COMMUNITY WEST BANCSHARES /
Form 10-Q
May 03, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2017 or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _________ to _________

Commission File Number: 000-23575

COMMUNITY WEST BANCSHARES
(Exact name of registrant as specified in its charter)

California	77-0446957
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
445 Pine Avenue, Goleta, California	93117
(Address of principal executive offices)	(Zip Code)

(805) 692-5821
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Y ES NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company)	Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common stock of the registrant issued and outstanding of 8,103,139 as of April 28, 2017.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

COMMUNITY WEST BANCSHARES
CONSOLIDATED BALANCE SHEETS

	March 31, 2017 (unaudited)	December 31, 2016
	(in thousands, except share amounts)	
Assets:		
Cash and due from banks	$ 1,796	$ 2,385
Federal funds sold	15	16
Interest-earning demand in other financial institutions	28,366	31,715
Cash and cash equivalents	30,177	34,116
Investment securities - available-for-sale, at fair value; amortized cost of $26,776 at March 31, 2017 and $22,731 at December 31, 2016	26,776	22,681
Investment securities - held-to-maturity, at amortized cost; fair value of $8,778 at March 31, 2017 and $9,149 at December 31, 2016	8,613	9,002
Federal Home Loan Bank stock, at cost	2,070	2,070
Federal Reserve Bank stock, at cost	1,373	1,373
Loans:		
Held for sale, at lower of cost or fair value	59,811	61,416
Held for investment, net of allowance for loan losses of $7,785 at March 31, 2017 and $7,464 at December 31, 2016	600,950	561,939
Total loans	660,761	623,355
Other assets acquired through foreclosure, net	145	137
Premises and equipment, net	4,591	3,931
Other assets	13,794	13,907
Total assets	$ 748,300	$ 710,572
Liabilities:		
Deposits:		
Non-interest-bearing demand	$ 102,553	$ 100,372
Interest-bearing demand	262,008	253,023
Savings	14,072	14,007
Certificates of deposit ($250,000 or more)	80,293	77,509
Other certificates of deposit	181,204	167,325
Total deposits	640,130	612,236
Other borrowings	37,000	29,000
Other liabilities	4,603	4,000
Total liabilities	681,733	645,236
Stockholders’ equity:		
Common stock — no par value, 20,000,000 shares authorized; 8,103,139 shares issued and outstanding at March 31, 2017 and 8,096,039 at December 31, 2016	41,704	41,575
Retained earnings	24,863	23,790
Accumulated other comprehensive income (loss)	—	(29)
Total stockholders’ equity	66,567	65,336
Total liabilities and stockholders’ equity	$ 748,300	$ 710,572

See the accompanying notes.

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COMMUNITY WEST BANCSHARES
CONSOLIDATED INCOME STATEMENTS (unaudited)

	Three Months Ended March 31,	
	2017	2016
Interest income:	(in thousands, except per share amounts)	
Loans, including fees	$ 8,442	$ 7,175
Investment securities and other	261	269
Total interest income	8,703	7,444
Interest expense:		
Deposits	858	651
Other borrowings	71	72
Total interest expense	929	723
Net interest income	7,774	6,721
Provision (credit) for loan losses	144	(247)
Net interest income after provision for loan losses	7,630	6,968
Non-interest income:		
Other loan fees	303	275
Document processing fees	133	115
Service charges	96	90
Other	109	99
Total non-interest income	641	579
Non-interest expenses:		
Salaries and employee benefits	3,931	3,452
Occupancy, net	645	486
Professional services	179	179
Data processing	168	171
Depreciation	163	149
Advertising and marketing	156	81
FDIC assessment	110	97
Loan servicing and collection	106	179
Stock based compensation	84	80
Other	381	462
Total non-interest expenses	5,923	5,336
Income before provision for income taxes	2,348	2,211
Provision for income taxes	992	928
Net income	$ 1,356	$ 1,283
Earnings per share:		
Basic	$ 0.17	$ 0.16
Diluted	$ 0.16	$ 0.15
Weighted average number of common shares outstanding:		
Basic	8,100	8,169
Diluted	8,532	8,467
Dividends declared per common share	$ 0.035	$ 0.03

See the accompanying notes.

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COMMUNITY WEST BANCSHARES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (unaudited)

	Three Months Ended March 31,	
	2017	2016
	(in thousands)	
Net income	$ 1,356	$ 1,283
Other comprehensive income, net:		
Unrealized income on securities available-for-sale (AFS), net (tax effect of ($0) and ($83) for each respective period presented)	29	117
Net other comprehensive income	29	117
Comprehensive income	$ 1,385	$ 1,400

See the accompanying notes.

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COMMUNITY WEST BANCSHARES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (unaudited)

	Common Stock		Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Stockholders' Equity
	Shares	Amount			
	(in thousands)				
Balance, December 31, 2016:	8,096	$41,575	$ (29)	$23,790	$ 65,336
Net income	—	—	—	1,356	1,356
Exercise of stock options	7	45	—	—	45
Stock based compensation	—	84	—	—	84
Dividends on common stock	—	—	—	(283)	(283)
Other comprehensive income, net	—	—	29	—	29
Balance, March 31, 2017	8,103	$41,704	$ -	$24,863	$ 66,567

See the accompanying notes.

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COMMUNITY WEST BANCSHARES

CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

	Three Months Ended March 31,	
	2017	2016
	(in thousands)	
Cash flows from operating activities:		
Net income	$ 1,356	$ 1,283
Adjustments to reconcile net income to cash provided by operating activities:		
Provision (credit) for loan losses	144	(247)
Depreciation	163	149
Stock based compensation	84	80
Deferred income taxes	17	190
Net accretion of discounts and premiums for investment securities	5	(8)
(Gains)/Losses on:		
Sale of repossessed assets, net	(3)	(2)
Loans originated for sale and principal collections, net	1,605	2,591
Changes in:		
Other assets	76	309
Other liabilities	604	(724)
Servicing assets, net	6	10
Net cash provided by operating activities	4,057	3,631
Cash flows from investing activities:		
Principal pay downs and maturities of available-for-sale securities	617	405
Purchase of available-for-sale securities	(4,660)	(5,472)
Proceeds from principal pay downs and maturities of securities held-to-maturity	382	108
Loan originations and principal collections, net	(39,274)	(6,074)
Net decrease in interest-bearing deposits in other financial institutions	—	(1)
Purchase of premises and equipment, net	(823)	(69)
Proceeds from sale of other real estate owned and repossessed assets, net	107	138
Net cash used in investing activities	(43,651)	(10,965)
Cash flows from financing activities:		
Net increase in deposits	27,894	1,737
Net increase in borrowings	10,000	—
Repayments on borrowings	(2,000)	—
Exercise of stock options	44	15
Cash dividends paid on common stock	(283)	(246)
Common stock repurchase	—	(754)
Net cash provided by financing activities	35,655	752
Net decrease in cash and cash equivalents	(3,939)	(6,582)
Cash and cash equivalents at beginning of year	34,116	35,519
Cash and cash equivalents at end of period	$ 30,177	$ 28,937
Supplemental disclosure:		
Cash paid during the period for:		
Interest	$ 890	$ 657
Income taxes	—	1,300
Non-cash investing and financing activity:		
Transfers to other assets acquired through foreclosure, net	112	114

See the accompanying notes.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Community West Bancshares ("CWBC"), incorporated under the laws of the state of California, is a bank holding company providing full service banking through its wholly-owned subsidiary Community West Bank, N.A. ("CWB" or the "Bank"). Unless indicated otherwise or unless the context suggest otherwise, these entities are referred to herein collectively and on a consolidated basis as the "Company."

Basis of Presentation

The accounting and reporting policies of the Company are in accordance with accounting principles generally accepted in the United States ("GAAP") and conform to practices within the financial services industry. The accounts of the Company and its consolidated subsidiary are included in these Consolidated Financial Statements. All significant intercompany balances and transactions have been eliminated.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant changes in the near term relate to the determination of the allowance for loan losses and the fair value of securities available for sale. Although Management believes these estimates to be reasonably accurate, actual amounts may differ. In the opinion of Management, all necessary adjustments have been reflected in the financial statements during their preparation.

Interim Financial Information

The accompanying unaudited consolidated financial statements as of and for the three months ended March 31, 2017 and 2016 have been prepared in a condensed format, and therefore do not include all of the information and footnotes required by GAAP for complete financial statements. These statements have been prepared on a basis that is substantially consistent with the accounting principles applied to our audited consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2016.

The information furnished in these interim statements reflects all adjustments which are, in the opinion of management, necessary for a fair statement of the results for each respective period presented. Such adjustments are of a normal recurring nature. The results of operations in the interim statements are not necessarily indicative of the results that may be expected for any other quarter or for the full year. The interim financial information should be read in conjunction with the Company's audited consolidated financial statements.

Reclassifications

Certain amounts in the consolidated financial statements as of December 31, 2016 and for the three months ended March 31, 2016 have been reclassified to conform to the current presentation. The reclassifications have no effect on net income, comprehensive income or stockholders' equity as previously reported.

Loans Held For Sale

Loans which are originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value determined on an aggregate basis. Valuation adjustments, if any, are recognized through a valuation allowance by charges to lower of cost or fair value provision. Loans held for sale are mostly comprised of SBA and commercial agriculture. The Company did not incur any lower of cost or fair value provision in the three months ended March 31, 2017 and 2016.

Loans Held for Investment and Interest and Fees from Loans

Loans are recognized at the principal amount outstanding, net of unearned income, loan participations and amounts charged off. Unearned income includes deferred loan origination fees reduced by loan origination costs. Unearned income on loans is amortized to interest income over the life of the related loan using the level yield method.

Interest income on loans is accrued daily using the effective interest method and recognized over the terms of the loans. Loan fees collected for the origination of loans less direct loan origination costs (net deferred loan fees) are amortized over the contractual life of the loan through interest income. If the loan has scheduled payments, the amortization of the net deferred loan fee is calculated using the interest method over the contractual life of the loan. If the loan does not have scheduled payments, such as a line of credit, the net deferred loan fee is recognized as interest income on a straight-line basis over the contractual life of the loan commitment. Commitment fees based on a percentage of a customer’s unused line of credit and fees related to standby letters of credit are recognized over the commitment period.

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When loans are repaid, any remaining unamortized balances of unearned fees, deferred fees and costs and premiums and discounts paid on purchased loans are accounted for through interest income.

Nonaccrual loans: For all loan types, when a borrower discontinues making payments as contractually required by the note, the Company must determine whether it is appropriate to continue to accrue interest. Generally, the Company places loans in a nonaccrual status and ceases recognizing interest income when the loan has become delinquent by more than 90 days or when Management determines that the full repayment of principal and collection of interest is unlikely. The Company may decide to continue to accrue interest on certain loans more than 90 days delinquent if they are well secured by collateral and in the process of collection. Other personal loans are typically charged off no later than 120 days delinquent.

For all loan types, when a loan is placed on nonaccrual status, all interest accrued but uncollected is reversed against interest income in the period in which the status is changed. Subsequent payments received from the customer are applied to principal and no further interest income is recognized until the principal has been paid in full or until circumstances have changed such that payments are again consistently received as contractually required. The Company occasionally recognizes income on a cash basis for non-accrual loans in which the collection of the remaining principal balance is not in doubt.

Impaired loans: A loan is considered impaired when, based on current information; it is probable that the Company will be unable to collect the scheduled payments of principal and/or interest under 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/or interest payments. Loans that experience insignificant payment delays or payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays or payment shortfalls on a case-by-case basis. When determining the possibility of impairment, management considers 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. For collateral-dependent loans, the Company uses the fair value of collateral method to measure impairment. The collateral-dependent loans that recognize impairment are charged down to the fair value less costs to sell. All other loans are measured for impairment either based on the present value of future cash flows or the loan’s observable market price.

Troubled debt restructured loan (“TDR”): A TDR is a loan on which the Company, for reasons related to the borrower’s financial difficulties, grants a concession to the borrower that the Company would not otherwise consider. These concessions included but are not limited to term extensions, rate reductions and principal reductions. Forgiveness of principal is rarely granted and modifications for all classes of loans are predominately term extensions. A TDR loan is also considered impaired. Generally, a loan that is modified at an effective market rate of interest may no longer be disclosed as a troubled debt restructuring in years subsequent to the restructuring if it is not impaired based on the terms specified by the restructuring agreement.

Allowance for Loan Losses and Provision for Loan Losses

The Company maintains a detailed, systematic analysis and procedural discipline to determine the amount of the allowance for loan losses (“ALL”). The ALL is based on estimates and is intended to be appropriate to provide for probable losses inherent in the loan portfolio. This process involves deriving probable loss estimates that are based on migration analysis and historical loss rates, in addition to qualitative factors that are based on management’s judgment. The migration analysis and historical loss rate calculations are based on the annualized loss rates utilizing a twelve-quarter loss history. Migration analysis is utilized for the Commercial Real Estate (“CRE”), Commercial, Commercial Agriculture, Small Business Administration (“SBA”), Home Equity Line of Credit (“HELOC”), Single Family Residential, and Consumer portfolios. The historical loss rate method is utilized primarily for the Manufactured Housing portfolio. The migration analysis takes into account the risk rating of loans that are charged

off in each loan category. Loans that are considered Doubtful are typically charged off. The following is a description of the characteristics of loan ratings. Loan ratings are reviewed as part of our normal loan monitoring process, but, at a minimum, updated on an annual basis.

Outstanding – This is the highest quality rating that is assigned to any loan in the portfolio. These loans are made to the highest quality borrowers with strong financial statements and unquestionable repayment sources. Collateral securing these types of credits are generally cash deposits in the bank or marketable securities held in custody.

Good – Loans rated in this category are strong loans, underwritten well, that bear little risk of loss to the Company. Loans in this category are loans to quality borrowers with very good financial statements that present an identifiable strong primary source and good secondary source of repayment. Generally, these credits are well collateralized by good quality and liquid assets or low loan to value market real estate.

Pass - Loans rated in this category are acceptable loans, appropriately underwritten, bearing an ordinary risk of loss to the Company. Loans in this category are loans to quality borrowers with financial statements presenting a good primary source as well as an adequate secondary source of repayment. In the case of individuals, borrowers with this rating are quality borrowers demonstrating a reasonable level of secure income, a net worth adequate to support the loan and presenting a good primary source as well as an adequate secondary source of repayment.

Watch – Acceptable credit that requires a temporary increase in attention by management. This can be caused by declines in sales, margins, liquidity or working capital. Generally the primary weakness is lack of current financial statements and industry issues.

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

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Substandard - A Substandard loan is inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. These loans have a well-defined weakness or weaknesses that jeopardize full collection of amounts due. They are characterized by the distinct possibility that the Company will sustain some loss if the borrower's deficiencies are not corrected.

Doubtful - A loan classified Doubtful has all the weaknesses inherent in one classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors, which may work to the advantage and strengthening of the loan, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition or liquidation procedures, capital injection, perfecting liens on additional collateral and refinancing plans.

Loss - Loans classified Loss are considered uncollectible and of such little value that their continuance as bankable loans is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this loan even though partial recovery may be realized in the future. Losses are taken in the period in which they are considered uncollectible.

The Company's ALL is maintained at a level believed appropriate by management to absorb known and inherent probable losses on existing loans. The allowance is charged for losses when management believes that full recovery on the loan is unlikely. The following is the Company's policy regarding charging off loans.

Commercial, CRE and SBA Loans

Charge-offs on these loan categories are taken as soon as all or a portion of any loan balance is deemed to be uncollectible. A loan is considered impaired when, based on current information, it is probable that the Company will be unable to collect the scheduled payments of principal and/or interest under 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/or interest payments. Loans that experience insignificant payment delays or payment shortfalls generally are not classified as impaired. Generally, loan balances are charged-down to the fair value of the collateral, if, based on a current assessment of the value, an apparent deficiency exists. In the event there is no perceived equity, the loan is charged-off in full. Unsecured loans which are delinquent over 90 days are also charged-off in full.

Single Family Real Estate, HELOC's and Manufactured Housing Loans

Consumer loans and residential mortgages secured by one-to-four family residential properties, HELOC and manufactured housing loans in which principal or interest is due and unpaid for 90 days, are evaluated for impairment. Loan balances are charged-off to the fair value of the property, less estimated selling costs, if, based on a current appraisal, an apparent deficiency exists. In the event there is no perceived equity, the loan is generally fully charged-off.

Consumer Loans

All consumer loans (excluding real estate mortgages, HELOCs and savings secured loans) are charged-off or charged-down to net recoverable value before becoming 120 days or five payments delinquent.

The ALL calculation for the different loan portfolios is as follows:

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- Commercial Real Estate, Commercial, Commercial Agriculture, SBA, HELOC, Single Family Residential, and Consumer – Migration analysis combined with risk rating is used to determine the required ALL for all non-impaired loans. In addition, the migration results are adjusted based upon qualitative factors that affect the specific portfolio category. Reserves on impaired loans are determined based upon the individual characteristics of the loan.

- Manufactured Housing – The ALL is calculated on the basis of loss history and risk rating, which is primarily a function of delinquency. In addition, the loss results are adjusted based upon qualitative factors that affect this specific portfolio.

The Company evaluates and individually assesses for impairment loans classified as substandard or doubtful in addition to loans either on nonaccrual, considered a TDR or when other conditions exist which lead management to review for possible impairment. Measurement of impairment on impaired loans is determined on a loan-by-loan basis and in total establishes a specific reserve for impaired loans. The amount of impairment is determined by comparing the recorded investment in each loan with its value measured by one of three methods:

- The expected future cash flows are estimated and then discounted at the effective interest rate.

- The value of the underlying collateral net of selling costs. Selling costs are estimated based on industry standards, the Company's actual experience or actual costs incurred as appropriate. When evaluating real estate collateral, the Company typically uses appraisals or valuations, no more than twelve months old at time of evaluation. When evaluating non-real estate collateral securing the loan, the Company will use audited financial statements or appraisals no more than twelve months old at time of evaluation. Additionally, for both real estate and non-real estate collateral, the Company may use other sources to determine value as deemed appropriate.

- The loan's observable market price.

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Interest income is not recognized on impaired loans except for limited circumstances in which a loan, although impaired, continues to perform in accordance with the loan contract and the borrower provides financial information to support maintaining the loan on accrual.

The Company determines the appropriate ALL on a monthly basis. Any differences between estimated and actual observed losses from the prior month are reflected in the current period in determining the appropriate ALL determination and adjusted as deemed necessary. The review of the appropriateness of the allowance takes into consideration such factors as concentrations of credit, changes in the growth, size and composition of the loan portfolio, overall and individual portfolio quality, review of specific problem loans, collateral, guarantees and economic and environmental conditions that may affect the borrowers' ability to pay and/or the value of the underlying collateral. Additional factors considered include: geographic location of borrowers, changes in the Company's product-specific credit policy and lending staff experience. These estimates depend on the outcome of future events and, therefore, contain inherent uncertainties.

Another component of the ALL considers qualitative factors related to non-impaired loans. The qualitative portion of the allowance on each of the loan pools is based on changes in any of the following factors:

- Concentrations of credit
- International risk
- Trends in volume, maturity, and composition of loans
- Volume and trend in delinquency, nonaccrual, and classified assets
- Economic conditions
- Geographic distance
- Policy and procedures or underwriting standards
- Staff experience and ability
- Value of underlying collateral
- Competition, legal, or regulatory environment
- Results of outside exams and quality of loan review and Board oversight

Off Balance Sheet and Credit Exposure

In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the consolidated financial statements when they are funded. They involve, to varying degrees, elements of credit risk in excess of amounts recognized in the consolidated balance sheets. Losses would be experienced when the Company is contractually obligated to make a payment under these instruments and must seek repayment from the borrower, which may not be as financially sound in the current period as they were when the commitment was originally made. 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. The Company enters into credit arrangements that generally provide for the termination of advances in the event of a covenant violation or other event of default. 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 Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the party. The commitments are collateralized by the same types of assets used as loan collateral.

As with outstanding loans, the Company applies qualitative factors and utilization rates to its off-balance sheet obligations in determining an estimate of losses inherent in these contractual obligations. The estimate for loan losses on off-balance sheet instruments is included within other liabilities and the charge to income that establishes this liability is included in non-interest expense.

Foreclosed Real Estate and Repossessed Assets

Foreclosed real estate and other repossessed assets are recorded at fair value at the time of foreclosure less estimated costs to sell. Any excess of loan balance over the fair value less estimated costs to sell of the other assets is charged-off against the allowance for loan losses. Any excess of the fair value less estimated costs to sell over the loan balance is recorded as a loan loss recovery to the extent of the loan loss previously charged-off against the allowance for loan losses; and, if greater, recorded as a gain on foreclosed assets. Subsequent to the legal ownership date, the Company periodically performs a new valuation and the asset is carried at the lower of carrying amount or fair value less estimated costs to sell. Operating expenses or income, and gains or losses on disposition of such properties, are recorded in current operations.

Income Taxes

The Company uses the asset and liability method, which recognizes an asset or liability representing the tax effects of future deductible or taxable amounts that have been recognized in the consolidated financial statements. Due to tax regulations, certain items of income and expense are recognized in different periods for tax return purposes than for financial statement reporting. These items represent “temporary differences.” Deferred income taxes are recognized for the tax effect of temporary differences between the tax basis of assets and liabilities and their financial reporting amounts at each period end based on enacted tax laws and statutory tax rates applicable to the periods in which the differences are expected to affect taxable income. A valuation allowance is established for deferred tax assets if, based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets may not be realized. Any interest or penalties assessed by the taxing authorities is classified in the financial statements as income tax expense. Deferred tax assets are included in other assets on the consolidated balance sheets.

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Management evaluates the Company's deferred tax asset for recoverability using a consistent approach which considers the relative impact of negative and positive evidence, including the Company's historical profitability and projections of future taxable income. The Company is required to establish a valuation allowance for deferred tax assets and record a charge to income if management determines, based on available evidence at the time the determination is made, that it is more likely than not that some portion or all of the deferred tax assets may not be realized.

The Company is subject to the provisions of ASC 740, Income Taxes ("ASC 740"). ASC 740 prescribes a more likely than not threshold for the financial statement recognition of uncertain tax positions. ASC 740 clarifies the accounting for income taxes by prescribing a minimum recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. On a quarterly basis, the Company evaluates income tax accruals in accordance with ASC 740 guidance on uncertain tax positions.

Earnings Per Share

Basic earnings per common share is computed using the weighted average number of common shares outstanding for the period divided into the net income. Diluted earnings per share include the effect of all dilutive potential common shares for the period. Potentially dilutive common shares include stock options and warrants.

Recent Accounting Pronouncements

In May 2014, the FASB issued guidance codified within ASU 2014-09, "Revenue Recognition - Revenue from Contracts with Customers," which amends the guidance in former Topic 605, Revenue Recognition. The new revenue recognition standard will supersede virtually all revenue guidance in U.S. GAAP, including industry specific guidance. The guidance in this Update affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets, unless those contracts are within the scope of other standards. ASU 2014-09 is effective for the Company for annual reporting periods beginning after December 15, 2016. In August 2015, this effective date was extended for the Company to December 15, 2017. The Company may elect to apply the amendments of this Update using one of the following two methods: 1) retrospectively to each prior reporting period presented or 2) retrospectively with the cumulative effect of initially applying this Update recognized at the date of initial application. The Company has made significant progress in evaluating the impact of the new standard on our revenue sources, and continues to evaluate its effect on our financial statement disclosures. A preliminary evaluation including the selection of an adoption method is expected to be completed by the end of the first part of 2017. The Company believes it is following an appropriate timeline to allow for proper recognition, presentation and disclosure upon adoption of the standard effective the beginning of 2018 and does not expect the adoption of this standard to have a material impact on the Company's Consolidated Financial Statements.

In January 2016, the FASB issued guidance codified within ASU 2016-01, "Financial Instruments – Overall, Subtopic 825-10: Recognition and Measurement of Financial Assets and Financial Liabilities," which amends certain guidance on classification and measurement of financial instruments. The update is intended to enhance the reporting model for financial instruments to provide users of financial instruments with more decision-useful information and addresses certain aspects of the recognition, measurement, presentation, and disclosure of financial instruments. ASU 2016-01 is effective for the Company for annual reporting periods beginning after December 15, 2017. The Company is currently evaluating the impact of the provisions in this standard on the Company's Consolidated Financial Statements. The adoption of this standard is not anticipated to have a material impact on the Company's Consolidated Financial Statements.

In February 2016, the FASB amended its standards with respect to the accounting for leases. The amended guidance serves to replace all current U.S. GAAP guidance on this topic and requires that an operating lease be recognized on

the statement of financial condition as a "right-to-use" asset along with a corresponding liability representing the rent obligation. Key aspects of current lessor accounting remain unchanged from existing guidance. This standard is expected to result in an increase to assets and liabilities recognized and, therefore, increase risk-weighted assets for regulatory capital purposes. The guidance requires the use of the modified retrospective transition approach for existing leases that have not expired before the date of initial application and will become effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The standard is effective for the Company as of January 1, 2019. The Company is currently evaluating the impact of the amended guidance on the Company's Consolidated Financial Statements and has not yet determined the effect of the standard on our ongoing financial reporting.

In March 2016, the FASB issued update guidance codified within ASU-2016-09, "Compensation – Stock Compensation (Topic 718), Improvements to Employee Share-Based Payment Accounting," which amends the guidance on certain aspects of share-based payments to employees. The new guidance will require entities to recognize all income tax effects of awards in the income statement when the awards vest or are settled. The guidance requires the use of the modified retrospective transition method by means of a cumulative-effect adjustment to equity as of the beginning of the period in which the guidance is adopted. The standard was effective for the Company as of January 1, 2017. The adoption of this standard did not have a material impact on the Company's Consolidated Financial Statements.

In June of 2016, the FASB issued update guidance codified within ASU-2016-13, “Financial Instruments – Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments,” which amends the guidance for recognizing credit losses from an “incurred loss” methodology that delays recognition of credit losses until it is probable a loss has been incurred to an expected credit loss methodology. The guidance requires the use of the modified retrospective transition method by means of a cumulative-effect adjustment to equity as of the beginning of the period in which the guidance is adopted. The standard is effective for the Company as of January 1, 2020. The Company is currently evaluating the impact of the amended guidance and has not yet determined the effect of the standard on its ongoing financial reporting.

In March 2017, the FASB issued updated guidance codified within ASU-2017-08, “Receivables – Nonrefundable Fees and Other Costs (Subtopic 310-20),” which is intended to enhance the accounting for the amortization of premiums for purchased callable debt securities. The standard is effective for the Company as of January 1, 2019. The Company does not believe the standard will have a material impact on the Company’s financials.

2. INVESTMENT SECURITIES

The amortized cost and estimated fair value of investment securities are as follows:

	March 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
Securities available-for-sale	(in thousands)			
U.S. government agency notes	$10,233	$ 49	$ (62)	$ 10,220
U.S. government agency collateralized mortgage obligations ("CMO")	16,477	46	(82)	16,441
Equity securities: Farmer Mac class A stock	66	49	-	115
Total	$26,776	$ 144	$ (144)	$ 26,776
Securities held-to-maturity				
U.S. government agency mortgage backed securities ("MBS")	$8,613	$ 293	$ (128)	$ 8,778
Total	$8,613	$ 293	$ (128)	$ 8,778

	December 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
Securities available-for-sale	(in thousands)			
U.S. government agency notes	$5,634	$ -	$ (62)	$ 5,572
U.S. government agency collateralized mortgage obligations ("CMO")	17,031	48	(85)	16,994
Equity securities: Farmer Mac class A stock	66	49	-	115
Total	$22,731	$ 97	$ (147)	$ 22,681
Securities held-to-maturity				
U.S. government agency mortgage backed securities ("MBS")	$9,002	$ 298	$ (151)	$ 9,149
Total	$9,002	$ 298	$ (151)	$ 9,149

At March 31, 2017 and December 31, 2016, $35.4 million and $31.7 million of securities at carrying value, respectively, were pledged to the Federal Home Loan Bank ("FHLB"), as collateral for current and future advances.

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The maturity periods and weighted average yields of investment securities at the period ends indicated were as follows:

	March 31, 2017									
	Less than One Year		One to Five Years		Five to Ten Years		Over Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Securities available-for-sale	(dollars in thousands)									
U.S. government agency notes	$1,970	2.6 %	$ 1,933	1.1 %	$ 6,317	1.4 %	$ -	-	$ 10,220	1.6 %
U.S. government agency CMO	-	-	3,250	1.7 %	10,110	1.4 %	3,081	1.8 %	16,441	1.5 %
Farmer Mac class A stock	-	-	-	-	-	-	-	-	115	-
Total	$1,970	2.6 %	$ 5,183	1.5 %	$ 16,427	1.4 %	$ 3,081	1.8 %	$26,776	1.5 %
Securities held-to-maturity										
U.S. government agency MBS	$-	-	$ 964	4.6 %	$ 4,991	3.2 %	$ 2,658	2.5 %	$8,613	3.2 %
Total	$-	-	$ 964	4.6 %	$ 4,991	3.2 %	$ 2,658	2.5 %	$8,613	3.2 %

	December 31, 2016									
	Less than One Year		One to Five Years		Five to Ten Years		Over Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Securities available-for-sale	(dollars in thousands)									
U.S. government agency notes	$1,973	2.6 %	$ 1,963	0.8 %	$ 1,636	1.3 %	$ -	-	$5,572	1.6 %
U.S. government agency CMO	-	-	2,063	1.9 %	11,827	1.1 %	3,104	1.5 %	16,994	1.2 %
Farmer Mac class A stock	-	-	-	-	-	-	-	-	115	-
Total	$1,973	2.6 %	$ 4,026	1.4 %	$ 13,463	1.1 %	$ 3,104	1.5 %	$22,681	1.3 %
Securities held-to-maturity										
U.S. government agency MBS	$-	-	$ 797	5.0 %	$ 5,531	3.2 %	$ 2,674	2.5 %	$9,002	3.2 %
Total	$-	-	$ 797	5.0 %	$ 5,531	3.2 %	$ 2,674	2.5 %	$9,002	3.2 %

The amortized cost and fair value of investment securities by contractual maturities as of the periods presented were as shown below:

	March 31, 2017		December 31, 2016	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value

Securities available-for-sale	(in thousands)			
Due in one year or less	$1,996	$ 1,970	$1,995	$ 1,973
After one year through five years	5,189	5,183	4,027	4,026
After five years through ten years	16,418	16,427	13,508	13,463
After ten years	3,107	3,081	3,135	3,104
Farmer Mac class A stock	66	115	66	115
	$26,776	$ 26,776	$22,731	$ 22,681
Securities held-to-maturity				
Due in one year or less	$-	$ -	$-	$ -
After one year through five years	964	1,055	797	864
After five years through ten years	4,991	5,194	5,531	5,762
After ten years	2,658	2,529	2,674	2,523
	$8,613	$ 8,778	$9,002	$ 9,149

Actual maturities may differ from contractual maturities as borrowers or issuers have the right to prepay or call the investment securities. Changes in interest rates may also impact prepayments.

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The following tables show all securities that are in an unrealized loss position:

	March 31, 2017					
	Less Than Twelve Months		More Than Twelve Months		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Securities available-for-sale	(in thousands)					
U.S. government agency notes	$32	$3,903	$ 30	$ 1,622	$62	$5,525
U.S. government agency CMO	33	6,807	49	1,691	82	8,498
Equity securities: Farmer Mac class A stock	-	-	-		-	-
	$65	$10,710	$ 79	$ 3,313	$144	$14,023
Securities held-to-maturity						
U.S. Government-agency MBS	$128	$2,529	$ -	$ -	$128	$2,529
Total	$128	$2,529	$ -	$ -	$128	$2,529

	December 31, 2016					
	Less Than Twelve Months		More Than Twelve Months		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Securities available-for-sale	(in thousands)					
U.S. government agency notes	$29	$3,936	$ 33	$ 1,636	$62	$5,572
U.S. government agency CMO	35	7,930	50	1,601	85	9,531
Equity securities: Farmer Mac class A stock	-	-	-		-	-
	$64	$11,866	$ 83	$ 3,237	$147	$15,103
Securities held-to-maturity						
U.S. Government-agency MBS	$151	$3,312	$ -	$ -	$151	$3,312
Total	$151	$3,312	$ -	$ -	$151	$3,312

As of March 31, 2017 and December 31, 2016, there were 16 and 17 securities, respectively, in an unrealized loss position. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers, among other things (i) the length of time and the extent to which the fair value has been less than cost (ii) the financial condition and near-term prospects of the issuer and (iii) the Company's intent to sell an impaired security and if it is not more likely than not it will be required to sell the security before the recovery of its amortized basis.

The unrealized losses are primarily due to increases in market interest rates over the yields available at the time the underlying securities were purchased. The fair value is expected to recover as the bonds approach their maturity date, repricing date or if market yields for such investments decline. Management does not believe any of the securities are impaired due to reasons of credit quality. Accordingly, as of March 31, 2017 and December 31, 2016, management believes the impairments detailed in the table above are temporary and no other-than-temporary impairment loss has been realized in the Company's consolidated income statements.

3. LOANS HELD FOR SALE

SBA and Agriculture Loans

As of March 31, 2017 and December 31, 2016, the Company had approximately $27.0 million and $26.5 million, respectively, of SBA loans included in loans held for sale. As of March 31, 2017 and December 31, 2016, the principal balance of SBA loans serviced for others was $13.6 million and $14.2 million, respectively.

The Company's agricultural lending program includes loans for agricultural land, agricultural operational lines, and agricultural term loans for crops, equipment and livestock. The primary products are supported by guarantees issued from the USDA, FSA, and the USDA Business and Industry loan program.

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As of March 31, 2017 and December 31, 2016, the Company had $32.8 million and $34.9 million of USDA loans included in loans held for sale, respectively. As of March 31, 2017 and December 31, 2016, the principal balance of USDA loans serviced for others was $1.2 million.

4. LOANS HELD FOR INVESTMENT

The composition of the Company's loans held for investment loan portfolio follows:

	March 31, 2017	December 31, 2016
	(in thousands)	
Manufactured housing	$202,332	$ 194,222
Commercial real estate	303,795	272,142
Commercial	70,798	70,369
SBA	10,173	10,164
HELOC	10,462	10,292
Single family real estate	11,727	12,750
Consumer	74	87
	609,361	570,026
Allowance for loan losses	(7,785)	(7,464)
Deferred fees, net	(461)	(453)
Discount on SBA loans	(165)	(170)
Total loans held for investment, net	$600,950	$ 561,939

The following table presents the contractual aging of the recorded investment in past due held for investment loans by class of loans:

	March 31, 2017							
	Current	30-59 Days* Past Due	60-89 Days* Past Due	Over 90 Days* Past Due	Total Past Due	Nonaccrual	Total	Recorded Investment Over 90 Days and Accruing
	(in thousands)							
Manufactured housing	$201,344	$ 248	$ -	$ -	$ 248	$ 740	$202,332	$ -
Commercial real estate:								
Commercial real estate	237,991	-	-	-	-	137	238,128	-
SBA 504 1st trust deed	26,560	-	-	-	-	212	26,772	-
Land	3,121	-	-	-	-	-	3,121	-
Construction	35,774	-	-	-	-	-	35,774	-
Commercial	68,995	3	-	-	3	1,800	70,798	-
SBA	9,444	-	-	-	-	729	10,173	-
HELOC	10,094	-	-	-	-	368	10,462	-
	11,518	-	-	21	21	188	11,727	21

Single family real estate				
Consumer	74	-	-	-