternative sources of repayment. The allowance consists of specific, general, and unallocated components. The specific component relates to loans that are classified as impaired. For such loans classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers nonimpaired loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. The appropriateness of the allowance for loan losses is estimated based upon these factors and trends identified by management at the time the financial statements are prepared. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available.

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

A troubled debt restructuring is a loan for which the Bank, for reasons related to the borrower's financial difficulties, grants a concession to the borrower that the Bank would not otherwise consider. The loan terms that have been modified or restructured due to the borrower's financial difficulty include, but are not limited to, a reduction in the stated interest rate; an extension of the maturity; an interest rate below market; a reduction in the face amount of the debt; a reduction in the accrued interest; or extension, deferral, renewal, or rewrite of the original loan terms.

Additionally, state and federal regulations, upon examination, may require the Bank to make additional provisions or adjustments to its allowance.

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

Transfers of financial assets - Transfers of an entire financial asset, a group of entire financial assets, or participating interest in an entire financial asset are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Bank, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Loan sales recognition - The Bank originates loans through the Small Business Administration (SBA) and sometimes sells the guaranteed portion. The Bank retains the servicing on the sold guaranteed portion of SBA loans. The Bank receives a fee for servicing the loan. The Bank recognizes a sale on loans if the transferred portion (or portions) and any portion that continues to be held by the transferor are participating interests.

To determine the gain or loss on sale of loans, the Bank's investment in the loan is allocated among the retained portion of the loan, the servicing retained, and the sold portion of the loan, based on the relative fair market value of each portion. The gain or loss on the sold portion of the loan is based on the difference between the sale proceeds and the allocated investment in the sold portion of the loan. A discount is recorded against the carrying value of the retained portion of the loan to offset the fair value allocation of said retained portion.

SBA servicing assets - The Bank accounts for SBA servicing rights as separately recognized servicing rights and initially measures them at fair value. For each class of separately recognized servicing assets and liabilities, an entity is permitted to choose either of the following subsequent measurement methods: (1) the amortization of servicing assets or liabilities in proportion to and over the period of estimated net servicing income or net servicing loss or (2) the reporting of servicing assets or liabilities at fair value at each reporting date and reporting changes in fair value in earnings in the period in which the changes occur.

The Bank subsequently measures each SBA servicing asset using the amortization method. Under the amortization method, servicing assets are amortized into noninterest income in proportion to, and over the period of, estimated net servicing income. The amortized assets are assessed for impairment or increased obligation based on the fair value at each reporting date.

Each class of separately recognized servicing assets subsequently measured using the amortization method is evaluated and measured for impairment. Impairment is determined by stratifying rights into tranches based on predominant characteristics, such as interest rate, loan type, and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the carrying amount of the servicing assets for that tranche. The valuation allowance is adjusted to reflect changes in the measurement of impairment after the initial measurement of fair value. Changes in valuation allowances are reported in net gains on loans sold within noninterest income on the statements of income. Fair value is based on market prices for comparable servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income.

SBA servicing assets totaled $68,147 and $71,358, included in other assets on the balance sheets, from servicing $3,733,390 and $2,807,740 in loans as of December 2016 and 2015, respectively.

Leaseholds and equipment - Bank leaseholds and equipment are stated at cost and depreciated or amortized using the straight-line method over the estimated useful lives of the related assets, which range from 3 to 10 years. Assets are reviewed for impairment when events indicate their carrying value may not be recoverable. If management determines impairment exists, the asset is reduced with an offsetting charge to expense.

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

Other real estate owned - Assets acquired through, or in lieu of, loan foreclosure are held-for-sale and are initially recorded at the lower of cost or estimated fair value at the date of foreclosure. Losses arising from the acquisition of property, in full or partial satisfaction of loans, are charged to the allowance for loan losses. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from other real estate owned on the statements of income.

Income taxes - The Bank records its provision for income tax under the liability method. Deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. Deferred taxes result from temporary differences in the recognition of certain income and expense amounts between the Bank's financial statements and its tax return. Deferred tax assets are reduced by a valuation allowance if, based on the weight of evidence available, it is more likely than not that some portion or all of a deferred tax asset will not be realized.

Financial instruments - In the ordinary course of business, the Bank enters into off-balance-sheet financial instruments consisting of commitments to extend credit, commercial letters of credit, standby letters of credit, and financial guarantees. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received.

Advertising costs - The Bank expenses advertising costs as they are incurred. Total advertising expense was $162,505 and $127,853 for the years ended December 31, 2016 and 2015, respectively.

Restricted assets - Federal Reserve Board regulations generally require maintenance of certain minimum reserve balances on deposit with the FRB or another institution in a pass-through relationship. The amounts of such balances are generally based on asset size and other factors. Such requirements were $406,000 and $180,000 at December 31, 2016 and 2015, respectively.

Comprehensive income - Accounting principles generally require that recognized revenue, expenses, gains, and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale investments, are reported as a separate component of the stockholders' equity section of the balance sheets. Accumulated other comprehensive loss consists of only one component: unrealized gains or losses on investment securities available-for-sale.

Stock-based compensation plan - Stock-based compensation cost is recognized at the grant-date fair value and is based on awards that are ultimately expected to vest. The cost is recognized over the period during which an employee is required to provide services in exchange for the award. The tax benefit resulting from tax deductions in excess of the compensation cost recognized is classified as a financing activity in the statements of cash flows. There were no tax benefits realized as of December 31, 2016 and 2015.

Fair value measurements - Fair values of financial instruments are estimated using relevant market information and other assumptions as disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect these estimates.

Reclassifications - Certain reclassifications have been made to the prior-year financial statements in order to conform to the current-year presentation with no effect on net income or total stockholder's equity.

Note 2 - Investment Securities

Amortized cost and estimated fair values of investment securities are summarized as follows:

December 31, 2016	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale securities				
Obligations of U.S. agencies	$ 3,234,810	$ 80	$ (79,610)	$ 3,155,280
Agency mortgage-backed securities	5,777,295	1,834	(105,936)	5,673,193
Agency collateralized mortgage obligations	2,205,120	-	(27,548)	2,177,572
Corporate bonds	999,471	15,029	-	1,014,500
SBA participation cert	544,710	-	(21,897)	522,813
	$ 12,761,406	$ 16,943	$ (234,991)	$ 12,543,358
December 31, 2015				
Available-for-sale securities				
Obligations of U.S. agencies	$ 2,307,012	$ 49,799	$ (4,359)	$ 2,352,452
Agency mortgage-backed securities	4,224,280	33,780	(43,738)	4,214,322
Agency collateralized mortgage obligations	1,358,837	-	(24,231)	1,334,606
Corporate bonds	999,191	-	(14,511)	984,680
	$ 8,889,320	$ 83,579	$ (86,839)	$ 8,886,060
Held-to-maturity				
Corporate bonds	$ 999,745	$ 2,945	$ -	$ 1,002,690

The amortized cost and estimated fair value of investment securities at December 31, 2016, by contractual or expected maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-Sale	
	Amortized Cost	Estimated Fair Value
1 to 5 years	$ 1,226,351	$ 1,215,295
More than 5 years	11,535,055	11,328,063
	$ 12,761,406	$ 12,543,358

There were no investment securities pledged at December 31, 2016 or 2015.

Note 2 - Investment Securities (continued)

Information pertaining to investment securities with gross unrealized losses aggregated by investment category and length of time that individual securities have been in a continuous loss position is as follows at December 31:

	Less Than 12 Months		Greater Than 12 Months	
December 31, 2016	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value
Available-for-sale securities				
Obligations of U.S. agencies	$ (79,610)	$ 2,155,200	$ -	$ -
Agency mortgage-backed securities	(64,705)	2,919,181	(41,231)	2,525,826
Agency collateralized mortgage obligations	(4,327)	1,037,821	(23,221)	1,139,751
SBA participation cert	(21,897)	522,813	-	-
	$ (170,539)	$ 6,635,015	$ (64,452)	$ 3,665,577
December 31, 2015				
Available-for-sale securities				
Obligations of U.S. agencies	$ (4,359)	$ 494,135	$ -	$ -
Agency mortgage-backed securities	(21,634)	1,630,434	(22,104)	1,608,818
Agency collateralized mortgage obligations	(4,368)	767,315	(19,863)	567,291
Corporate bonds	(14,511)	984,680	-	-
	$ (44,872)	$ 3,876,564	$ (41,967)	$ 2,176,109

There were fifteen and nine securities in an unrealized loss position at December 31, 2016 and 2015, respectively. Unrealized losses have not been recognized into income because management does not intend to sell and does not expect it will be required to sell the investments. The decline is largely due to changes in market conditions and interest rates, rather than credit quality. The fair value is expected to recover as the underlying securities in the portfolio approach maturity date and market conditions improve. The Bank does not consider these securities to be other than temporarily impaired at December 31, 2016 or 2015.

There were three securities sold for gross realized gains of $27,624 and none for losses in 2016, and there were no securities sold in 2015.

Note 3 - Loans

The major classifications of loans at December 31 are summarized as follows:

	2016	2015
Residential 1-4 family	$ 14,818,260	$ 9,807,801
Residential multi-family	6,604,440	5,354,882
Residential construction, 1-4 family & multifamily	10,044,770	7,907,342
Home equity loans and lines of credit	1,685,920	1,516,890
C & I loans	26,892,441	24,594,304
Agriculture*	23,729,982	25,463,642
CRE land/development and construction	7,763,099	1,427,140
CRE income property - owner-occupied (OOC)	52,306,041	39,181,708
CRE income property - nonowner-occupied (NOC)	46,948,800	36,880,582
Consumer	1,239,053	945,697
	192,032,806	153,079,988
Deferred loan fees, net	(563,365)	(480,287)
Total loans	191,469,441	152,599,701
Allowance for loan losses	(2,974,275)	(2,555,069)
Total loans, net	$ 188,495,166	$ 150,044,632

*Balances included in Agriculture primarily consist of maritime loans.

The Bank pledged certain commercial, multi-family, and 1-4 family residential loans as collateral for purposes of borrowings with the FHLB and FRB. Loans totaling $48,327,718 and $64,307,423 were pledged to the FHLB at December 31, 2016 and 2015, respectively. There were $0 and $1,864,211 in loans pledged to the FRB at December 31, 2016 and 2015, respectively (Note 7).

Past due loans - Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due.

The following table presents past due loans, net of partial loan charge-offs, by type as of December 31, 2016 and 2015:

2016	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans
Residential 1-4 family	$ 393,066	$ -	$ 378,626	$ 771,692	$ 14,046,568	$ 14,818,260
Residential multi-family	-	-	-	-	6,604,440	6,604,440
Residential construction, 1-4 family and multifamily	-	-	-	-	10,044,770	10,044,770
Home equity loans and lines of credit	-	-	-	-	1,685,920	1,685,920
C & I loans	-	-	-	-	26,892,441	26,892,441
Agriculture	-	-	-	-	23,729,982	23,729,982
CRE land/development and construction	-	-	-	-	7,763,099	7,763,099
CRE income property - OOC	-	-	-	-	52,306,041	52,306,041
CRE income property - NOC	-	-	-	-	46,948,800	46,948,800
Consumer	-	-	-	-	1,239,053	1,239,053
	$ 393,066	$ -	$ 378,626	$ 771,692	$ 191,261,114	$ 192,032,806

Note 3 - Loans (continued)

2015	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans
Residential 1-4 family	$ -	$ -	$ 410,221	$ 410,221	$ 9,397,580	$ 9,807,801
Residential multi-family	-	-	-	-	5,354,882	5,354,882
Residential construction, 1-4 family and multifamily	-	-	-	-	7,907,342	7,907,342
Home equity loans and lines of credit	-	-	-	-	1,516,890	1,516,890
C & I loans	-	-	-	-	24,594,304	24,594,304
Agriculture	-	-	-	-	25,463,642	25,463,642
CRE land/development and construction					1,427,140	1,427,140
CRE income property - OOC	-	-	-	-	39,181,708	39,181,708
CRE income property - NOC	-	-	-	-	36,880,582	36,880,582
Consumer	-	-	-	-	945,697	945,697
	$ -	$ -	$ 410,221	$ 410,221	$ 152,669,767	$ 153,079,988

The following table presents the recorded investment in nonaccrual loans at December 31:

	2016	2015
Residential 1-4 family	$ 378,626	$ 410,221

There were no loans 90 days past due and still accruing at December 31, 2016 or 2015.

The following table presents loans individually evaluated for impairment by class of loans as of December 31, 2016 and 2015:

2016	Recorded Investments (Loan Balance Less Charge-off)	Unpaid Principal Balance	Related Allowance	Average Investment in Impaired Loans	Interest Income Recognized
With allowance recorded					
C & I loans	$ 112,298	$ 112,298	$ 25,747	$ 123,320	$ 7,788
With no allowance recorded					
Agriculture	3,685,433	3,685,433	-	3,891,523	198,925
Residential 1-4 family	378,626	378,626	-	392,073	-
	4,064,059	4,064,059	-	4,283,596	198,925
Total	$ 4,176,357	$ 4,176,357	$ 25,747	$ 4,406,916	$ 206,713
2015					
With allowance recorded					
C & I loans	$ 136,334	$ 136,334	$ 29,995	$ 147,030	$ 7,582
With no allowance recorded					
Agriculture	3,926,313	3,926,313	-	4,020,180	205,413
Residential 1-4 family	410,221	410,221	-	412,558	12,506
Total	$ 4,472,868	$ 4,472,868	$ 29,995	$ 4,579,768	$ 225,501

Note 3 - Loans (continued)

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by class and based on impairment method as of December 31, 2016 and 2015:

	Allowance for Loan Losses			Loans Receivable		
2016	Ending Balance	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment	Ending Balance	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment
Residential 1-4 family	$ 204,791	$ -	$ 204,791	$ 14,818,260	$ 378,626	$ 14,439,634
Residential multi-family	65,973	-	65,973	6,604,440	-	6,604,440
Residential construction, 1-4 family and multifamily	261,648	-	261,648	10,044,770	-	10,044,770
Home equity loans and lines of credit	26,059	-	26,059	1,685,920	-	1,685,920
C & I loans	450,937	25,747	425,190	26,892,441	112,298	26,780,143
Agriculture	396,118	-	396,118	23,729,982	3,685,433	20,044,549
CRE land/development and construction	73,576	-	73,576	7,763,099	-	7,763,099
CRE income property - OOC	751,853	-	751,853	52,306,041	-	52,306,041
CRE income property - NOC	707,696	-	707,696	46,948,800	-	46,948,800
Consumer	35,624	-	35,624	1,239,053	-	1,239,053
	$ 2,974,275	$ 25,747	$ 2,948,528	$ 192,032,806	$4,176,357	$ 187,856,449

	Allowance for Loan Losses			Loans Receivable		
2015	Ending Balance	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment	Ending Balance	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment
Residential 1-4 family	$ 168,752	$ -	$ 168,752	$ 9,807,801	$ 410,221	$ 9,397,580
Residential multi-family	73,759	-	73,759	5,354,882	-	5,354,882
Residential construction, 1-4 family and multifamily	242,283	-	242,283	7,907,342	-	7,907,342
Home equity loans and lines of credit	31,067	-	31,067	1,516,890	-	1,516,890
C & I loans	334,772	29,995	304,777	24,594,304	136,334	24,457,970
Agriculture	477,591	-	477,591	25,463,642	3,926,313	21,537,329
CRE land/development and construction	28,717	-	28,717	1,427,140	-	1,427,140
CRE income property - OOC	611,551	-	611,551	39,181,708	-	39,181,708
CRE income property - NOC	575,635	-	575,635	36,880,582	-	36,880,582
Consumer	10,942	-	10,942	945,697	-	945,697
	$ 2,555,069	$ 29,995	$ 2,525,074	$ 153,079,988	$4,472,868	$ 148,607,120

Note 3 - Loans (continued)

The following table presents the activity in the allowance for loan losses and impairment method by segment for the years ended December 31, 2016 and 2015:

2016	Beginning Balance	Provision for Loan Losses	Charge-offs	Recoveries	Ending Balance
Residential 1-4 family	$ 168,752	$ 66,039	$ (30,000)	$ -	$ 204,791
Residential multi-family	73,759	(7,786)	-	-	65,973
Residential construction, 1-4 family and multifamily	242,283	19,365	-	-	261,648
Home equity loans and lines of credit	31,067	(5,008)	-	-	26,059
C & I loans	334,772	92,994	-	23,171	450,937
Agriculture	477,591	(81,473)	-	-	396,118
CRE land/development and construction	28,717	18,824	-	26,035	73,576
CRE income property - OOC	611,551	140,302	-	-	751,853
CRE income property - NOC	575,635	132,061	-	-	707,696
Consumer	10,942	24,682	-	-	35,624
	$ 2,555,069	$ 400,000	$ (30,000)	$ 49,206	$ 2,974,275
2015					
Residential 1-4 family	$ 204,119	$ (35,367)	$ -	$ -	$ 168,752
Residential multi-family	62,362	11,397	-	-	73,759
Residential construction,		-			
1-4 family and multifamily	231,275	(21,211)	-	32,219	242,283
Home equity loans and lines of credit	57,323	(26,256)	-	-	31,067
C & I loans	424,567	(87,174)	(22,181)	19,560	334,772
Agriculture	464,426	13,165	-	-	477,591
CRE land/development and construction	40,541	(23,359)	-	11,535	28,717
CRE income property - OOC	323,871	287,680	-	-	611,551
CRE income property - NOC	583,821	(8,186)	-	-	575,635
Consumer	21,631	(10,689)	-	-	10,942
	$ 2,413,936	$ 100,000	$ (22,181)	$ 63,314	$ 2,555,069

Credit quality indicator - Federal regulations provide for the classification of lower quality loans and other assets, such as debt and equity securities, as substandard, doubtful, or loss. An asset is considered substandard if it is inadequately protected by the current net worth and pay capacity of the borrower or of any collateral pledged. Substandard assets include those characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all the weaknesses inherent in those classified substandard, with the added characteristic that the weaknesses present make collection or liquidation in full highly questionable and improbable on the basis of currently existing facts, conditions, and values. Assets classified as loss are those considered uncollectible and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted.

The extension of credit in the form of loans to individuals and businesses is one of the Bank's principal commerce activities. The Bank's policies and applicable laws and regulations require risk analysis, as well as ongoing portfolio and credit management. The Bank manages its credit risk through lending limit constraints, credit review, approval policies, and ongoing internal monitoring. The Bank also manages credit risk through diversification of the loan portfolio by type of loan, type of industry, type of borrower, and by limiting the aggregation of debt to a single borrower.

Note 3 - Loans (continued)

In analyzing the Bank's existing portfolio, risk ratings are assigned to each loan. These numeric ratings range in value from 1 to 10 and are based on the following criteria:

1. Ratings of 1-5 indicate low to minimal credit risk (pass).

2. Rating of 6 indicates an average to above average credit risk with adequate repayment capacity when prolonged periods of adversity do not exist (watch).

3. Rating of 7 indicates potential weaknesses and higher credit risk requiring greater attention by Bank personnel and management to help prevent further deterioration (special mention).

4. Rating of 8 indicates a loss is possible if loan weaknesses are not corrected (substandard).

5. Rating of 9 indicates loss is highly probable; however, the amount of the loss has not yet been determined (doubtful).

6. Rating of 10 indicates the loan is uncollectible and, when identified, is charged off (loss).

Periodically, the Bank reviews all loans to assess the ability of the borrowers to service all interest and principal obligations and, as a result, the risk rating may be adjusted accordingly. Risk ratings should be reviewed and updated whenever appropriate, with more periodic reviews as the risk and dollar value of loss on the loan increases. In the event that full collection of principal and interest is not reasonably ensured, the loan is appropriately downgraded and, if warranted, placed on nonaccrual status even though the loan may be current as to principal and interest payments. Additionally, the Bank assesses whether an impairment of a loan warrants specific reserves or a write-down of the loan.

The following table represents the internally assigned grade as of December 31 by type of loans:

2016	Pass/Watch	Special Mention	Substandard	Doubtful	Loss	Total
Residential 1-4 family	$ 14,152,681	$ 286,953	$ 378,626	$ -	$ -	$ 14,818,260
Residential multi-family	6,604,440	-	-	-	-	6,604,440
Residential construction, 1-4 family and multifamily	10,044,770	-	-	-	-	10,044,770
Home equity loans and lines of credit	1,552,098	133,822	-	-	-	1,685,920
C & I loans	24,638,869	2,225,498	28,074	-	-	26,892,441
Agriculture	18,729,969	371,866	4,628,147	-	-	23,729,982
CRE land/development and construction	7,763,099	-	-	-	-	7,763,099
CRE income property - OOC	49,728,358	2,577,683	-	-	-	52,306,041
CRE income property - NOC	44,058,353	2,890,447	-	-	-	46,948,800
Consumer	1,208,505	30,548	-	-	-	1,239,053
	$ 178,481,142	$ 8,516,817	$ 5,034,847	$ -	$ -	$ 192,032,806

Note 3 - Loans (continued)

2015	Pass/Watch	Special Mention	Substandard	Doubtful	Loss	Total
Residential 1-4 family	$ 8,860,336	$ 537,244	$ 410,221	$ -	$ -	$ 9,807,801
Residential multi-family	5,354,882	-	-	-	-	5,354,882
Residential construction, 1-4 family and multifamily	7,907,342	-	-	-	-	7,907,342
Home equity loans and lines of credit	1,315,291	201,599	-	-	-	1,516,890
C & I loans	24,091,357	468,864	34,083	-	-	24,594,304
Agriculture	20,089,135	431,093	4,943,414	-	-	25,463,642
CRE land/development and construction	1,427,140	-	-	-	-	1,427,140
CRE income property - OOC	39,181,708	-	-	-	-	39,181,708
CRE income property - NOC	33,928,507	2,952,075	-	-	-	36,880,582
Consumer	945,697	-	-	-	-	945,697
	$ 143,101,395	$ 4,590,875	$ 5,387,718	$ -	$ -	$ 153,079,988

Loans classified as troubled debt restructurings (TDRs) totaled $3,713,507 and $3,960,396 at December 31, 2016 and 2015, respectively. These loans are included in the impaired loan disclosures. A troubled debt restructuring is a loan to a borrower that is experiencing financial difficulty that has been modified from its original terms and conditions in such a way that the Bank is granting the borrower a concession of some kind. The Bank has granted a variety of concessions to borrowers in the form of loan modifications.

The following table presents newly restructured TDR loans by class that occurred during the years ended December 31 by type of concession granted:

2016	Number of Contracts	Payment Modification	Combination Modification	Total Modifications
Pre and post-modification outstanding recorded investment				
Agriculture	2	$ 1,684,228	$ 1,271,365	$ 2,955,593
2015				
Pre and post-modification outstanding recorded investment				
C & I loans	1	$ 34,083	$ -	$ 34,083
Agriculture	3	2,472,933	1,453,380	3,926,313

There were no TDR loans that were modified within the prior 12 months that subsequently defaulted during the years ended December 31, 2016 or 2015.

The Bank had no commitments to extend additional credit to borrowers owing loans whose terms have been modified in troubled debt restructurings.

Note 4 - Leaseholds and Equipment

Bank leaseholds and equipment at December 31 are classified as follows:

	2016	2015
Leasehold improvements	$ 1,672,694	$ 1,648,257
Furniture, fixtures, and office equipment	1,244,630	1,183,403
	2,917,324	2,831,660
Accumulated depreciation and amortization	(2,467,951)	(2,173,214)
	$ 449,373	$ 658,446

Note 5 - Other Real Estate Owned

The following table presents other real estate owned as of December 31:

	2016	2015
Beginning balance	$ 5,340,420	$ 5,609,998
Capitalized improvements	128,965	-
Sales	(539,110)	(269,578)
Ending balance	$ 4,930,275	$ 5,340,420

Other real estate owned as of December 31, 2016, consists of land and a single-family residence.

Note 6 - Deposits

Deposits as of December 31 consisted of the following:

	2016	2015
Savings accounts	$ 4,836,411	$ 3,173,175
Certificates of deposit	53,548,301	49,805,038
Demand accounts		
Noninterest-bearing	35,096,445	31,088,351
Interest-bearing	21,390,070	14,706,473
Money market accounts	89,435,166	65,075,823
	$ 204,306,393	$ 163,848,860

At December 31, 2016, scheduled maturities of certificates of deposit are as follows:

2017	$ 31,791,820
2018	17,786,764
2019	2,027,294
2020	961,598
2021	980,825
	$ 53,548,301

Note 6 – Deposits (continued)

The Bank had $7,330,119 and $6,487,487 of certificates of deposit that met or exceeded the $250,000 federally insured limit at December 31, 2016 and 2015, respectively.

Note 7 - Credit Arrangements

As of December 31, 2015, the Bank had a committed line of credit through the Federal Reserve Bank of San Francisco for a discounted rate based on the type of loans pledged as collateral (Note 3). Loans pledged to the FRB equated to a borrowing capacity of $1,361,041 and no outstanding balance at December 31, 2015. There was no committed line of credit at December 31, 2016.

The Bank has line-of-credit agreements with separate unaffiliated banks totaling $2,000,000 and $10,000,000, subject to certain collateral requirements. These two lines provide for lending at the corresponding bank's federal fund rates. There were no borrowings outstanding on either of these lines at December 31, 2016 and 2015.

The Bank is a member of the FHLB of Des Moines and, as such, has a committed credit line of up to 20% of total eligible assets, subject to certain collateral requirements. Borrowings generally provide for interest at the then-current published rates. At December 31, 2016 and 2015, loans pledged to the FHLB equated to a borrowing capacity of $33,232,836 and $33,229,245, respectively. At December 31, 2016 and 2015, the Bank had $2,000,000 and $5,000,000 of borrowings, respectively, outstanding with the FHLB, with fixed rates ranging from 0.83% to 0.85% under these agreements. The borrowings have a weighted-average interest rate of 0.84% and 0.70% as of December 31, 2016 and 2015, respectively. Current borrowings are collateralized by pledged loans (Note 3).

All $2,000,000 of the FHLB advances held at December 31, 2016, have contractual maturities that occur in 2017.

Note 8 - Federal Income Taxes

The components of the federal income tax expense are as follows at December 31:

	2016	2015
Current	$ 280,000	$ -
Deferred	250,000	425,000
	$ 530,000	$ 425,000

Note 8 - Federal Income Taxes (continued)

The following are the significant components of the Bank's deferred tax assets and liabilities at December 31:

	2016	2015
Deferred tax asset		
Allowance for loan losses	$ 423,589	$ 287,589
Net operating loss carryforward	2,172,016	2,454,911
Organization expenditures	37,098	46,250
OREO valuation adjustments	680,122	670,020
Nonaccrual interest	10,438	3,774
Property and equipment depreciation	77,947	42,669
Unrealized losses on securities	76,108	1,108
Other	16,942	127,317
Subtotal	3,494,260	3,633,638
Deferred tax liabilities		
Deferred loan costs	121,090	108,638
SBA servicing asset	23,170	-
Subtotal	144,260	108,638
Net deferred tax asset	$ 3,350,000	$ 3,525,000

Pursuant to Sections 382 and 383 of the Internal Revenue Code, annual use of net operating loss and credit carryforwards may be limited in the event a cumulative change in ownership of more than 50% occurs within a three-year period. The Bank determined such an ownership change occurred as of December 12, 2011, as a result of the exercise of stock warrants. This ownership change results in annual limitations on the use of net operating loss carryforwards and may limit the Bank's ability to fully utilize its deferred tax assets. The deferred tax asset associated with the net operating loss carryforward reflects preliminary limitations based on the filed 2011 tax return.

The Bank has federal net operating loss carryforwards of approximately $6,843,000 at December 31, 2016, before the consideration of any Section 382 limits. Federal net operating loss carryforwards, to the extent not used, will begin to expire in 2029.

A valuation allowance is required for deferred tax assets if, based on available evidence, it is more-likely-than-not that all or some portion of the asset will not be realized due to the inability to generate sufficient taxable income to use the benefit of the deferred tax asset. After evaluating the positive and negative evidence associated with the deferred tax asset, including the consideration of the Bank's earnings history over the recent three-year period and improving asset quality, the Bank determined that no valuation allowance is necessary at December 31, 2016.

The variance between recording tax at the statutory rate of 34% and tax expense actually recorded primarily relates to the change in the valuation allowance.

At December 31, 2016, the Bank had unamortized preopening expenditures of approximately $109,000 (for tax reporting purposes) that can be used to offset future federal income taxes. These expenditures are amortizing at a rate of approximately $24,000 per year.

At December 31, 2016 and 2015, the Bank had no unrecognized tax benefits. The Bank recognizes interest accrued and penalties related to unrecognized tax benefits in tax expense. During the years ended December 31, 2016 and 2015, the Bank recognized no interest and penalties. The Bank files income tax returns in the U.S. federal jurisdiction. With few exceptions, the Bank is no longer subject to U.S. federal income tax examinations by tax authorities for years before 2013.

Note 9 - Employee Benefits

The Bank has a 401(k) defined contribution plan (the 401k Plan) for those employees who meet the eligibility requirements set forth in the 401(k) Plan. Eligible employees can contribute up to 100% of compensation subject to certain limits based on federal tax laws. The 401(k) Plan also allows for discretionary employer matching contributions equal to 100% up to the first 3%, and 50% up to the next 2% of compensation. Matching contributions vest immediately. The Bank's contribution for the years ended December 31, 2016 and 2015, was $85,819 and $80,152, respectively.

Note 10 - Stockholders' Equity

Warrants - At December 31, 2015, there were warrants outstanding to purchase 107,500 shares of the Bank's common stock at $10 per share, which were issued in connection with the Bank's initial offering. During 2016, 500 warrants were exercised, and on September 15, 2016, the remaining 107,000 warrants to purchase the Bank's common stock at $10 per share, related to the Bank's initial offering, expired.

Regulatory capital - The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory—and possibly additional discretionary—actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items, as calculated under regulatory accounting practices. The Bank's capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

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

To be categorized as adequately capitalized, the Bank must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios, as set forth in the table. The institution is well capitalized under the prompt corrective action provisions.

As of December 31, 2016, the most recent notification from the FDIC categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios, as set forth in the following table. There are no conditions or events since the notification that management believes have changed the Bank's category.

Note 10 - Stockholders' Equity (continued)

The Bank's actual capital amounts and ratios as of December 31 are also presented in the table.

	Actual		For Capital Adequacy Purposes			To Be Well Capitalized Under Prompt Corrective Action Provisions		
	Amount	Ratio	Amount		Ratio	Amount		Ratio
As of December 31, 2016								
Total capital (to risk-weighted assets)	$ 26,213,000	12.4%	$ 16,911,613	≥	8.0%	$ 21,139,516	≥	10.0%
Tier I capital (to risk-weighted assets)	23,548,000	11.1%	12,728,649	≥	6.0%	16,971,532	≥	8.0%
Common equity Tier 1 capital (to risk-weighted assets)	23,548,000	11.1%	9,546,486	≥	4.5%	13,789,369	≥	6.5%
Tier I capital (to average assets)	23,548,000	10.6%	8,886,038	≥	4.0%	11,107,547	≥	5.0%
As of December 31, 2015								
Total capital (to risk-weighted assets)	$ 24,642,000	13.9%	$ 14,151,902	≥	8.0%	$ 17,689,878	≥	10.0%
Tier I capital (to risk-weighted assets)	22,408,000	12.7%	10,611,523	≥	6.0%	14,148,698	≥	8.0%
Common equity Tier 1 capital (to risk-weighted assets)	22,408,000	12.7%	7,958,642	≥	4.5%	11,495,817	≥	6.5%
Tier I capital (to average assets)	22,408,000	12.2%	7,334,861	≥	4.0%	9,168,576	≥	5.0%

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 0.0% for 2015 to 2.50% by 2019. The capital conservation buffer for 2016 is 0.625%. The net unrealized gain or loss on available-for-sale securities is not included in computing regulatory capital. Management believes as of December 31, 2016, the Bank meets all capital adequacy requirements to which they are subject.

Note 11 - Lease Commitments

Operating lease commitments - The Bank leases its office, administrative, and loan operations space at standard market rates from a related party LLC of which two directors are members. The Everett branch has a 12-year term, with an option to renew for two 5-year terms, and a loan operations space that has a 10-year lease ending in May 2018, with an option to renew for two 5-year terms to be mutually determined at that time. Total amounts paid to the related entity for Everett lease space were $294,815 and $268,193 for the years ended December 31, 2016 and 2015, respectively.

The Bank entered into a new lease agreement with an unaffiliated party for the Ballard Branch location beginning in September 2015. The lease is a three-year lease ending August 2018 and contains two renewal options for three years each.

The Bank also has a lease agreement with an unaffiliated party for the Lynnwood office. The lease is a 10-year lease ending January 2018, and contains an option to renew for two 5-year terms at rates to be mutually determined at that time.

Note 11 - Lease Commitments (continued)

All lease agreements require the Bank to pay its pro rata share of building operating expenses. The minimum annual lease payments through the initial lease term for the years ending December 31 are as follows:

2017	$ 431,233
2018	141,186
	$ 572,419

Rental expense charged to operations was $487,194 and $469,643 for the years ended December 31, 2016 and 2015, respectively.

Subsequent to year-end, the Bank entered into a purchase and sale agreement for $11,400,000 to acquire the current main branch building and select adjacent buildings in Everett, Washington, for the purposes of continued operations. The transaction is expected to close in 2017.

Note 12 - Stock-Based Compensation Plan

The Bank has one stock-based compensation plan, which is described below. The total compensation cost for restricted stock and stock options that has been charged against operations for the plan was $111,959 in 2016 and $67,902 in 2015. There was no compensation cost capitalized and no income tax benefits realized on these stock-based compensation arrangements in 2016 or 2015.

Stock option plan - In December 2006, stockholders approved an equity incentive plan (the Plan) to promote the best interest of the Bank by providing an incentive to those key employees who contribute to its success. The Plan permits the grant of incentive stock options for employees, nonqualified stock options for directors, and restricted stock grants. The maximum amount of common stock that may be issued under the Plan is 330,000 shares, of which there are 66,000 shares available for restricted stock grants. During 2012, stockholders approved an amendment to the Plan, increasing the number of authorized shares to 800,000 available for options, of which there are 400,000 shares available for restricted stock grants. This plan expired during 2016.

Incentive stock and nonqualified stock option awards are generally granted with an exercise price equal to the market price of the Bank's stock at the date of grant; those option awards generally vest and become exercisable in incremental percentages from one to five years of continuous service from the grant date, and expire after 10 years. Certain option and share awards provide for accelerated vesting upon death of the optionee or if there is a change in control (as defined in the Plan).

Restricted stock grants vest ratably over three to five years from the date of grant. The fair value equals their value on the date of grant.

The fair value of each option award is estimated on the date of grant using the Black-Scholes-Merton valuation model that uses the assumptions noted in the following table. Expected volatilities are based on historical volatility of the Bank's stock and other factors. The expected term of options granted was evaluated by a calculation that factored in the contractual term and vesting period, and considered different employee segments. The risk-free interest rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

	2016	2015
Risk-free interest rate	1.90%-2.06%	2.04%
Dividend yield rate	0.00%	0.00%
Expected volatility	35%	30%
Expected term (in years)	6.5 years	6.5 years

Note 12 - Stock-Based Compensation Plan (continued)

A summary of incentive and nonqualified stock option activity is presented below:

	Granted Options for Common Stock	Weighted-Average Exercise Price of Shares Under Plan	Weighted-Average Remaining Contractual Term (Years)
Outstanding at December 31, 2015	330,560	$ 3.05	
Granted	160,000	3.45	
Exercised	(11,780)	3.02	
Forfeited	(21,160)	3.21	
Outstanding at December 31, 2016	457,620	$ 3.18	6.63
Options exercisable at December 31, 2016	199,320	$ 3.00	3.97

The weighted-average grant-date fair value of options granted was $1.31 and $1.09 for each of the years ended December 31, 2016 and 2015. As of December 31, 2016, there was $196,262 of total unrecognized compensation cost related to incentive and nonqualified stock options granted under the Plan. That cost is expected to be recognized over a weighted-average period of two years. There were no tax benefits realized from the exercise of options in 2016 or 2015.

Restricted stock grants - The fair value of restricted stock grants is determined based on the last trade price or most recent stock valuation on the grant date. A summary of nonvested restricted stock grants activity is presented below:

	Shares	Weighted-Average Grant-Date Fair Value
Nonvested at December 31, 2015	14,165	$ 3.08
Granted	8,000	3.45
Vested	(6,630)	3.08
Forfeited	-	-
Nonvested at December 31, 2016	15,535	$ 3.27

As of December 31, 2016, there was $28,873 of total unrecognized compensation cost related to restricted stocks granted under the Plan. That cost is expected to be recognized over a weighted-average period of approximately three years.

Note 13 - Related Party Transactions

Certain directors, executive officers, and principal stockholders are Bank customers and have had banking transactions with the Bank. All loans and commitments included in such transactions were made in compliance with applicable laws on substantially the same terms (including interest rates and collateral) as those prevailing at the time for comparable transactions with other persons and do not involve more than the normal risk of collectibility or present any other unfavorable features. The following summarizes these transactions with directors, executive officers, principal stockholders, and companies with which they are associated at December 31:

	2016	2015
Beginning balance	$ 3,935,140	$ 3,082,781
New loans	856,708	1,228,149
Repayments	(201,202)	(339,392)
Transfers out	-	(36,398)
Ending balance	$ 4,590,646	$ 3,935,140
Deposits	$ 11,994,292	$ 8,831,286

The Bank leases office space from a related party LLC, of which two directors are members (Note 11).

MPB Directors Buildout LLC, as described in Note 1, did not have any activity or agreements outstanding at December 31, 2016 or 2015.

Note 14 - Commitments and Contingencies

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit, standby letters of credit, and financial guarantees. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheets. The contract or notional amounts of those instruments reflect the extent of the Bank's involvement in particular classes of financial instruments.

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

Commitments to extend credit and financial guarantees - 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. Because many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank's experience has been that approximately 81% of loan commitments are drawn upon by customers. The Bank evaluates customers' creditworthiness on a case-by-case basis and follows the Bank's normal credit policies. The amount of collateral obtained, if it is deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, income-producing commercial properties, and other real estate.

The distribution of commitments to extend credit approximates the distribution of loans outstanding. Commercial and standby letters of credit were granted primarily to commercial borrowers. The Bank, as a matter of policy, does not extend credit in excess of 20% of Tier I capital, or $5.0 million, to any single borrower or group of related borrowers.

Note 14 - Commitments and Contingencies (continued)

Standby letters of credit and financial guarantees written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing, and similar transactions. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank maintains various levels of collateral supporting those commitments for which collateral is deemed necessary.

The Bank has not been required to perform on any financial guarantees. The Bank has not incurred any losses on its commitments in 2016 or 2015.

A summary of the notional amounts of the Bank's financial instruments with off-balance-sheet risk at December 31 follows:

	2016	2015
Commitments to extend credit	$ 46,272,503	$ 41,821,174
Standby letters of credit	$ 302,791	$ 198,327

Legal contingencies - Various legal claims also arise from time to time in the normal course of business that, in the opinion of management, will have no material effect on the Bank's financial statements.

Note 15 - Fair Value of Financial Instruments

Fair value is the price to sell an asset or transfer a liability in an orderly transaction between market participants in the Bank's principal market. The Bank has established and documented its process for determining the fair values of its assets and liabilities, where applicable. Fair value is based on quoted market prices, when available, for identical or similar assets or liabilities. In the absence of quoted market prices, management determines the fair value of the Bank's assets and liabilities using valuation models or third-party pricing services, both of which rely on market-based parameters when available, such as interest rate yield curves, option volatilities and credit spreads, or unobservable inputs. Unobservable inputs may be based on management's judgment, assumptions, and estimates related to credit quality, liquidity, interest rates, and other relevant inputs.

Valuation adjustments, such as those pertaining to counterparty and the Bank's own credit quality and liquidity, may be necessary to ensure that assets and liabilities are recorded at fair value. Credit valuation adjustments are made when market pricing is not indicative of the counterparty's credit quality.

Any changes to valuation methodologies are reviewed by management to ensure that they are relevant and justified. Valuation methodologies are refined as more market-based data becomes available.

There are three levels of inputs that may be used to measure fair values:

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 - Either (i) quoted prices for similar assets or liabilities; (ii) observable inputs, such as interest rates or yield curves; or (iii) inputs derived principally from or corroborated by observable market data.

Level 3 - Unobservable inputs.

The hierarchy gives the highest ranking to Level 1 inputs and the lowest ranking to Level 3 inputs. The level in the fair value hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the overall fair value measurement.

Note 15 - Fair Value of Financial Instruments (continued)

Qualitative disclosures of valuation techniques

Investment securities - Where quoted prices are available in an active market, securities are classified as Level 1. Level 1 instruments include highly liquid government bonds, securities issued by the U.S. Treasury, and exchange-traded equity securities. If quoted prices are not available, management determines fair value using pricing models, quoted prices of similar securities, or discounted cash flows. Such instruments are classified as Level 2. In certain cases where there is limited activity in the market for a particular instrument, assumptions must be made to determine its fair value. Such instruments are classified as Level 3.

Assets measured at fair value on a recurring basis - Assets are considered to be fair valued on a recurring basis if fair value is measured regularly (i.e., daily, weekly, monthly, or quarterly). The following table shows the Bank's assets and liabilities measured at fair value on a recurring basis:

	Level 1	Level 2	Level 3	Total
2016				
Obligations of U.S. agencies	$ -	3,155,280	$ -	$ 3,155,280
Agency mortgage-backed securities	-	5,673,193	-	5,673,193
Agency collateralized mortgage obligations	-	2,177,572	-	2,177,572
Corporate bonds	-	1,014,500	-	1,014,500
SBA participation cert		522,813		522,813
2015				
Obligations of U.S. agencies	$ -	$ 2,352,452	$ -	$ 2,352,452
Agency mortgage-backed securities	-	4,214,322	-	4,214,322
Agency collateralized mortgage obligations	-	1,334,606	-	1,334,606
Corporate bonds	-	984,680	-	984,680

Assets measured at fair value on a nonrecurring basis - Assets are considered to be fair valued on a nonrecurring basis if the fair value measurement of the instrument does not necessarily result in a change in the amount recorded on the balance sheets. Generally, nonrecurring valuation is the result of the application of other accounting pronouncements that require assets or liabilities to be assessed for impairment or recorded at the lower of cost or fair value. The following table presents the Bank's assets measured at fair value on a nonrecurring basis:

	Level 1	Level 2	Level 3	Total
December 31, 2016				
Impaired loans	$ -	$ -	$ 2,328	$ 2,328
Other real estate owned	-	-	4,930,275	4,930,275
December 31, 2015				
Impaired loans	$ -	$ -	$ 4,088	$ 4,088
Other real estate owned	-	-	5,340,420	5,340,420

Valuations of impaired loans are periodically performed by management, and the fair value of the loans is carried at the fair value of the underlying collateral less cost to foreclose, sell, and carry the collateral. Fair value of the underlying collateral is determined by an appraisal performed by a qualified independent appraiser. Other real estate owned is valued in a similar manner as impaired loans.

Note 15 - Fair Value of Financial Instruments (continued)

Quantitative information about Level 3 fair value measurements - The range and weighted average of the significant unobservable inputs used to fair value Level 3 nonrecurring assets during the years ending December 31, 2016 and 2015, along with the valuation techniques used, are shown in the following table:

		Fair Value at December 31, 2016	Valuation Technique	Unobservable Input	Range[1]
Impaired loans	$	2,328	Market comparable	Adjustment to appraisal value	0% - 10%
OREO	$	4,930,275	Market comparable	Adjustment to appraisal value	0% - 10%

[1] Discount for selling costs.

		Fair Value at December 31, 2015	Valuation Technique	Unobservable Input	Range[1]
Impaired loans	$	4,088	Market comparable	Adjustment to appraisal value	0% - 10%
OREO	$	5,340,420	Market comparable	Adjustment to appraisal value	0% - 10%

[1] Discount for selling costs.

The fair value estimates on the following page are subjective in nature and involve uncertainties and matters of significant judgment; therefore, they are not necessarily indicative of the amounts the Bank could realize in a current market exchange. The Bank has not included certain material items in its disclosure, such as the value of the long-term relationships with the Bank's lending and deposit clients, since this is an intangible and not a financial instrument. Additionally, the estimates do not include any tax ramifications. There may be inherent weaknesses in any calculation technique and changes in the underlying assumptions used, including discount rates and estimates of future cash flows that could materially affect the results. For all of these reasons, the aggregation of the fair value calculations presented herein do not represent, and should not be construed to represent, the underlying value of the Bank.