Commencement Bank

Financial Report
December 31, 2015 and 2014

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Financial Report

December 31 2015 and 2014

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FORTNER, BAYENS, LEVKULICH
■
& GARRISON, P.C.

Independent Auditors' Report

Board of Directors
Commencement Bank
Tacoma, Washington

Report on the Financial Statements

We have audited the accompanying financial statements of Commencement Bank, which are comprised of the balance sheets as of December 31, 2015 and 2014, and the related statements of income, comprehensive income, 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.

Auditors' 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 of material misstatement.

An audit includes 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 Commencement Bank as of December 31, 2015 and 2014, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Fortner, Bayens, Levkulich & Garrison, P.C.

Denver, Colorado
March 30, 2016

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Certified Public Accountants • A Professional Corporation

Financial Statements

Balance Sheets

(Dollars in Thousands)

Commencement Bank
December 31, 2015 and 2014

	2015	2014
Assets		
Cash and due from banks	$ 4,026	$ 3,795
Interest-bearing deposits in other financial institutions	21,224	22,007
Cash and cash equivalents	25,250	25,802
Federal Funds Sold	5	-
Securities available for sale	3,387	2,929
Federal Home Loan Bank stock, at cost	329	284
Federal Reserve Bank stock, at cost	666	631
Loans	145,086	133,410
Allowance for credit losses	(1,962)	(1,851)
Net loans	143,124	131,559
Premises and equipment, net	600	698
Other real estate owned	338	642
Cash surrender value of life insurance	4,375	4,217
Accrued interest receivable	319	327
Other assets	673	565
Total assets	$179,066	$167,654
Liabilities and Shareholders' Equity		
Liabilities		
Deposits:		
Demand, noninterest-bearing	$ 28,301	$ 24,394
Savings and interest-bearing demand	66,174	65,183
Time	58,154	53,060
Total deposits	152,629	142,637
FHLB Borrowings	3,200	3,200
Accrued interest payable	27	23
Other liabilities	671	273
Total liabilities	156,527	146,133
Commitments and Contingencies (Note 9)	- -	- -
Shareholders' Equity		
Common stock (par value: $1); authorized 10,000,000 shares; 2,219,500 shares issued and outstanding in 2015 and 2014	2,219	2,219
Additional paid in capital	20,949	20,911
Accumulated deficit	(644)	(1,631)
Accumulated other comprehensive income (loss)	15	22
Total shareholders' equity	22,539	21,521
Total liabilities and shareholders' equity	$179,066	$167,654

See notes to financial statements.

Statements of Income

(Dollars in Thousands)

Commencement Bank
For the Years Ended December 31, 2015 and 2014

	2015	2014
Interest and Dividend Income		
Loans	$6,977	$6,564
Interest-bearing deposits in other financial institutions	62	45
Securities available for sale	51	66
Dividends on Federal Reserve Bank and FHLB Stock	41	37
Total interest income	7,131	6,712
Interest Expense		
Deposits	731	726
Long-term borrowings	28	28
Total interest expense	759	754
Net interest income	6,372	5,958
Provision for Credit Losses	(121)	45
Net interest income after provision for credit losses	6,493	5,913
Noninterest Income		
Service charges on deposit accounts	148	175
Gain (loss) on other real estate owned	70	(5)
Gain on sale of available for sale security	1	8
Other	274	237
Total noninterest income	493	415
Noninterest Expense		
Salaries and employee benefits	3,302	2,973
Occupancy	379	352
Furniture and equipment	97	103
Data processing	362	342
Marketing and development	72	109
Other	1,121	1,129
Total noninterest expense	5,333	5,008
Net Income Before Income Taxes	1,653	1,320
Income Tax Expense	511	400
Net Income	1,142	920
Basic earnings per share	$0.51	$0.41
Diluted earnings per share	$0.51	$0.41

See notes to financial statements.

Statements of Comprehensive Income

(Dollars in Thousands)

Commencement Bank
For the Years Ended December 31, 2015 and 2014

	2015	2014
Other Comprehensive Income		
Unrealized gains (losses) on available for sale securities	($6)	$51
Reclassification adjustment for gain realized in net income	1	(8)
Tax effect	(2)	(14)
Total other comprehensive income (loss)	(7)	29
Total Comprehensive Income	$1,135	$949

See notes to financial statements.

Statements of Shareholders' Equity
(Dollars in Thousands, Except Share Information)

Commencement Bank
For the Years Ended December 31, 2015 and 2014

	Shares of Common Stock	Common Stock	Additional Paid in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (loss)	Total
Balance at December 31, 2013	2,219,500	$2,219	$20,893	($2,551)	$(7)	$20,554
Net income	- -	- -	- -	920	- -	920
Other comprehensive loss	- -	- -	- -	- -	29	29
Stock-based compensation expense	- -	- -	18	- -	- -	18
Balance at December 31, 2014	2,219,500	2,219	20,911	(1,631)	22	21,521
Net income	- -	- -	- -	1,142	- -	1,142
Other comprehensive income	- -	- -	- -	- -	(7)	(7)
Stock-based compensation expense	- -	- -	38	- -	- -	38
Cash dividend	- -	- -	- -	(155)	- -	(155)
Balance at December 31, 2015	2,219,500	$2,219	$20,949	($644)	$15	$22,539

See notes to financial statements.

Statements of Cash Flows

(Dollars in Thousands)

Commencement Bank
For the Years Ended December 31, 2015 and 2014

	2015	2014
Cash Flows from Operating Activities		
Net Income	$1,142	$920
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	(121)	45
Loan recoveries	232	224
Depreciation and amortization	160	166
Stock-based compensation expense	38	18
Net amortization of premium on securities available for sale	41	45
Gain on sale of available for sale investment securities	(1)	(8)
Deferral of loan origination costs and fees, less amortization	72	38
Increase in cash surrender value of life insurance	(158)	(141)
(Gain) loss on sale of other real estate owned	(70)	- -
Write-down of other real estate owned	- -	5
Deferred federal income tax	(36)	415
Decrease in accrued interest receivable	8	21
Increase (decrease) in accrued interest payable	4	(6)
Other	312	182
Net cash provided by operating activities	1,623	1,924
Cash Flows from Investing Activities		
Activity in securities available for sale:		
Maturities, prepayments and calls	409	703
Sales	997	995
Purchases	(1,914)	- -
(Increase) decrease in federal funds sold	(5)	10
Purchase of Federal Home Loan Bank and Federal Reserve Bank stock	(259)	(28)
Sale of Federal Home Loan Bank and Federal Reserve Bank stock	179	11
Increase in loans made to customers, net of principal collections	(11,748)	(5,474)
Proceeds from sale of other real estate owned	374	53
Purchases of premises, equipment and software	(45)	(91)
Net cash used in investing activities	(12,012)	(3,821)
Cash Flows from Financing Activities		
Net increase (decrease) in deposits	9,992	(4,087)
Payment of cash dividend	(155)	- -
Net cash provided by (used in) financing activities	9,837	(4,087)
Net change in cash and cash equivalents	(552)	(5,984)
Cash and Cash Equivalents		
Beginning of period	25,802	31,786
End of period	$25,250	$25,802
Supplemental Disclosure of Cash Flow Information		
Interest paid	$755	$760
Income taxes paid	$380	$15

See notes to financial statements.

Commencement Bank
December 31, 2015 and 2014

Note 1 - Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Commencement Bank (the Bank), opened December 11, 2006, and operates one branch in Tacoma, Washington and two loan production offices in Enumclaw and Auburn, Washington. The Bank provides loan and deposit services to customers, who are predominately individuals and small and midsized businesses in western Washington.

Financial Statement Presentation

Preparation of financial statements in conformity with accounting principles generally accepted in the United States of America and practices within the banking industry requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities, as of the date of the balance sheet, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for credit losses and the valuation of deferred tax assets. All dollar amounts are stated in thousands.

Subsequent Events

Management evaluates events occurring subsequent to the balance sheet date, through the date the financial statements are eligible to be issued, to determine whether the events require recognition or disclosure in the financial statements. If a subsequent event evidences conditions existing at the balance sheet date, the effects are recognized in the financial statements (recognized subsequent event). If a subsequent event evidences conditions arising after the balance sheet date, the effects are not recognized in the financial statements but rather disclosed in the notes to the financial statements (non-recognized subsequent events). The effects of subsequent events are only recognized if material, or disclosed if the financial statements would otherwise be misleading.

With respect to the December 31, 2015 financial statements, Management has considered subsequent events through March 30, 2016, which is the date the financial statements were available to be issued.

Securities Available for Sale

Securities available for sale consist of debt securities that the Bank intends to hold for an indefinite period but not necessarily to maturity. Such securities may be sold to implement the Bank's asset and liability management strategies and in response to changes in interest rates and similar factors. Securities available for sale are reported at fair value. Unrealized gains and losses, net of the related deferred tax effect, are reported as a net amount in a separate component of shareholders' equity entitled "accumulated other comprehensive income." Realized gains and losses on securities available for sale, determined using the specific-identification method, are included in earnings. Amortization of premiums and accretion of discounts are recognized in interest income over the period to maturity. For mortgage-backed securities, actual maturity may differ from contractual maturity due to principal payments and amortization of premiums and accretion of discounts may vary due to prepayment speed assumptions.

Commencement Bank
December 31, 2015 and 2014

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

Securities Available for Sale (continued)

Management evaluates securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as an impairment charge to earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which is recognized as an impairment charge to earnings, and 2) OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. For equity securities, the entire amount of impairment is recognized through earnings.

Federal Home Loan Bank of Des Moines Stock

In May 2015, the Federal Home Loan Bank of Seattle merged into the Federal Home Loan Bank of Des Moines. All stock held by the Bank was converted to the Federal Home Loan Bank of Des Moines at that time. The Bank, as a member of the Federal Home Loan Bank of Des Moines (FHLB), is required to maintain an investment in capital stock of the FHLB in an amount equal to the greater of 0.12 percent of total assets and or 4.0 percent of advances from the FHLB. The recorded amount of the FHLB stock equals its fair value because the shares can be redeemed only by the FHLB at the $100 per share par value. The Bank views its investment in the FHLB stock as a long-term investment. Accordingly, when evaluating for impairment, the value is determined based on the ultimate recovery of the par value rather than recognizing temporary declines in value. The determination of whether a decline affects the ultimate recovery is influenced by criteria such as: 1) the significance of the decline in net assets of the FHLB as compared to the capital stock amount and length of time a decline has persisted; 2) impact of legislative and regulatory changes on the FHLB and 3) the liquidity position of the FHLB.

Federal Reserve Bank of San Francisco Stock

The Bank, as a member of the Federal Reserve Bank of San Francisco (FRB), is required to subscribe to Federal Reserve Stock in an amount equivalent to 6 percent of its capital and surplus. Although the par value of the stock is $100 per share, banks pay only $50 per share at the time of purchase, with the understanding that the other half of the subscription amount is subject to call at any time. The recorded amount of the FRB stock equals its fair value because the shares can be redeemed only by the FRB at the par value.

Loans Receivable

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at their outstanding principal balances and adjusted for any charge-offs, the allowance for credit losses, any deferred fees or costs on originated loans, and unamortized premiums or discounts on purchased loans. Loan fees and certain direct loan origination costs are deferred, and the net fee or cost is recognized as an adjustment to interest income.

Because some loans may not be repaid in full, an allowance for credit losses is recorded. An allowance for credit losses is a valuation allowance for probable incurred credit losses. The allowance for credit losses is increased by a provision for credit losses charged to expense and decreased by charge-offs (net of recoveries). The allowance is based on ongoing, quarterly assessments of the probable and estimable losses inherent in the loan portfolio. The Bank's methodology for assessing the appropriateness of the allowance consists of several key elements, which include the formula allowance and specific allowances.

Commencement Bank
December 31, 2015 and 2014

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

Loans Receivable (continued)

Troubled debt restructurings are loans for which concessions in terms have been made as a result of the borrower experiencing financial difficulty. Generally, concessions granted to customers include lower interest rates and modification of the payment stream to lower or defer payments. Interest on troubled debt restructurings is accrued under the new terms if the loans are performing and full collection of principal and interest is expected. However, interest accruals are discontinued on troubled debt restructurings that meet the Bank's nonaccrual criteria.

Interest income on loans is accrued over the term of the loans based upon the principal outstanding. The accrual of interest on loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due. Past due status is based on contractual terms of loans. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent that cash payments are received until, in management's judgment, the borrower has the ability to make contractual interest and principal payments, in which case the loan is returned to accrual status.

Generally, loans are charged off in whole or in part on a loan-by-loan basis after they become significantly past due and based upon management's review of the collectability of all or a portion of the loan unless the loan is in the process of restructuring. Charge off amounts are determined based upon the carrying amount of loans and the amount estimated to be collectible as determined by analyses of expected future cash flows and liquidation of loan collateral.

Allowance for Credit Losses

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

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as doubtful, substandard or special mention. 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 is lower than the carrying value of that loan. Impaired loans are all specifically identified loans for which it is probable that the Bank will not collect all amounts due according to the contractual terms of the loan agreement. The general component covers non-classified 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.

Commencement Bank
December 31, 2015 and 2014

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

Allowance for Credit Losses (continued)

The formula portion of the general credit loss allowance is established by applying a loss percentage factor to the different loan types. The allowances are provided based on management's continuing evaluation of the pertinent factors underlying the quality of the loan portfolio, including changes in the size and composition of the loan portfolio, actual loan loss experience, current economic conditions, geographic concentrations, seasoning of the loan portfolio, specific industry conditions, and the duration of the current business cycle. The recovery of the carrying value of loans is susceptible to future market conditions beyond the Bank's control, which may result in losses or recoveries differing from those provided. Specific allowances are established for loans evaluated for impairment in accordance with guidance which requires an allowance to be established as a component of the allowance for credit losses when it is probable all amounts due will not be collected pursuant to the contractual terms of the loan and the recorded investment in the loan exceeds its fair value. Fair value is measured using either the present value of expected future cash flows discounted at the loan's effective interest rate, the observable market price of the loan, or the fair value of the collateral, if the loan is collateral dependent. All loans subject to evaluation and considered impaired are included in nonperforming assets. Smaller balances are excluded from this analysis.

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 that 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 on a loan by loan basis for loans 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.

Large groups of smaller balance homogenous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer and residential loans for impairment disclosures.

The general component relates to non-impaired loans, and is based on historical loss experience adjusted for the effects of qualitative factors that are likely to cause estimated credit losses as of the evaluation date to differ from the portfolio's historical loss experience. Qualitative factors include the following: Economic conditions; industry conditions; changes in lending policies and procedures; trends in the volume and terms of loans; the experience, ability and depth of lending staff; levels and trends in delinquencies; levels and trends in charge-off and recovery activity; levels and trends of loan quality as determined by an internal loan grading system; portfolio concentrations.

On a quarterly basis, management estimates the allowance balance required using the criteria identified above in relation to the relevant risks for each of the Bank's major loan segments. For construction, land and land development loans, major risk factors include demand levels for residential and commercial development, and real estate prices. For mortgage loans secured by residential real estate, major risk factors include unemployment levels and real estate prices. For mortgage loans secured by commercial real estate, major risk factors include demand levels for products and services, rental rates and real estate prices. For commercial and industrial loans, major risk factors include demand for products and services, and operating cash flows. For consumer and other loans, the major risk factor is unemployment levels.

Commencement Bank
December 31, 2015 and 2014

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

Allowance for Credit Losses (continued)

The quality of the Bank's loan portfolio is assessed as a function of the levels of past due loans and impaired loans, and internal credit quality ratings which are updated quarterly by management. The ratings on the Bank's internal credit scale are broadly grouped into the categories "non-classified" and "classified." Non-classified loans are those loans with minimal identified credit risk, as well as loans with potential credit weaknesses which deserve management's attention but for which full collection of contractual principal and interest is not significantly at risk. Classified loans are those loans that have well-defined weakness that put full collection of contractual principal and interest at risk, and classified loans for which it is probable that the Bank will not collect all contractual principal or interest are also considered impaired. The credit quality ratings are an important part of the Bank's overall credit risk management process and are considered in the determination of the allowance for credit losses.

Determination of the allowance is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance. Such agencies may require the Bank to recognize additional losses based on their judgments about information available to them at the time of their examination.

Premises and Equipment

Premises and equipment are stated at cost, less accumulated depreciation, which is computed on the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized over the term of the lease or the estimated useful life of the improvement, whichever is less. Asset lives range from three to ten years. Gains or losses on dispositions are reflected in earnings.

The 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.

Bank Owned Life Insurance

The Bank has purchased single premium life insurance policies for certain officers. The value of the policies is recorded at the amount that would be received if the policies were surrendered. Increases or decreases in the cash value of the policies are recognized as income or expense in the period of change. The Bank entered into a Split Dollar Life insurance agreement with certain officers and key employees on these policies.

Deferred Rent and Lease Incentives

Rental payments under operating leases for the Bank are charged to expense on the straight-line basis, after consideration of rent holidays, step-rent provisions and escalation clauses.

Commencement Bank
December 31, 2015 and 2014

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

Income Taxes

Deferred tax assets and liabilities result from differences between the financial statement carrying amounts and the tax bases of assets and liabilities, and 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. The deferred tax provision represents the difference between the net deferred tax asset and liability at the beginning and end of the year. Deferred tax assets are reduced by a valuation allowance, when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with the presumption that a tax examination will occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely to be realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded.

The Bank is no longer subject to examination by taxing authorities for years before 2012.

New Accounting Pronouncements

The Financial Accounting Standards Board recently issued Accounting Standards Update 2016-01, Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. Under the new standard, certain equity investments are required to be carried at fair value, with changes in fair value recognized in net income. This applies to equity investments with readily determinable fair values that are not consolidated or carried on the equity method. Debt securities classified as available-for-sale will continue to be carried at fair value with changes in fair value recorded through other comprehensive income. The standard also reduces or eliminates several financial reporting disclosure requirements. The standard is effective for the Bank beginning January 1, 2019; however, for 2015 the Bank has early adopted a provision that eliminates the disclosures of the fair values of financial instruments carried at amortized cost. Other provisions of the standard are not expected to have a significant impact to the consolidated financial statements.

On February 25, 2016, the Financial Accounting Standards Board (FASB) issued new lease accounting guidance in Accounting Standards Update No. 2016-02, Leases (Topic 842). Under the new guidance, lessees will be required to recognize certain assets and liabilities for all leases (with the exception of short-term leases) at the commencement date. Nonpublic business entities should apply the amendments for fiscal years beginning January 1, 2020, for a calendar year entity. Early application is permitted for all nonpublic business entities upon issuance. Management has not yet determined the impact to the Bank's financial statements, if any.

Cash Equivalents and Cash Flows

The Bank considers all amounts included in the balance sheet caption "Cash and due from banks" and interest-bearing deposits in other financial institutions to be cash equivalents. Cash flows from loans, deposits and short-term borrowings are reported net. At times, cash balances on deposit in other financial institutions exceed FDIC insurance limits; however, the Bank has not experienced any losses due to these concentrations.

Commencement Bank
December 31, 2015 and 2014

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

Advertising

The Bank expenses advertising costs as incurred.

Stock-Based Compensation

The Bank has a stock-based compensation option plan and stock warrants, which are described more fully in Note 11. The Bank accounts for the stock option plan under the recognition and measurement principles as defined by guidance, which requires the cash flows related to the tax benefits resulting from tax deductions in excess of compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows.

Comprehensive Income

Components of comprehensive income are net income and all other non-owner changes in equity. Other comprehensive income consists of unrealized holding gains and losses on available for sale securities.

Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants, excluding transaction costs. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

When measuring fair value, entities should maximize the use of observable inputs and minimize the use of unobservable inputs. The following describes the three levels of inputs that may be used to measure fair value:

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

- *Level 2 Inputs*— Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

- *Level 3 Inputs* - Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer, or broker traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities.

Commencement Bank
December 31, 2015 and 2014

Note 2 - Securities

Debt securities have been classified according to management's intent. The amortized cost of the Bank's securities and their approximate fair value are as follows:

Securities available for sale	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2015				
Mortgage-backed securities	$3,364	$44	$(21)	$3,387
Total	$3,364	$44	($21)	$3,387
December 31, 2014				
Mortgage-backed securities	$1,900	$43	$- -	$1,943
US Treasury	997	- -	(11)	986
Total	$2,897	$43	($11)	$2,929

The Bank only held mortgage-backed securities at December 31, 2015. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations, with or without call or prepayment penalties.

The following tables present the gross unrealized losses and fair value of securities available for sale aggregated by the length of time the individual securities have been in a continuous unrealized loss position at December 31, 2015 and 2014:

	Less than 12 months		12 months or more	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2015				
Mortgage-backed securities	$ 1,831	$ (21)	$ - -	$ - -
December 31, 2014				
US Treasury	$ - -	$ - -	$ 986	$ (11)

The investment securities shown in the previous tables have fair values less than amortized cost and therefore contain unrealized losses. Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. There are one and two investment securities with unrealized losses at December 31, 2015 and 2014, respectively. The Bank anticipates full recovery of amortized cost with respect to these securities at maturity or earlier in the event of a more favorable market interest rate environment.

There was $1 in gross gains realized on sales of securities in 2015 and $8 in gross gains realized on sales of securities in 2014. There were no gross losses realized on sales of securities in 2015 or 2014.

The fair value of pledged securities totaled $3,387 and $1,943 at December 31, 2015 and 2014, respectively.

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Note 3 – Loans and Allowance for Credit Losses

Loans at December 31 consist of the following:

	2015	2014
Commercial	$39,412	$41,305
Real estate:		
Residential 1-4 family	11,742	10,497
Multi-Family	12,498	11,915
Commercial	75,719	64,783
Construction and land	4,187	3,651
Consumer	1,862	1,521
	145,420	133,672
Less net deferred loan origination fees	334	262
Loans, net of deferred fees	$145,086	$133,410

Transactions in the allowance for credit losses for the year ended December 31, 2015 are as follows:

	Year ended December 31, 2015			
	Real Estate	Commercial	Consumer	Total
Balance at beginning of period	$ 1,267	$ 566	$ 18	$ 1,851
Provision for loan losses	150	(270)	(1)	(121)
Charge-offs	-	- -	- -	- -
Recoveries	- -	232	- -	232
Balance at end of period	$ 1,417	$ 528	$ 17	$ 1,962

Transactions in the allowance for credit losses for the year ended December 31, 2014 are as follows:

	Year ended December 31, 2014			
	Real Estate	Commercial	Consumer	Total
Balance at beginning of period	$ 1,179	$ 492	$ 61	$ 1,732
Provision for loan losses	(9)	162	(108)	45
Charge-offs	-	(150)	-	(150)
Recoveries	97	62	65	224
Balance at end of period	$ 1,267	$ 566	$ 18	$ 1,851

Note 3 – Loans and Allowance for Credit Losses (continued)

Components of the allowance for credit losses, and the related carrying amount of loans for which the allowance is determined, are as follows:

	December 31, 2015			
	Real Estate	Commercial	Consumer	Total
Allocation of Allowance to:				
Impaired loans – evaluated individually	$ -	$ -	$ -	$ -
Impaired loans – evaluated collectively	-	-	-	-
Total impaired loans	-	-	-	-
Unimpaired loans – evaluated collectively	1,417	528	17	1,962
	$ 1,417	$ 528	$ 17	$ 1,962

	December 31, 2015			
	Real Estate	Commercial	Consumer	Total
Recorded Investment In:				
Impaired loans – evaluated individually	$ -	$ -	$ -	$ -
Impaired loans – evaluated collectively	-	-	-	-
Total impaired loans	-	-	-	-
Unimpaired loans – evaluated collectively	104,146	39,412	1,862	145,420
	$ 104,146	$ 39,412	$ 1,862	$145,420

	December 31, 2014			
	Real Estate	Commercial	Consumer	Total
Allocation of Allowance to:				
Impaired loans – evaluated individually	$ -	$ -	$ -	$ -
Impaired loans – evaluated collectively	-	-	-	-
Total impaired loans	-	-	-	-
Unimpaired loans – evaluated collectively	1,267	566	18	1,851
	$ 1,267	$ 566	$ 18	$ 1,851

Note 3 – Loans and Allowance for Credit Losses (continued)

	December 31, 2014			
	Real Estate	Commercial	Consumer	Total
Recorded Investment In:				
Impaired loans – evaluated individually	$ -	$ -	$ -	$ -
Impaired loans – evaluated collectively	-	-	-	-
Total impaired loans	-	-	-	-
Unimpaired loans – evaluated collectively	90,846	41,305	1,521	133,672
	$ 90,846	$ 41,305	$ 1,521	$133,672

The carrying amounts of loans by performance status at December 31, 2015, are as follows:

	Accruing Loans				
	Current	30-89 Days Past Due	90 Days or More Past Due	Nonaccrual Loans	Total Loans
Real Estate	$ 104,146	$ -	$ -	$ -	$ 104,146
Commercial	39,412	-	-	-	39,412
Consumer	1,862	-	-	-	1,862
	$ 145,420	$ -	$ -	$ -	$ 145,420

The carrying amounts of loans by credit quality at December 31, 2015 are as follows:

		Classified	
	Non-Classified	Unimpaired	Impaired
Real Estate	$ 102,419	$ 1,727	$ -
Commercial	37,862	1,550	-
Consumer	1,862	-	-
	$ 142,143	$ 3,277	$ -

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Note 3 – Loans and Allowance for Credit Losses (continued)

The carrying amounts of loans by performance status at December 31, 2014 are as follows:

	Accruing Loans				
	Current	30-89 Days Past Due	90 Days or More Past Due	Nonaccrual Loans	Total Loans
Real Estate	$ 90,846	$ -	$ -	$ -	$ 90,846
Commercial	40,883	-	422	-	41,305
Consumer	1,521	-	-	-	1,521
	$ 133,250	$ -	$ 422	$ -	$ 133,672

The carrying amounts of loans by credit quality at December 31, 2014 are as follows:

		Classified	
	Non-Classified	Unimpaired	Impaired
Real Estate	$ 90,596	$ 250	$ -
Commercial	40,841	491	-
Consumer	1,521	-	-
	$ 132,931	$ 741	$ -

There were no impaired loans as of or during the year ended December 31, 2015. Information relative to impaired loans at December 31, 2014 is as follows:

	December 31, 2014						Year Ended December 31, 2014	
	Recorded Investment In Impaired Loans With No Valuation Allowance	Recorded Investment In Impaired Loans With A Valuation Allowance	Total Impaired Loans	Valuation Allowance on Impaired Loans	Contractual principal of impaired loans	Commitments to Extend Credit on Impaired Loans	Average Impaired Loans	Interest Income Recognized On Impaired Loans
Real Estate	$ -	$ -	$ -	$ -	$ -	$ -	$ 56	$ -
Commercial	-	-	-	-	-	-	58	-
Consumer	-	-	-	-	-	-	-	-
Reserve	-	-	-	-	-	-	-	-
Overdrafts	-	-	-	-	-	-	-	-
	$ -	$ -	$ -	$ -	$ -	$ -	$ 114	$ -

The Bank had no troubled debt restructurings outstanding as of December 31, 2015 and 2014.

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Note 3 – Loans and Allowance for Credit Losses (continued)

Certain related parties of the Bank, principally directors and their associates were loan customers of the Bank in the ordinary course of business during the year ended December 31, 2015 and 2014. Loans outstanding at December 31, 2015 and 2014, to key officers and directors totaled $4,311 and $3,489, respectively. During the years ended December 31, 2015 and 2014, loan advances totaled $10,234 and $5,930 and principal payments totaled $9,412 and $8,512, respectively.

Note 4 - Premises and Equipment

Components of premises and equipment at December 31 are as follows:

	2015	2014
Leasehold improvements	$ 688	$ 688
Furniture and equipment	684	639
	$1,372	1,327
Less accumulated depreciation and amortization	772	629
Premises and equipment, net	$ 600	$ 698

Note 5 - Deposits

The composition of deposits at December 31 is as follows:

	2015	2014
Demand deposits, non-interest-bearing	$ 28,301	$ 24,394
NOW and money market accounts	64,739	63,981
Savings deposits	1,435	1,202
Time certificates over $250,000	17,249	12,303
Other time certificates	40,905	40,757
Total deposits	$152,629	$142,637

Scheduled maturities of time certificates of deposit for future years ending December 31 are as follows:

2016	$44,694
2017	7,448
2018	5,810
2019	83
2020	119
Total	$58,154

Certain related parties of the Bank, principally directors and their affiliates were deposit customers of the Bank in the ordinary course of business during year ended December 31, 2015, and 2014. Deposits from these customers at December 31, 2015 and 2014 totaled $5,543 and $4,949, respectively.

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Note 6 – FHLB Borrowings

The Bank has long-term borrowings with the FHLB of Des Moines with total credit on the lines equal to 35% of the Bank's total assets or $66,792, which is available dependent upon sufficient collateral and FHLB stock ownership. The Bank has borrowings of $3,200 and $3,200 as of December 31, 2015 and 2014, respectively. As of December 31, 2015, the maturity date related to these borrowings was April 2018 and they bear an interest rate of 0.88%. The Bank also has letters of credit outstanding for $4,500 and $3,000, which are used to pledge for public deposits as of December 31, 2015 and 2014, respectively.

The Bank has a blanket pledge of $68,465 in loans as collateral for the FHLB borrowings at December 31, 2015. In addition the Bank has pledged $22,331 of loans as collateral for borrowings with the Federal Reserve Bank. Available borrowings through this facility are approximately $10,548.

The Bank has agreements with commercial banks for lines of credit totaling $9,500 at December 2015 and December 2014, none of which was used at both December 31, 2015 and 2014.

Note 7 - Employee Benefits

The Bank has a 401(k) profit sharing plan covering substantially all employees. Contributions to the 401(k) profit sharing plan consist of matching contributions, which match 100% of the employees' contributions up to 3% and then match 50% of the following 2%. The Bank may also make profit sharing contributions which are at the discretion of its board of directors. There were $78 in contributions by the Bank to this plan for the year ended December 31, 2015 and $69 in contributions for the year ended December 31, 2014.

The Bank has also established a non-qualified Supplemental Executive Retirement Plan ("SERP") to provide its President with supplemental retirement benefits. The periodic pension expense for the supplemental plan amounted to $162 for the year ended December 31, 2015. The present value of the projected benefit obligation and the vested benefit obligation was $325 at December 31, 2015, all of which is unfunded. A discount rate of 4.8% was used in determining the actuarial projected benefit at December 31, 2015.

Note 8 - Income Taxes

Allocation of income taxes between current and deferred portions is as follows:

	2015	2014
Income Taxes		
Current expense (benefit)	$547	$(15)
Deferred expense (benefit)	(36)	415
Total income taxes	$511	$400

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Note 8 - Income Taxes (continued)

Tax effects of temporary differences that give rise to significant portions of deferred tax assets and liabilities at December 31 are as follows:

	2015	2014
Deferred Tax Assets		
Allowance for credit losses	$ 270	$ 303
Accumulated depreciation	7	-
Charitable contributions	-	12
Organizational costs	101	118
Capital loss	21	21
Writedowns on other real estate owned	17	18
SERP expense	110	55
Total deferred tax assets	526	527
Deferred Tax Liabilities		
Cash basis accounting	-	33
Accumulated depreciation	-	17
Deferred income	107	94
Unrealized gain on available for sale securities	7	11
Total deferred tax liabilities	114	155
Net deferred tax assets before valuation allowance	412	372
Valuation Allowance	(21)	(21)
Net deferred tax assets	$ 391	$ 351

Note 9 - Commitments and Contingencies

The Bank is party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit. These instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized on the accompanying balance sheet.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments. A summary of the Bank's commitments at December 31 is as follows:

	2015	2014
Commitments to extend credit	$43,107	$41,292

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. Since 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 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 party. Collateral held varies, but may include accounts receivable, inventory, property and equipment, residential real estate and income-producing commercial properties.

Note 9 - Commitments and Contingencies (continued)

At December 31, 2015, the Bank had an allowance for credit losses on unfunded commitments of $65 carried as a component of other liabilities.

Because of the nature of its activities, the Bank is subject to various pending and threatened legal actions which may arise in the ordinary course of business. In the opinion of management, liabilities arising from these claims, if any, will not have a material effect on the financial position of the Bank. Management has not been informed of any such claims at December 31, 2015.

The Bank has entered into an employment contract with its President, Chief Financial Officer, Chief Credit Officer and Chief Operations Officer which provide for contingent payments subject to future events.

In November, 2011, the Bank executed a lease for a new facility that it occupies beginning in March, 2012. The term of the lease is for 10 years, beginning March 1, 2012, with two options to extend the lease term for five years each. Rental expense of leased premises was $292 and $269 for the years ended December 31, 2015 and 2014, respectively, which is included in occupancy expense.

Minimum net rental commitments under noncancellable leases having an original or remaining term of one year or more for future years ending December 31 are as follows:

2016	$303
2017	296
2018	294
2019	301
2020	308
Thereafter	422
Total net rental commitments required	$1,924

Note 10 - Significant Concentrations of Credit Risk

Most of the Bank's business activity is with customers located in the state of Washington. Loans are generally limited, by federal and state banking regulations, to 20 percent of the Bank's shareholders' equity, excluding accumulated other comprehensive income plus allowance for loan and lease losses.

Note 11 - Stock Compensation Plans

Stock Warrants

In 2006, the Bank granted organizing shareholders 148,500 warrants to purchase the Bank's common stock, at $10 per share. Warrants are vested upon grant, have a ten-year contractual life and expire in 2016. No warrants have been exercised to date. The estimated remaining life is 0.92 years.

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Note 11 - Stock Compensation Plans (continued)

Employee Stock Options

Under the Bank's employee stock option plan, the Bank may grant both incentive and nonqualified options for up to 450,000 shares of its common stock to certain key employees, 90,000 of which may be granted as restricted stock. The exercise price of each option equals the fair market value of the Bank's stock on the date of grant, and an option's maximum term is eight years. Options vest ratably over five years. The Bank has 398,500 options available, of which 76,500 may be granted as restricted stock.

The fair value of each option grant is estimated on the date of grant, based on the Black-Scholes option pricing model and using the following weighted-average assumptions at December 31:

	2015	2014
Dividend yield	0.00%	0.00%
Expected life	5.5 years	5.5 years
Risk-free interest rate	1.69%	1.67%
Expected volatility	40.53%	50.73%

At the time of the stock grant there were no plans to issue a cash dividend in the near term; therefore, management assumed no dividend yield. The Bank elected to apply the simplified method prescribed by guidance to calculate the expected life of the options. The Bank utilized a five-year, risk-free yield rate for the interest rate utilized. The Bank used historical data to determine expected volatility. The weighted-average fair value of options granted during 2015 and 2014 was $4.54 and $5.08, respectively.

The Black-Scholes model used by the Bank to calculate option values and other currently accepted option valuation models was developed to estimate the fair value of freely tradable, fully transferable options without vesting restrictions, which significantly differ from the Bank's stock option awards. These models require highly subjective assumptions, including future stock price volatility and expected time to exercise, which greatly affect the calculated values.

A summary of the status of the Bank's stock option plans and stock warrants as of December 31, 2015, along with activities during the year are presented below:

	Shares	Weighted Exercise Price	Weighted-Average Grant Date Fair Value	Aggregate Intrinsic Value	Weighted-Average Contractual Life (Years)
Outstanding at beginning of year	187,500	$9.99	$8.84	$--	2.38
Options granted	3,000	11.50	4.54		
Options forfeited	(9,500)	11.68	4.54		
Outstanding at end of year	181,000	$ 9.93	$8.94	$--	1.61
Vested or expected to vest at end of year	179,950	$ 9.93	$8.97	$--	1.58
Exercisable at end of year	165,700	$9.88	$9.33	$--	1.22

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Note 11 - Stock Compensation Plans (continued)

Employee Stock Options (continued)

A summary of the status of the Bank's stock option plans and stock warrants as of December 31, 2014, along with activities during the year are presented below:

	Shares	Weighted Exercise Price	Weighted-Average Grant Date Fair Value	Aggregate Intrinsic Value	Weighted-Average Contractual Life (Years)
Outstanding at beginning of year	360,250	$9.98	$6.37	$--	2.14
Options granted	4,000	10.83	5.08		
Options forfeited	(176,750)	9.99	3.78		
Outstanding at end of year	187,500	$ 9.99	$8.79	$--	2.41
Vested or expected to vest at end of year	185,686	$ 10.00	$8.84	$--	2.38
Exercisable at end of year	169,400	$10.01	$9.24	$--	2.02

No warrants were exercised during the years ended December 31, 2015 and 2014.

Employee Restricted Stock

During 2015, the Bank adopted a Restricted Stock Plan to provide for the issuance of shares and restricted stock units to employees. Compensation expense is recognized over the vesting period of the awards based on the fair value of the stock at issue date. The fair value of the stock was determined by using the 3rd party valuation reflected on the over-the-counter market "OTCQX", where the Bank is listed. The shares vest in 2016 through 2020. Total shares issuable under the plan were 90,000 at December 31, 2015.

The following is a schedule of the Bank's nonvested shares at December 31, 2015:

	Shares	Weighted Average Grant-Date Price
Nonvested at beginning of year	0	$0
Granted	13,500	$11.50
Vested	0	$0
Forfeited	0	$0
Nonvested at end of year	13,500	$11.50

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Note 11 - Stock Compensation Plans (continued)

Employee Restricted Stock (continued)

As of December 31, 2015, there was $142,000 of total unrecognized compensation cost related to nonvested shared granted under the plan.

The Bank did not have any excess tax benefits resulting from disqualifying dispositions of shares acquired upon exercise of incentive stock options for the years ended December 31, 2015 and 2014. For the years ended December 31, 2015 and 2014, the Bank recognized stock-based compensation expense of $25 and $18, respectively.

At December 31, 2015, stock-based compensation expense related to unvested stock options granted aggregated approximately $56 and is expected to be recognized as follows:

2016	$21
2017	17
2018	12
2019	5
2020	1
Total	$56

Note 12 - Regulatory Matters

Banks and bank holding companies are subject to various regulatory capital requirements administered by state and 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 about components, risk weighting and other factors.

The Basel III Capital Rules became effective for the Bank on January 1, 2015, subject to a phase-in for certain provisions. Quantitative measures established by the Basel III Capital Rules to ensure capital adequacy require the maintenance of minimum amounts and ratios (set forth in the table below) of common equity tier 1 capital, tier 1 capital and total capital (as defined in the regulations) to risk-weighted assets (as defined), and of tier 1 capital to quarterly average assets (as defined).

At December 31, 2015, the Bank's regulatory capital is comprised of the following: 1) Common equity tier 1 capital – consisting of common stock and related paid-in-capital, and retained earnings; 2) Additional tier 1 capital – there are no components of tier 1 capital beyond common equity tier 1capital; 3) Tier 2 capital - consisting of a permissible portion of the allowance for loan losses; and 4) total capital - the aggregate of all tier 1 and tier 2 capital. In connection with the adoption of the Basel III Capital Rules, the Bank elected to opt-out of the requirement to include most components of accumulated other comprehensive income in common equity tier 1 capital. At December 31, 2014, the Bank's regulatory capital is comprised of the same components as at December 31, 2015, except that the regulations in effect at that time did not distinguish between common equity tier 1 and additional tier 1 capital.

When fully phased in on January 1, 2019, the Basel III capital rules will require the Bank to maintain a minimum ratio of common equity tier 1 capital to risk-weighted assets of at least 4.5%, plus a 2.5% "capital conservation buffer" (which is added to the 4.5% common equity tier 1 capital ratio as the buffer is phased in, effectively resulting in a minimum ratio of common equity tier 1 capital to risk-weighted assets of 7% upon full phase in). The Bank will also be required to maintain a tier 1 capital to risk-weighted assets ratio of 6.0% (8.5% including the capital conservation buffer), a total capital to risk-

Commencement Bank
December 31, 2015 and 2014

Note 12 - Regulatory Matters (continued)

weighted assets ratio of 8.0% (10.5% including the capital conservation buffer), and a tier 1 capital to quarterly average assets ratio of 4.0%.

The aforementioned capital conservation buffer phases in at 0.625% annually over a four year period beginning January 1, 2016, and is designed to absorb losses during periods of economic stress. Banking institutions with capital ratios above the base minimums but below the effective minimums (which include the buffer) will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall.

The following table presents actual and required capital ratios as of December 31, 2015 for the Bank under the Basel III Capital Rules. The minimum required capital amounts presented include the minimum required capital levels as of December 31, 2015 based on the phase-in provisions of the Basel III Capital Rules and the minimum required capital levels as of January 1, 2019 when the Basel III Capital rules have been fully phased-in, and include the capital conservation buffer. Capital levels required to be considered well capitalized are based on prompt corrective action regulations, as amended to reflect changes under the Basel III Capital rules.

	Actual		Minimum required for capital adequacy purposes - Basel III phase-in schedule		Required to be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2015						
Tier 1 capital (to average assets)	$22,118	11.70%	$7,560	4.00%	$9,450	5.00%
Tier 1 capital (to risk-weighted assets)	22,118	14.54	9,127	6.00	12,170	8.00
Common Equity Tier 1 capital (to risk-weighted assets)	22,118	14.54	6,846	4.50	9,888	6.50
Total capital (to risk-weighted assets)	24,024	15.79	12,170	8.00	15,212	10.00

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December 31, 2015 and 2014

Note 12 - Regulatory Matters (continued)

The following table presents the Bank's actual and required capital ratios as of December 31, 2014 under the regulatory capital rules then in effect.

	Actual		Capital Adequacy Purposes		To be Well-Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2014						
Tier 1 capital (to average assets)	$21,500	12.63%	$6,807	4.00%	$8,508	5.00%
Tier 1 capital (to risk-weighted assets)	21,500	16.28	5,282	4.00	7,923	6.00
Total capital (to risk-weighted assets)	23,154	17.54	10,564	8.00	13,204	10.00

Note 13 – Fair Value of Financial Instruments

The following is a description of the Bank's valuation methodologies for financial assets and liabilities recorded at fair value:

Securities Available for Sale – The fair values of securities available for sale are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1) or matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2).

Collateral-Dependent Impaired Loans – The Bank does not record loans at fair value on a recurring basis. However, from time to time, fair value adjustments are recorded on these loans to reflect (1) partial write-downs that are based on the current appraised or market-quoted value of the underlying collateral or (2) the full charge-off of the loan carrying value. In some cases, the properties for which market quotes or appraised values have been obtained are located in areas where comparable sales data is limited, outdated, or unavailable. Fair value estimates for collateral-dependent impaired loans are obtained from real estate brokers or other third-party consultants (Level 3).

Other Real Estate Owned – The Bank does not record other real estate owned at fair value on a recurring basis. However, from time to time, fair value adjustments are recorded on these properties to reflect the current appraised value (less an estimate of cost to sell). In some cases, the properties for which appraised values have been obtained are located in areas where comparable sales data is limited, outdated, or unavailable. Fair value estimates for real estate held for sale are obtained from independent appraisers (Level 3).

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December 31, 2015 and 2014

Note 13 – Fair Value of Financial Instruments (continued)

The following table provides the hierarchy and fair value for each major category of assets and liabilities measured at fair value:

	December 31, 2015			
	Fair Value Measurements Using			
	Level 1	Level 2	Level 3	Total
Assets and liabilities measured at fair value on a recurring basis				
Assets:				
Securities available for sale	$ -	$3,387	$ -	$3,387
Assets measured at fair value on a non-recurring basis				
Other real estate owned	-	-	338	338

	December 31, 2014			
	Fair Value Measurements Using			
	Level 1	Level 2	Level 3	Total
Assets and liabilities measured at fair value on a recurring basis				
Assets:				
Securities available for sale	$ -	$2,929	$ -	$2,929
Assets measured at fair value on a non-recurring basis				
Other real estate owned	-	-	642	642

At December 31, 2015, other real estate owned with a book value of $338 is carried at its fair value of $338. At December 31, 2014, other real estate owned with a book value of $695 is carried at its fair value of $642.

During 2015 and 2014, there were no changes or amounts in Level 3 assets or liabilities measured at fair value on a recurring basis.