

2017

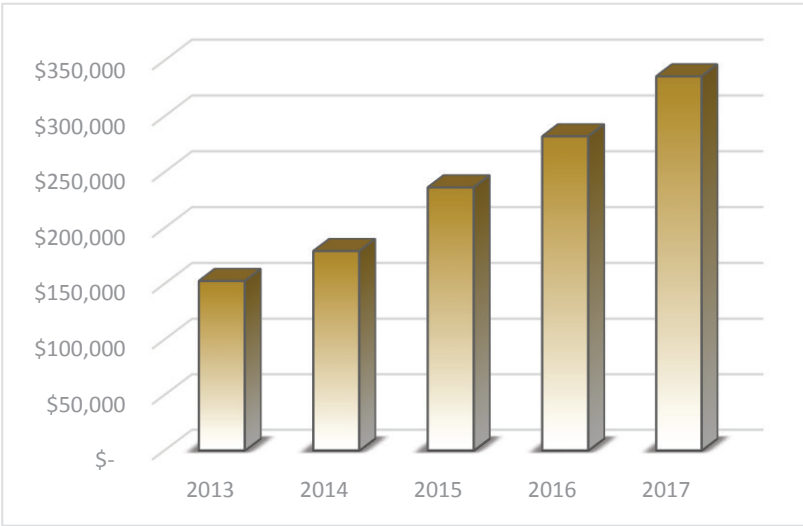
ANNUAL REPORT



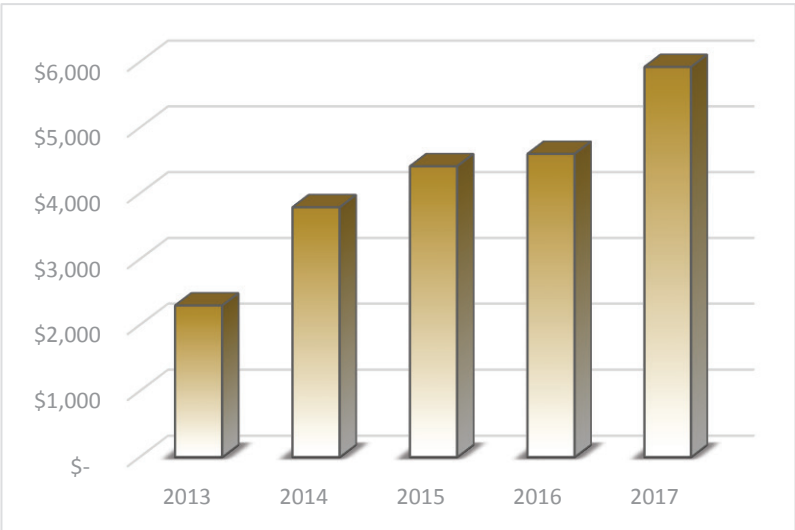
SUMMITBANK

PERFORMANCE HIGHLIGHTS

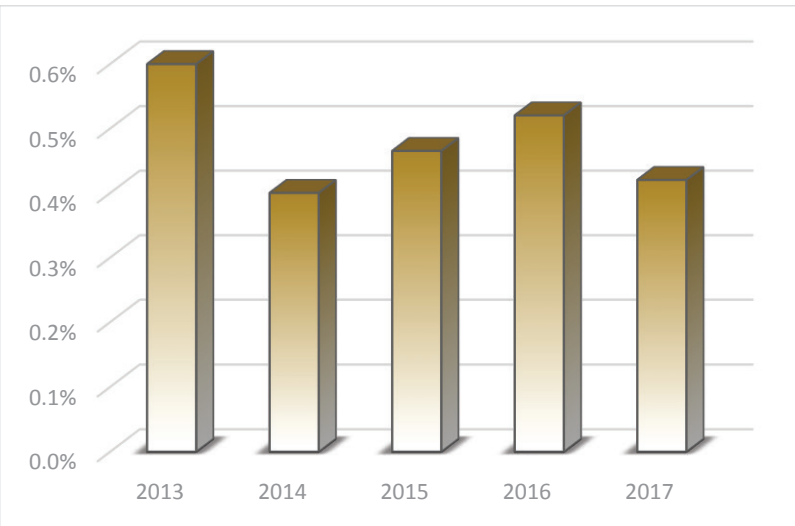
TOTAL ASSETS (in thousands)



NET INCOME BEFORE TAXES (in thousands)



NON-PERFORMING ASSETS AS A PERCENTAGE OF ASSETS



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To our Shareholders,

We begin this letter with an expression of gratitude and appreciation for our clients, shareholders and colleagues who comprise the dynamic team that is Summit Bank. In a time of extensive bank consolidation, we recognize the significance of Summit Bank's independence and local ownership. Now more than ever, we remain committed to community banking and the core values of integrity, confidentiality, service, team work and community that are inherent in Summit's culture and reflected in the way we do business.

Why is community banking important? All Summit's banking decisions are made locally. This, along with strong homegrown support and relationships, is the reason we are the local community bank of choice for businesses and professionals in the markets we serve.

2017 was a record year for Summit Bank. Our net income for the fiscal year was \$3.28 million, which is a 15% increase in earnings over \$2.86 million in 2016. We achieved our fifth consecutive year of annual loan growth in excess of 20%. Deposit growth this year was also strong with total deposits increasing by \$44.9 million, or 17.7%, over 2016. These accomplishments can be attributed to the continued success of our clients and the addition of new relationships. In addition, Summit was named the Top Community Bank Lender in Oregon for U.S. Small Business Administration (SBA) loans for the third year in a row.

In a report released from S&P Global Market Intelligence, Summit Bank was named one of the top performing banks in the country. This report ranks all community banks under \$1 billion in assets. Summit ranked number 78 in 2017, which puts the Bank in the top two percent of the nearly 4,600 community banks headquartered throughout the country.

Also in 2017, Summit was recognized for the first time by *Oregon Business Magazine* as one of the 100 Best Companies to Work For in Oregon. We ranked #19 for medium-size companies, and were acknowledged for excellence in work environment,

*Our net
income for
the fiscal year
was \$3.28
million,
which is a
15% increase
in earnings.*



management, communications, decision-making, career development, benefits and compensation. This award helps validate the emphasis on a strong internal culture and that Summit Bank is a great place to work.

Other investments this year included technological advancements to assist our clients to be more efficient. We have rolled out innovative new products, including Direct Connect, a dot bank web site (which comes with additional security features to keep our clients' personal and financial information safe), Business Mobile Banking, Online Wire Manager and ACH Manager.

Our Central Oregon office continues to grow and thrive, so much so that we are currently in the midst of constructing additional office space. In an effort to provide a greater impact in Central Oregon, the Bank formed a Central Oregon Advisory Board, which consists of business and community leaders throughout the region including Jamie Danek of Humm Kombucha; Jay Moore, MD, MPH of The Center; Wes Price of Price Fronk & Co. CPA Firm; Bill Smith of William Smith Properties; Hayden Watson of Hayden Homes; and Becca Williams, owner of Red Plate Foods.

Summit also added a returning board member, Ann Marie Mehlum, who was previously a founding director and Chief Executive Officer of Summit Bank. She brings institutional knowledge, outstanding leadership and banking expertise to our board.

In short, 2017 was a strong year for Summit Bank. We are thankful for our colleagues, whose dedication and commitment make Summit Bank one of the best places to work in the State of Oregon; for our clients who continue to grow and thrive with us; and our shareholders, who believe that our community's business owners, professionals and individuals deserve attention, professionalism and dedication from their banking team. Thanks to all of you for continuing to make Summit your local bank of choice.

Sincerely,



R. Paul Weinhold
Board Chair



Craig A. Wanichuk
President & CEO

*Also in 2017,
Summit was
recognized for
the first time
by Oregon
Business
Magazine
as one of
the 100 Best
Companies
to Work For
in Oregon.*



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Independent Auditors' Report

To the Board of Directors and
Stockholders of Summit Bank

We have audited the accompanying balance sheets of Summit Bank as of December 31, 2017 and 2016, and the related statements of income, comprehensive income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' 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 auditors consider 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 Summit Bank as of December 31, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

DELAP LLP

March 13, 2018

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SUMMITBANK
BALANCE SHEETS

	December 31	
	2017	2016
ASSETS		
Cash and cash equivalents:		
Cash and due from banks	\$ 10,289,330	\$ 11,595,785
Interest-bearing deposits with other banks	2,173,218	1,835,887
Deposits with Federal Reserve Bank	28,502,391	23,217,004
Total cash and cash equivalents	40,964,939	36,648,676
Investment securities available-for-sale, at estimated fair value	5,388,179	5,833,268
Loans, less allowance for loan losses	276,502,843	226,967,658
Interest receivable	1,034,066	827,948
FHLB and PCBB stock, at cost	778,400	723,600
Premises and equipment, net of accumulated depreciation	4,834,430	4,926,904
Deferred income taxes, net	924,195	1,079,967
Repossessioned assets, net	1,031,060	1,016,304
Cash surrender value of bank-owned life insurance	3,708,474	3,655,538
Other assets	522,852	316,979
Total assets	\$ 335,689,438	\$ 281,996,842
LIABILITIES and STOCKHOLDERS' EQUITY		
Liabilities:		
Deposits:		
Noninterest-bearing demand	\$ 86,498,040	\$ 89,511,363
Savings and interest-bearing demand	185,881,945	136,743,287
Time deposits	26,232,634	27,454,953
Total deposits	298,612,619	253,709,603
Interest payable	89,591	78,706
Other liabilities	2,317,001	1,684,865
Repurchase agreements	136,378	1,631,664
Total liabilities	301,155,589	257,104,838
Stockholders' equity:		
Preferred stock, no par value; 1,000,000 shares authorized; none issued	-	-
Common stock, no par value; 10,000,000 shares authorized, 4,095,961 and 3,549,766 shares outstanding in 2017 and 2016	19,888,805	13,529,594
Retained earnings	14,652,721	11,369,466
Accumulated other comprehensive loss	(7,677)	(7,056)
Total stockholders' equity	34,533,849	24,892,004
Total liabilities and stockholders' equity	\$ 335,689,438	\$ 281,996,842

The accompanying notes are an integral part of these financial statements.

SUMMITBANK
STATEMENTS OF INCOME

	Year Ended December 31	
	2017	2016
Interest income:		
Interest and fees on loans	\$ 15,885,890	\$ 12,420,262
Interest on investment securities	116,656	114,446
Interest on deposits with other banks	365,885	146,775
Total interest income	16,368,431	12,681,483
Interest expense	676,566	413,568
Net interest income	15,691,865	12,267,915
Provision for loan losses	2,280,085	1,380,536
Net interest income after provision for loan losses	13,411,780	10,887,379
Noninterest income:		
Gains on sales of loans and securities	775,463	603,954
Bank card and interchange fees	309,738	228,053
Service charges on deposit accounts	92,908	143,887
Real estate lease income	81,462	132,272
Loan servicing fees	157,206	105,869
Bank-owned life insurance income	52,936	67,116
Losses on sales and write-downs of repossessed assets, net	(415,762)	(378,005)
Other	303,202	200,016
Total noninterest income	1,357,153	1,103,163
Noninterest expense:		
Salaries and employee benefits	6,028,641	5,197,660
Occupancy and equipment expense	599,053	555,425
Data processing	589,139	477,148
Repossessed assets expenses	172,421	69,885
Other	1,458,132	1,090,410
Total noninterest expense	8,847,386	7,390,528
Income before income taxes	5,921,547	4,600,013
Income tax provision	2,638,292	1,744,612
Net income	\$ 3,283,255	\$ 2,855,401
Earnings per share:		
Basic	\$.84	\$.81
Diluted	\$.83	\$.80

The accompanying notes are an integral part of these financial statements.

STATEMENTS OF COMPREHENSIVE INCOME

	Year Ended December 31	
	2017	2016
Net income	\$ 3,283,255	\$ 2,855,401
Other comprehensive income (loss):		
Change in unrealized gains (losses) on investment securities available-for-sale	(6,254)	(20,248)
Tax effect of the change in unrealized gains (losses) on investment securities available-for-sale	5,633	5,000
Comprehensive income	<u>\$ 3,282,634</u>	<u>\$ 2,840,153</u>

The accompanying notes are an integral part of these financial statements.

STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

For the Years Ended December 31, 2017 and 2016

	Common Stock		Retained	Accumulated	
	Shares	Amount	Earnings	Other Comprehensive Income (loss)	Total
Balance, December 31, 2015	3,510,239	\$ 13,231,581	\$ 8,514,065	\$ 8,192	\$ 21,753,838
Net income			2,855,401		2,855,401
Other comprehensive income (loss)				(15,248)	(15,248)
Issuance of common stock, net	6	-			-
Stock options exercised	31,080	180,477			180,477
Share-based compensation	8,441	117,536			117,536
Balance, December 31, 2016	3,549,766	13,529,594	11,369,466	(7,056)	24,892,004
Net income			3,283,255		3,283,255
Other comprehensive income (loss)				(621)	(621)
Issuance of common stock, net of stock offering costs	470,048	5,993,113			5,993,113
Stock options exercised	67,155	238,680			238,680
Share-based compensation	8,992	127,418			127,418
Balance, December 31, 2017	4,095,961	\$ 19,888,805	\$ 14,652,721	\$ (7,677)	\$ 34,533,849

The accompanying notes are an integral part of these financial statements.

STATEMENTS OF CASH FLOWS

	Year Ended December 31	
	2017	2016
Cash flows from operating activities:		
Net income	\$ 3,283,255	\$ 2,855,401
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	339,144	342,541
Share-based compensation	127,418	117,536
Amortization of investment premiums, net	32,791	52,205
Provision for loan losses	2,280,085	1,380,536
Gains on sales of loans and securities	(775,463)	(603,954)
Bank-owned life insurance income	(52,936)	(67,116)
Losses on sales of repossessed assets, net	184,183	176,177
Write-downs of repossessed assets	231,579	201,828
Deferred income taxes	155,772	(3,000)
Change in:		
Interest receivable and other assets	(411,991)	(245,537)
Deferred loan fees	146,106	154,684
Interest payable and other liabilities	643,021	(1,616,497)
Net cash provided by operating activities	6,182,964	2,744,804
Cash flows from investing activities:		
Purchases of investment securities	(1,957,137)	(2,889,648)
Sales of investment securities	-	62,993
Purchases of FHLB stock	(54,800)	(68,400)
Principal payments and maturities of investment securities	2,368,814	2,563,060
Net proceeds from sales of loans	9,272,394	14,453,618
Purchases of loans	(1,402,605)	(3,694,160)
Proceeds from sales of repossessed assets	1,182,683	468,578
Purchase of bank-owned life insurance	-	(500,000)
Loans originated, net of principal collected	(60,668,903)	(55,120,373)
Purchases of premises and equipment	(246,670)	(111,713)
Net cash used in investing activities	(51,506,224)	(44,836,045)
Cash flows from financing activities:		
Net increase in deposits	44,903,016	43,980,903
Proceeds from common stock offering, net of costs	5,993,113	-
Increase (decrease) in repurchase agreements	(1,495,286)	189,368
Proceeds from stock options exercised	238,680	180,477
Net cash provided by financing activities	49,639,523	44,350,748
Net increase in cash and cash equivalents	4,316,263	2,259,507
Cash and cash equivalents, beginning of year	36,648,676	34,389,169
Cash and cash equivalents, end of year	\$ 40,964,939	\$ 36,648,676
Supplemental information:		
Cash paid during the year for interest	\$ 665,681	\$ 409,561
Cash paid during the year for income taxes	1,779,849	1,829,268
Change in unrealized gains and losses on investment securities available-for-sale, net of deferred income taxes	(621)	(15,248)
Transfer of loans to repossessed assets	\$ 1,613,201	\$ 940,898

The accompanying notes are an integral part of these financial statements.

1. Summary of Significant Accounting Policies:

Nature of Operations – Summit Bank (the Bank) provides commercial banking, financing, real estate lending and other services primarily in Lane and Deschutes Counties in Oregon.

Financial Statement Presentation – The accounting and reporting policies of the Bank conform with accounting principles generally accepted in the United States of America (GAAP) and prevailing practices within the banking industry. The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and the disclosure 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. The most significant estimates are the allowance for loan losses and fair value estimates. The Bank has evaluated subsequent events through March 13, 2018, the date the financial statements were available to be issued.

Cash and Cash Equivalents – For purposes of reporting cash flows, cash and cash equivalents are cash on-hand and due from banks. Such amounts include both interest-bearing and non interest-bearing deposits with other banks, short-term time deposits, and federal funds sold on an overnight basis and may exceed amounts insured by the Federal Deposit Insurance Corporation (FDIC).

Investment Securities – The Bank classifies all investment securities as available-for-sale. Securities available-for-sale are held for indefinite periods of time and may be sold in response to changes in market interest rates, shifts in the maturity mix or concentration of Bank assets or liabilities, or to alleviate liquidity demands. Securities designated as available-for-sale are reported at estimated fair value. Unrealized gains and losses are excluded from earnings and are included in other comprehensive income (loss) in stockholders' equity, net of applicable deferred taxes.

Gains and losses realized on sales of securities are recognized using the specific identification method. Interest income on debt securities is included in income using the effective interest method. Interest income includes accretion and amortization of discounts and premiums resulting from securities purchased at other than par value. Both are calculated using a "constant yield" methodology either to maturity (for non-callable securities) or to "worst call date" for callable securities. Premiums and discounts on mortgage backed securities are amortized/accreted based upon current and expected future rates of prepayments on the securities.

The Bank evaluates its securities classified as available-for-sale for other-than-temporary impairments (OTTI) in accordance with GAAP. Accordingly, for investment securities that are in an unrealized loss position, the Bank assesses whether it intends to sell or it is more likely than not that it will be required to sell a security before recovery of its amortized cost basis.

For investment securities that are considered other-than-temporarily impaired and that the Bank does not intend to sell and will not be required to sell prior to recovery of the amortized cost basis, the Bank would separate the amount of the impairment into the amount that is credit related (credit loss component) and the amount due to all other factors. The credit loss component would be recognized in earnings and would be the difference between the security's amortized cost basis and the present value of its expected future cash flows discounted at the security's effective yield. The remaining difference between the security's fair value and the present value of expected future cash flows would be due to factors that are not credit related and would be recognized in other comprehensive income (loss). Management believes that any unrealized losses on investment securities at December 31, 2017 are temporary.

Loans and Income Recognition – Loans are stated at the amount of unpaid principal, reduced by net deferred loan origination fees and an allowance for loan losses. Interest on loans is calculated using the simple-interest method on daily balances of the principal amounts outstanding. Accrual of interest is discontinued on a loan when management believes, after considering economic and business conditions and collection efforts, that the borrower's financial condition is such that collection of the interest is doubtful. Payments received on nonaccrual loans are applied to the principal balance and no interest income is recognized. Interest income is subsequently recognized only to the extent cash payments are received satisfying all delinquent principal and interest amounts, and the prospects for future payments in accordance with the loan agreement appear relatively certain. A nonaccrual loan may be restored to accrual status when none of its principal and interest is due and unpaid and the Bank expects full repayment of the remaining contractual principal and interest, or when it otherwise becomes well secured and in the process of collection. Loan origination fees, net of associated direct costs, if significant, are deferred and amortized using the interest or straight-line method over the contractual life of the loan as an adjustment of the yield of the related loan. If a loan is repaid prior to maturity, any remaining unamortized net deferred origination fee is recognized in income at the time of repayment.

Allowance for Loan Losses – The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged off against the allowance when management believes that the collectability of the principal is unlikely. The allowance is an amount that management considers adequate to absorb possible losses on existing loans that may become uncollectible based on evaluations of the collectability of loans and prior loss experience. While management has allocated the allowance for loan losses to various loan classes, the allowance is general in nature and is available for the loan portfolio in its entirety. The allowance for loan losses consists of general and specific components.

The general component covers all non-impaired loans. For all such loans – other than small commercial equipment loans – the general component is based on the Bank's risk rating system and historical loss experience adjusted for qualitative factors. The Bank calculates its historical loss rates by using a combination of (1) a weighted-average of the Bank's most recent 36 months of loss history, with more weight applied to more current months, and (2) historical loss data for Oregon and certain peer banks. The Bank calculates and applies its historical loss rates by individual loan types in its portfolio. These historical loss rates are adjusted for qualitative and environmental factors including, but not limited to: changes in the concentrations, trends and current nature of the loan portfolio; overall portfolio quality; results from internal and external loan reviews; review of specific problem loans; and current economic conditions that may affect the borrower's ability to pay.

Small commercial equipment loans are reserved for as a pool of smaller-balance homogeneous loans. The methodology employed to assign reserve rates is migration analysis wherein probable loss rates are established as migration occurs through risk ratings. The Bank revisits these loss rates at regular intervals, and adjusts the applicable rates as dictated through loss experience. As individual loans migrate downward through established risk ratings, increasing reserves as estimated by the aforementioned migration analysis are applied to related loan balances.

The specific component of the allowance relates to loans that are considered impaired. A loan is considered impaired when management believes that it is probable that all amounts will not be collected according to the contractual terms. An impaired loan is valued using the estimated fair value of the loan's collateral (less estimated costs to sell) or related government guaranty, the present value of expected cash flows discounted at the loan's effective interest rate, or the observable market price of the loan. These estimates are necessarily subjective and may be adjusted as more current information becomes available. Any adjustment could be significant.

NOTES TO FINANCIAL STATEMENTS

Federal and state bank regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan losses. Such agencies may require the Bank to recognize additions to the allowance in the future based on their judgment of the information available to them at the time of their examinations.

Allowance for Unfunded Loan Commitments – The Bank maintains a separate reserve for estimated losses related to unfunded loan commitments. The Bank estimates the amount of probable losses related to unfunded loan commitments by applying an estimated loss factor to the expected amount of commitments that will actually require funding. In accordance with industry practice and regulatory guidance, the reserve for estimated losses related to unfunded loan commitments is included in other liabilities in the accompanying balance sheets and was \$77,669 and \$63,870 as of December 31, 2017 and 2016 respectively. Changes in the reserve for estimated losses related to unfunded loan commitments are recorded in provision for loan losses in the accompanying statements of income.

Federal Home Loan Bank (FHLB) and Pacific Coast Bankers' Bank (PCBB) Stock – FHLB and PCBB stock consists of the following at December 31:

	2017	2016
FHLB stock	\$ 338,400	\$ 283,600
PCBB stock	440,000	440,000
	<u>\$ 778,400</u>	<u>\$ 723,600</u>

The Bank, as a member of the FHLB system, is required to maintain a minimum level of investment in FHLB stock based on specific percentages of its outstanding mortgages, total assets and FHLB advances. At December 31, 2017, the Bank's minimum required investment was \$338,400. Stock redemptions may be requested at par value and are made at the discretion of the FHLB. The Bank's investment in FHLB stock is carried at cost, which approximates its fair value. The Bank evaluates its investment in FHLB stock for impairment as needed. The Bank's determination of whether this investment is impaired is based on its assessment of the ultimate recoverability of cost rather than by recognizing temporary declines in value.

The Bank also holds an investment in its primary correspondent bank, PCBB. This investment is accounted for under the cost method.

Premises and Equipment – Premises and equipment are stated at cost, net of accumulated depreciation. Additions and betterments are capitalized. Expenditures for repairs and maintenance are charged to expense as incurred. Gains or losses realized from sales or retirements are reflected in current operations. Depreciation is computed by the straight-line method over the estimated useful lives of the assets.

Impairment of Long-lived Assets – The Bank accounts for long-lived assets at amortized cost. Management reviews long-lived assets for possible impairment whenever events or circumstances indicate that the carrying amount of such assets may not be recoverable. If there is an indication of impairment, management would prepare an estimate of future cash flows (undiscounted and without interest charges) expected to result from the use of the asset and its eventual disposition. If these estimated cash flows were less than the carrying amount of the asset, an impairment loss would be recognized to write down the asset to its estimated fair value.

Reposessed Assets – Repossessed assets consist of commercial equipment and commercial real property and are considered held-for-sale. Repossessed assets are initially recorded at fair value at the date of acquisition based on current appraisals and management's estimate of value, establishing

NOTES TO FINANCIAL STATEMENTS

a new cost basis. Any excess of the loan balance over the net realizable value of the property is charged to the allowance for loan losses when a property is acquired. Subsequent to acquisition, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less estimated costs to sell. Any revenue and expenses from operations are included in other noninterest expense. Gains and losses on sales, write-downs, and changes in valuation allowances are recorded in non-interest income.

The valuation of repossessed assets is subjective in nature and may be adjusted in future periods because of changes in economic conditions. The valuation of repossessed assets is also subject to review by bank regulatory authorities who may require increases or decreases to carrying amounts based on their evaluation of the information available to them at the time of their examination of the Bank.

Bank-owned Life Insurance (BOLI) - The Bank is the owner and beneficiary of BOLI on certain Bank officers. BOLI policies are recorded at their cash surrender values (net of surrender charges). Income from BOLI policies is recognized when earned and is included in noninterest income.

Advertising – Advertising costs are charged to expense during the period in which they are incurred. Advertising expenses were \$132,910 and \$67,604 for the years ended December 31, 2017 and 2016, respectively.

Income Taxes – Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are calculated on differences between the financial statement and tax basis of assets and liabilities using tax rates in effect for the year in which the differences are expected to be realized. A valuation allowance is recognized if, based on the available evidence, it is determined 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.

Uncertain tax positions that meet the more likely than not recognition threshold are measured to determine the amount of benefit to recognize. An uncertain tax position is measured at the amount of benefit that management believes has a greater than 50% likelihood of realization upon settlement. The Bank's policy is to recognize interest and penalties related to income tax settlements as a component of income tax expense.

The Bank files income tax returns for federal and various state jurisdictions. There is no material impact of potential tax uncertainties on the Bank's financial condition or results of operations at December 31, 2017.

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

Derivative Instruments – The Bank uses derivative financial instruments (interest rate swaps) to limit exposure to changes in interest rates related to specific loan assets. Derivatives entered into by the Bank are designated as fair value hedges and generally exhibit perfect effectiveness between changes in the value of the interest rate swap and the hedged instrument (loan asset). All derivatives and related hedged loans are recognized in the balance sheet at their fair values. Changes in the fair value of a derivative that is highly effective, along with the loss or gain on the hedged loan asset that is

attributable to the hedged risk, are recorded in current-period earnings. The Bank formally documents all relationships between hedging instruments and hedged assets, as well as its risk-management objective and strategy for undertaking various hedged transactions. The Bank also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values of hedged items.

The Bank would discontinue hedge accounting when: (1) it is determined that a derivative is no longer effective in offsetting changes in the fair value of the associated hedged loan asset; (2) the derivative expires or is sold, terminated, or exercised; or (3) management determines that designation of the derivative as a hedge instrument is no longer appropriate. The hedged loan asset would no longer be adjusted for changes in fair value and the derivative would be carried at its fair value in the balance sheet, with changes in its fair value recognized in current-period earnings.

Stockholders' Equity and Earnings per Share - Basic earnings per share are computed by dividing net income by the weighted average number of shares outstanding during the period. Diluted earnings per share include the effect of common stock equivalents that would arise from the exercise of stock options and the vesting of restricted stock and restricted stock units discussed in Note 9.

Share-Based Compensation - GAAP requires companies to measure compensation expense for all share-based payments based on the fair value of the awards at the grant date and recognize such costs as an expense over the requisite service period (which is generally the vesting period). See Note 9 for discussion of the Bank's share-based compensation arrangements.

SBA Loans Sales and Servicing - The Bank sells or transfers loans, including the government guaranteed portion of the loans (with loan servicing retained) for proceeds equal to the principal amount of loans, as adjusted to yield interest to the investor based upon the current market rates. The Bank records an asset representing the right to service sold loans when it retains the servicing rights. This asset is included in other assets in the accompanying balance sheet. The carrying value of loans sold is allocated between the loans and the servicing rights, based on their relative fair values. The fair value of servicing rights is estimated by discounting estimated future cash flows from servicing using discount rates that approximate current market rates and using estimated prepayment rates. The servicing rights, if any, are carried at the lower of cost or market and are amortized in proportion to, and over the period of the estimated net servicing income, assuming prepayments.

For purposes of evaluating and measuring impairment, the fair value of servicing rights is based on a discounted cash flow methodology, which considers current prepayment speeds and market discount rates. Impairment is measured as the amount by which the carrying value of servicing rights exceeds the related fair value. No impairment charges were recorded in 2017 or 2016 related to servicing assets and the Bank held no servicing rights assets as of December 31, 2017 and 2016.

New Accounting Pronouncements - In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09). ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (1) identify the contract(s) with a customer, (2) identify the performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations in the contract, and (5) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 is effective for annual periods, and interim reporting periods within those annual periods, beginning after December 15, 2017. The Bank does not expect the adoption of ASU 2014-09 to have a material impact on the Bank's

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future financial statements.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments – Overall: Recognition and Measurement of Financial Assets and Financial Liabilities* (ASU 2016-01). ASU 2016-01 generally requires equity investments – except those accounted for under the equity method of accounting or those that result in consolidation of the investee – to be measured at fair value with changes in fair value recognized in net income. However, an entity may choose to measure equity investments that do not have readily determinable fair values at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer. ASU 2016-01 is intended to simplify the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment. ASU 2016-01 also eliminates certain disclosures related to the fair value of financial instruments and requires entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. ASU 2016-01 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Bank does not expect the adoption of ASU 2016-01 to have a material impact on the Bank's future financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases* (ASU 2016-02). ASU 2016-02 is intended to increase transparency and comparability among organizations by requiring the recognition of lease assets and lease liabilities on the balance sheet and disclosure of key information about leasing arrangements. The principal change required by ASU 2016-02 relates to lessee accounting, and is that for operating leases, a lessee is required to (1) recognize a right-of-use asset and a lease liability, initially measured at the present value of the lease payments, in the statement of financial position, (2) recognize a single lease cost, calculated so that the cost of the lease is allocated over the lease term on a generally straight-line basis, and (3) classify all cash payments within operating activities in the statement of cash flows. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. If a lessee makes this election, it should recognize lease expense for such leases generally on a straight-line basis over the lease term. ASU 2016-02 also changes disclosure requirements related to leasing activities, and requires certain qualitative disclosures along with specific quantitative disclosures. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Bank is currently evaluating the impact that the adoption of ASU 2016-02 will have on the Bank's future financial statements.

In March 2016, the FASB issued ASU 2016-09, *Improvements to Employee Share-Based Payment Accounting* (ASU 2016-19). ASU 2016-09 includes provisions intended to simplify various aspects related to how share-based payments are accounted for and presented in the financial statements. ASU 2016-09 is effective for annual periods, and interim periods within those annual periods, beginning after December 31, 2016, with early adoption permitted. The Bank adopted ASU 2016-09 during the year ended December 31, 2017 and it did not have a significant impact on the accompanying financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments - Credit Losses* (ASU 2016-13). ASU 2016-13 replaces the existing incurred losses methodology for estimating allowances with a current expected credit losses methodology with respect to most financial assets measured at amortized cost and certain other instruments, including trade and other receivables, loans, held to maturity investment securities and off-balance sheet commitments. In addition, ASU 2016-13 requires credit losses relating to available for sale debt securities to be recorded through an allowance for credit losses rather than a reduction of the carrying amount. ASU 2016-13 also changes the accounting for purchased credit-impaired debt securities and loans. ASU 2016-13 retains many of the disclosure requirements in current GAAP and expands certain disclosure requirements. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Bank is currently evaluating the impact that the adoption of ASU 2016-13 will have on the Bank's

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future financial statements.

In March 2017, the FASB issued ASU 2017-08, *Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities* (ASU 2017-08). ASU 2017-08 shortens the amortization period for certain callable debt securities held at a premium. ASU 2017-08 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The adoption of ASU No. 2017-08 is not expected to have a material impact on the Bank's future financial statements.

In May 2017, the FASB issued ASU 2017-09, *Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting*. ASU 2017-09 was issued to provide clarity as to when to apply modification accounting when there is a change in the terms or conditions of a share-based payment award. According to ASU 2017-09, an entity should account for the effects of a modification unless the fair value, vesting conditions, and balance sheet classification of the award are the same after the modification as compared to the original award prior to modification. ASU 2017-09 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. The adoption of ASU 2017-09 is not expected to have a material impact on the Bank's future financial statements.

2. Restricted Assets:

The Bank must meet reserve requirements as established by Federal Reserve Board (FRB) regulation which were \$5,786,000 and \$2,675,000 at December 31, 2017 and 2016, respectively. Accordingly, the Bank complies with such requirements by holding cash on hand and maintaining average reserve balances on deposit with its primary correspondent bank in accordance with the regulations.

3. Investment Securities Available for Sale:

The tables below detail the amortized cost and estimated fair values of available-for-sale investment securities, as well as the amount of any unrealized losses and the length of time these unrealized losses existed as of the dates indicated:

December 31, 2017								
	Available-for-Sale			Securities in Continuous Unrealized Loss Position for Less Than 12 Months		Securities in Continuous Unrealized Loss Position for 12 Months or Longer		
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Obligations of U.S. Government and U.S. sponsored agencies	\$ 1,151,580	\$ -	\$ (4,864)	\$ 1,146,716	\$ -	\$ -	\$ 1,146,716	\$ (4,864)
Corporate debt securities	750,000	4,315	(3,579)	750,736	246,421	(3,579)	-	-
Mortgage-backed securities	3,499,909	7,044	(16,226)	3,490,727	1,810,718	(10,374)	415,499	(5,852)
	<u>\$ 5,401,489</u>	<u>\$ 11,359</u>	<u>\$ (24,669)</u>	<u>\$ 5,388,179</u>	<u>\$ 2,057,139</u>	<u>\$ (13,953)</u>	<u>\$ 1,562,215</u>	<u>\$ (10,716)</u>
December 31, 2016								
	Available-for-Sale			Securities in Continuous Unrealized Loss Position for Less Than 12 Months		Securities in Continuous Unrealized Loss Position for 12 Months or Longer		
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Obligations of U.S. Government and U.S. sponsored agencies	\$ 1,631,729	\$ -	\$ (5,490)	\$ 1,626,239	\$ 1,626,239	\$ (5,490)	\$ -	\$ -
Corporate debt securities	500,000	-	(2,316)	497,684	249,801	(199)	247,883	(2,117)
Mortgage-backed securities	3,708,595	12,176	(11,426)	3,709,345	1,852,253	(11,426)	-	-
	<u>\$ 5,840,324</u>	<u>\$ 12,176</u>	<u>\$ (19,232)</u>	<u>\$ 5,833,268</u>	<u>\$ 3,728,293</u>	<u>\$ (17,115)</u>	<u>\$ 247,883</u>	<u>\$ (2,117)</u>

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The unrealized losses on the Bank's investment securities were primarily attributable to increases in market interest rates subsequent to their purchase by the Bank. The Bank expects the fair value of these securities to recover as the securities approach their maturity dates or sooner if market yields for such securities decline. The Bank does not believe that these securities are other than temporarily impaired because of their credit quality or related to any issuer or industry specific event. Based on management's evaluation and intent, the unrealized losses related to the investment securities in the above tables are considered temporary.

The amortized cost and estimated fair value of investment securities at December 31, 2017 are shown below by contractual maturity or projected average life depending on the type of security. Obligations of U.S. government sponsored agencies and corporations are shown by contractual maturity. Mortgage-backed securities are disclosed by projected average life.

	Available-for-Sale	
	Amortized Cost	Estimated Fair Value
Due in one year or less	\$ 1,773,973	\$ 1,768,421
Due after one year through five years	3,132,164	3,121,584
Due after five years through ten years	495,352	498,174
	<u>\$ 5,401,489</u>	<u>\$ 5,388,179</u>

There were no sales of investment securities during the year ended December 31, 2017. Proceeds from sales of investment securities available-for-sale during the year ended December 31, 2016 were \$62,993; such sales resulted in a gross realized gain of \$2,251 which was included in 2016 earnings.

At December 31, 2017, investment securities with a total estimated fair value of \$4,594,240 and amortized cost of \$4,609,000 were pledged for FHLB borrowings, repurchase agreements and other purposes. At December 31, 2016, investment securities with a total estimated fair value of \$5,249,469 and amortized cost of \$5,255,478 were pledged for FHLB borrowings, repurchase agreements and other purposes.

4. **Loans and Allowance for Loan Losses:**

Major classifications of loans at December 31 are as follows:

NOTES TO FINANCIAL STATEMENTS

	2017	2016
Real Estate		
Acquisition, Development & Construction	\$ 13,778,058	\$ 13,084,669
Commercial	77,110,635	66,358,372
Multifamily	13,294,047	13,407,702
Owner Occupied	71,482,684	49,615,057
Commercial and Industrial		
Small Commercial Equipment	36,271,703	31,711,511
Other Commercial & Industrial	50,811,362	40,050,800
Consumer		
Secured	16,123,679	14,537,993
Unsecured	2,563,195	2,318,364
	<u>281,435,363</u>	<u>231,084,468</u>
Deferred Loan Origination Fees, net	(886,501)	(740,395)
	<u>280,548,862</u>	<u>230,344,073</u>
Allowance for Loan Losses	(4,046,019)	(3,376,415)
Loans receivable, net	<u><u>\$ 276,502,843</u></u>	<u><u>\$ 226,967,658</u></u>

Risk Elements – The Bank manages credit risk through lending limit constraints, credit review, approval policies and extensive ongoing internal monitoring. Additionally, credit risk is managed via diversification of the loan portfolio by loan, industry and borrower type as well as limits on the aggregation of debt to a single borrower. The Bank also obtains periodic credit file reviews from independent third-parties as part of its ongoing credit monitoring process. The following are the loan segment risk characteristics of the Bank's portfolio:

Acquisition, Development & Construction – Includes both loans and lines of credit for the purpose of purchasing, carrying and developing land into commercial developments or residential subdivisions. Also included in this designation are loans and lines of credit for construction of residential, multi-family and commercial buildings. Generally, the primary source of repayment is dependent upon the sale or refinance of the real estate collateral. Construction lending can involve a higher level of risk than other types of lending because funds are advanced based on a prospective value of the project at completion, the total estimated construction cost of the project, and the borrowers' equity at risk. Additionally, the repayment of the loan may be conditional on the success of the ultimate project which could be subject to interest rate changes, governmental regulations, general economic conditions and the ability of the borrower to sell or lease the property or refinance the indebtedness. The bank attempts to mitigate the risks associated with this type of credit by limiting concentration exposure and utilizing enhanced underwriting procedures as outlined in proprietary policies and procedures as approved by the board of directors not less than annually.

Commercial Real Estate – Loans in this category are assigned to one of two specific subcategories:

- **Commercial** – Includes loans to finance income-producing commercial properties. Loans in this class include retail centers, hotels, office buildings, single-tenant retail buildings, warehouses and other properties where the source of repayment on the loan comes primarily from non-related tenant lease income. There are board-approved enhanced underwriting

NOTES TO FINANCIAL STATEMENTS

procedures in place that govern the approval and funding of these types of loans, ensuring the highest probability of full repayment of principal.

- **Owner Occupied** – Includes loans secured by business facilities to finance business operations, equipment and owner-occupied facilities for commercial customers. Generally, the primary source of repayment is the operating cash flow from business activities of the owner of the property or related entity. These loans are underwritten in such a way as to ensure the highest probability of repayment in full, according to board-approved policies and procedures.

Multi-family Real Estate – These loans are secured by – and are generally repaid by the lease income from – real estate properties built to house 5 or more families in a single property or complex. Apartment buildings and complexes are the major collateral in this category. This category does not include 1-4 family rental properties. These loans are underwritten in such a way as to ensure the highest probability of repayment in full, according to board-approved policies and procedures.

Commercial & Industrial - Loans in this category are assigned to one of two specific subcategories:

- **Small Commercial Equipment** – Includes loans secured by commercial equipment, typically rolling stock. The primary source of repayment is generally derived from income generated by utilization of the equipment collateralizing the loans, and thus, is more subject to potential disruption relative to larger and more diversified borrowers. The lack of significant secondary sources of repayment results in a higher risk of loss and thus these loans carry market rates of interest that are higher than the Bank's other loan types. These loans possess homogeneous risk characteristics unique to small business lending to the transportation industry. These risks are mitigated via ongoing industry trend analysis and through concentration limits on the portfolio as a whole as well as within industry subclasses. The majority of these loans are originated to borrowers outside of the Bank's primary market areas of Lane and Deschutes counties, throughout the western United States.
- **Other Commercial and Industrial** – The primary source of repayment for these loans is generally cash flow from continuing business operations. These loans are underwritten according to board-approved internal policies and procedures. Under the Bank's policy, primary and secondary repayment sources must be identified upon approval and prior to funding.

Consumer – The bank engages in limited consumer lending of both a secured and unsecured nature. This primarily takes the form of home equity lines of credit and personal and professional lines of credit which may or may not be secured by tangible collateral. These loans are underwritten in such a way as to ensure the highest probability of repayment in full, according to board-approved policies and procedures.

Loans serviced for others are not included in the accompanying balance sheets. The unpaid principal balances of such serviced loans were \$27,505,000 and \$23,251,161 at December 31, 2017 and 2016, respectively.

The loan portfolio at December 31, 2017 and 2016 includes \$45,153,144 and \$40,442,382, respectively, of loans which have rates of interest that change more often than annually. The loan portfolio additionally includes at December 31, 2017 and 2016, fixed rate loans of \$59,909,731 and \$49,409,369, respectively, that are effectively converted to variable rate loans via interest rate swaps. The December 31, 2017 loan portfolio includes \$2,139,046 of loans with interest rates at their contractual floors.

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Changes in the allowance for loan losses for the year ended December 31, 2017 are as follows:

	Beginning Balance	Charge-offs	Recoveries	Provision	Ending Balance	Specific Reserve	General Allocation
Real Estate							
Acquisition, Development & Construction	\$ 209,420	\$ -	\$ -	\$ 154	\$ 209,574	\$ -	\$ 209,574
Commercial	528,814	-	-	109,010	637,824	-	637,824
Multifamily	151,807	-	-	(14,177)	137,630	-	137,630
Owner Occupied	410,933	-	-	117,316	528,249	-	528,249
Commercial and Industrial							
Small Commercial Equipment	1,326,302	(1,647,741)	39,199	1,787,531	1,505,291	24,759	1,480,532
Other Commercial & Industrial	575,863	-	-	299,279	875,142	93,320	781,822
Consumer							
Secured	147,070	-	11,860	(36,301)	122,629	-	122,629
Unsecured	26,206	-	-	3,474	29,680	7,390	22,290
Total	<u>\$ 3,376,415</u>	<u>\$ (1,647,741)</u>	<u>\$ 51,059</u>	<u>\$ 2,266,286</u>	<u>\$ 4,046,019</u>	<u>\$ 125,469</u>	<u>\$ 3,920,550</u>

Changes in the allowance for loan losses for the year ended December 31, 2016 are as follows:

	Beginning Balance	Charge-offs	Recoveries	Provision	Ending Balance	Specific Reserve	General Allocation
Real Estate							
Acquisition, Development & Construction	\$ 142,833	\$ -	\$ -	\$ 66,587	\$ 209,420	\$ -	\$ 209,420
Commercial	456,991	-	2,140	69,683	528,814	-	528,814
Multifamily	74,813	-	-	76,994	151,807	-	151,807
Owner Occupied	452,695	-	-	(41,762)	410,933	-	410,933
Commercial and Industrial							
Small Commercial Equipment	1,071,933	(816,899)	32,774	1,038,494	1,326,302	-	1,326,302
Other Commercial & Industrial	446,877	-	-	128,986	575,863	68,864	506,999
Consumer							
Secured	124,435	-	-	22,635	147,070	-	147,070
Unsecured	25,319	-	-	887	26,206	9,240	16,966
Total	<u>\$ 2,795,896</u>	<u>\$ (816,899)</u>	<u>\$ 34,914</u>	<u>\$ 1,362,504</u>	<u>\$ 3,376,415</u>	<u>\$ 78,104</u>	<u>\$ 3,298,311</u>

NOTES TO FINANCIAL STATEMENTS

Risk Rating – The monitoring process of the Bank’s loan portfolio includes periodic reviews of individual loans with a risk rating assigned to each loan. Risk ratings are assigned according to various qualitative and quantitative measurements.

- Risk ratings 1 – 6 represent increasing degrees of risk within the regulatory definition of “Pass” loans as ratings move from 1 to 6. Regulatory bodies do not draw distinctions between these categories; as such, assignment of these ratings is for internal management purposes only.
- Risk Rating 7 – loans in this category adhere to the regulatory definition of “Special Mention” loans. A Special Mention loan has potential weaknesses that deserve management’s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or in the institution’s credit position at some future date. Special Mention loans are not adversely classified and do not expose the institution to sufficient risk to warrant adverse classification.
- Risk Rating 8 – loans in this category adhere to the regulatory definition of “Substandard.” Loans classified Substandard are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the borrower’s debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.
- Risk Rating 9 – loans in this category adhere to the regulatory definition of “Doubtful.” Loans classified Doubtful have all of the weaknesses inherent in those classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable.
- Risk Rating 10 – loans in this category adhere to the regulatory definition of “Loss.” Loans classified Loss are uncollectible and of such little value that their continuance as a bankable asset is not warranted. When identified, these loans are charged off.

Loans risk rated 8, 9 or 10 are reviewed regularly to assess the ability of the borrowers to service all interest and principal obligations and, as a result, the risk ratings may be adjusted accordingly. In the event that full collection of principal and interest is not reasonably assured, the loan is appropriately downgraded and if warranted, placed on non-accrual status even though the loan may be current as to principal and interest payments. Additionally, an assessment is made as to whether an impairment of a loan warrants specific reserves or a write down of the loan.

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The following tables present the Bank's loan portfolio by loan type and credit quality indicator as of December 31, 2017 and 2016:

As of December 31, 2017					
Loan Grade					
	Pass (Ratings 1-6)	Special Mention (Rating 7)	Substandard (Rating 8)	Doubtful (Rating 9)	Totals
Real Estate					
Acquisition, Development & Construction	\$ 13,778,058	\$ -	\$ -	\$ -	\$ 13,778,058
Commercial	76,500,486	610,149	-	-	77,110,635
Multifamily	13,294,047	-	-	-	13,294,047
Owner Occupied	69,379,678	2,103,006	-	-	71,482,684
Commercial and Industrial					
Small Commercial Equipment	35,812,280	294,114	87,265	78,044	36,271,703
Other Commercial & Industrial	47,521,676	2,212,638	1,077,048	-	50,811,362
Consumer					
Secured	15,925,970	-	197,709	-	16,123,679
Unsecured	2,563,195	-	-	-	2,563,195
Total	<u>\$ 274,775,390</u>	<u>\$ 5,219,907</u>	<u>\$ 1,362,022</u>	<u>\$ 78,044</u>	<u>\$ 281,435,363</u>
Percentage of Total Portfolio	97.64%	1.85%	0.48%	0.03%	100.00%

As of December 31, 2016					
Loan Grade					
	Pass (Ratings 1-6)	Special Mention (Rating 7)	Substandard (Rating 8)	Doubtful (Rating 9)	Totals
Real Estate					
Acquisition, Development & Construction	\$ 13,084,669	\$ -	\$ -	\$ -	\$ 13,084,669
Commercial	64,248,323	2,110,049	-	-	66,358,372
Multifamily	13,407,702	-	-	-	13,407,702
Owner Occupied	47,460,813	2,154,243	-	-	49,615,057
Commercial and Industrial					
Small Commercial Equipment	31,083,857	373,320	254,334	-	31,711,511
Other Commercial & Industrial	39,031,409	182,658	836,733	-	40,050,800
Consumer					
Secured	14,277,082	-	260,912	-	14,537,993
Unsecured	2,318,364	-	-	-	2,318,364
Total	<u>\$ 224,912,219</u>	<u>\$ 4,820,270</u>	<u>\$ 1,351,979</u>	<u>\$ -</u>	<u>\$ 231,084,468</u>
Percentage of Total Portfolio	97.32%	2.09%	0.59%	0.00%	100.00%

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The following tables present an aged analysis of past due and nonaccrual loans as of December 31, 2017 and 2016:

As of December 31, 2017

	30-59 Days Past Due Still Accruing	60-89 Days Past Due Still Accruing	Nonaccrual	Total Past Due and Nonaccrual	Total Current	Total Loans Receivable
Real Estate						
Acquisition, Development & Construction	\$ -	\$ -	\$ -	\$ -	\$ 13,778,058	\$ 13,778,058
Commercial	-	-	-	-	77,110,635	77,110,635
Multifamily	-	-	-	-	13,294,047	13,294,047
Owner Occupied	-	-	-	-	71,482,684	71,482,684
Commercial and Industrial						
Small Commercial Equipment	521,965	251,679	165,309	938,953	35,332,750	36,271,703
Other Commercial & Industrial	-	-	218,975	218,975	50,592,387	50,811,362
Consumer						
Secured	-	-	-	-	16,123,679	16,123,679
Unsecured	-	-	-	-	2,563,195	2,563,195
Total	<u>\$ 521,965</u>	<u>\$ 251,679</u>	<u>\$ 384,284</u>	<u>\$ 1,157,928</u>	<u>\$ 280,277,435</u>	<u>\$ 281,435,363</u>
Percentage of Total Portfolio	0.19%	0.09%	0.14%	0.41%	99.59%	100.00%

As of December 31, 2016

	30-59 Days Past Due Still Accruing	60-89 Days Past Due Still Accruing	Nonaccrual	Total Past Due and Nonaccrual	Total Current	Total Loans Receivable
Real Estate						
Acquisition, Development & Construction	\$ -	\$ -	\$ -	\$ -	\$ 13,084,669	\$ 13,084,669
Commercial	-	-	-	-	66,358,372	66,358,372
Multifamily	-	-	-	-	13,407,702	13,407,702
Owner Occupied	-	-	-	-	49,615,057	49,615,057
Commercial and Industrial						
Small Commercial Equipment	918,170	239,221	254,334	1,411,725	30,299,786	31,711,511
Other Commercial & Industrial	-	-	193,873	193,873	39,856,927	40,050,800
Consumer						
Secured	-	-	-	-	14,537,993	14,537,993
Unsecured	-	-	-	-	2,318,364	2,318,364
Total	<u>\$ 918,170</u>	<u>\$ 239,221</u>	<u>\$ 448,207</u>	<u>\$ 1,605,598</u>	<u>\$ 229,478,870</u>	<u>\$ 231,084,468</u>
Percentage of Total Portfolio	0.40%	0.10%	0.19%	0.69%	99.31%	100.00%

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The following is an analysis of impaired loans as of December 31, 2017:

	Impaired Loans with Allowance			Impaired Loans without Allowance		Total Impaired Loans	
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Recorded Investment	Unpaid Principal Balance
Commercial and Industrial							
Small Commercial Equipment							
Nonaccrual	\$ 83,187	\$ 82,532	\$ 24,759	\$ -	\$ -	\$ 83,187	\$ 82,532
Other	-	-	-	-	-	-	-
Other Commercial & Industrial							
Nonaccrual	219,681	218,975	73,560	-	-	219,681	218,975
Other	124,068	123,641	19,760	-	-	124,068	123,641
Subtotals	426,936	425,148	118,079	-	-	426,936	425,148
Consumer							
Secured							
Nonaccrual	-	-	-	-	-	-	-
Other	-	-	-	-	-	-	-
Unsecured							
Nonaccrual	-	-	-	-	-	-	-
Other	37,122	36,958	7,390	-	-	37,122	36,958
Subtotals	37,122	36,958	7,390	-	-	37,122	36,958
Totals	\$ 464,058	\$ 462,106	\$ 125,469	\$ -	\$ -	\$ 464,058	\$ 462,106

The following is an analysis of impaired loans as of December 31, 2016:

	Impaired Loans with Allowance			Impaired Loans without Allowance		Total Impaired Loans	
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Recorded Investment	Unpaid Principal Balance
Commercial and Industrial							
Small Commercial Equipment							
Nonaccrual	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Other	-	-	-	-	-	-	-
Other Commercial & Industrial							
Nonaccrual	194,325	193,873	48,744	-	-	194,325	193,873
Other	117,871	117,444	20,120	-	-	117,871	117,444
Subtotals	312,196	311,317	68,864	-	-	312,196	311,317
Consumer							
Secured							
Nonaccrual	-	-	-	-	-	-	-
Other	-	-	-	277,601	276,367	277,601	276,367
Unsecured							
Nonaccrual	-	-	-	-	-	-	-
Other	38,634	38,509	9,240	-	-	38,634	38,509
Subtotals	38,634	38,509	9,240	277,601	276,367	316,235	314,876
Totals	\$ 350,830	\$ 349,826	\$ 78,104	\$ 277,601	\$ 276,367	\$ 628,431	\$ 626,193

NOTES TO FINANCIAL STATEMENTS

The following tables present the average recorded investment in impaired loans and interest income recognized for the periods indicated:

Year Ended December 31, 2017			
	Average Recorded Investment		Interest Recognized on Impaired Loans
Commercial and Industrial			
Small Commercial Equipment	\$ 53,211	\$	28,123
Other Commercial & Industrial	301,436		6,521
Consumer			
Secured	235,679		16,332
Unsecured	37,863		2,268
Total	<u>\$ 628,189</u>	<u>\$</u>	<u>53,244</u>

Year Ended December 31, 2016			
	Average Recorded Investment		Interest Recognized on Impaired Loans
Commercial and Industrial			
Small Commercial Equipment	\$ 13,754	\$	-
Other Commercial & Industrial	277,819		15,118
Consumer			
Secured	262,080		18,233
Unsecured	39,230		2,356
Total	<u>\$ 592,883</u>	<u>\$</u>	<u>35,707</u>

The cash basis interest income on impaired loans was not materially different than the interest recognized on impaired loans as shown in the above tables.

The Bank reports certain loans as troubled debt restructurings (TDRs) when the Bank grants a concession(s) to a borrower experiencing financial difficulties that it would not otherwise consider. Examples of such concessions include extending the maturity date(s) or providing a lower interest rate than would normally be available for a transaction of similar risk. A TDR loan is considered to be impaired and is individually evaluated for impairment. Loans reported as TDRs accruing interest totalled \$58,777 and \$38,509 at December 31, 2017 and 2016 respectively.

The Bank modified (by extending an interest only payment period) and recorded a single loan with a principal balance of \$21,819 as a TDR during 2017 and none were modified in 2016. There were no TDR loans restructured during 2017 or 2016, nor were there any TDRs which incurred a payment default within twelve months of the restructure date during 2017 or 2016. There were no commitments to lend additional funds to borrowers whose loans have been modified and recorded as TDRs at December 31, 2017. Determination of the allowance for credit losses for TDR loans does not differ materially from the process for other impaired loans in the Bank's portfolio.

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NOTES TO FINANCIAL STATEMENTS

5. Premises and equipment:

Premises and equipment at December 31 consists of the following:

	<u>2017</u>	<u>2016</u>
Land	\$ 1,862,215	\$ 1,862,215
Buildings and improvements	3,916,033	3,828,418
Computer equipment and software	612,140	556,121
Furniture and equipment	910,083	807,047
Total	<u>7,300,471</u>	<u>7,053,801</u>
Accumulated depreciation	<u>(2,466,041)</u>	<u>(2,126,897)</u>
Property, net	<u>\$ 4,834,430</u>	<u>\$ 4,926,904</u>

The Bank owns its headquarters building and leases to others approximately 40% of the building. Rental income recorded under noncancelable leases as well as other month-to-month agreements totalled \$81,462 and \$132,272 for the years ended December 31, 2017 and 2016, respectively, and is recorded in noninterest income. At December 31, 2017, future expected rental revenues to be received under such noncancelable leases are as follows:

2018	\$ 80,684
2019	55,095
2020	16,704
2021	16,704
2022	13,920
Total	<u>\$ 183,107</u>

6. Time Deposits:

Individual time deposits that met or exceeded the FDIC standard insurance coverage limit of \$250,000 totalled \$2,964,280 and \$1,418,851 at December 31, 2017 and 2016, respectively.

At December 31, 2017, the scheduled annual maturities of time deposits is as follows:

2018	\$ 23,962,118
2019	531,883
2020	1,725,633
2021	13,000
	<u>\$ 26,232,634</u>

NOTES TO FINANCIAL STATEMENTS**7. Borrowings:**

The Bank has repurchase agreements (REPOs) of \$136,378 (average rate 0.26%) and \$1,631,664 (average rate 0.20%) at December 31, 2017 and 2016, respectively. A REPO represents an agreement between the Bank and a customer to collateralize funds deposited by the customer in an interest-bearing repurchase sweep account. Investment securities are pledged by the Bank as collateral in an amount equal to the REPOs.

The Bank has a borrowing line with the FHLB equal to a maximum of 35% of the Bank's total assets, subject to limits based on collateral consisting of FHLB stock, funds on deposit with FHLB and eligible portions of the Bank's loan and securities portfolios. The available borrowing line at December 31, 2017 is approximately \$8,700,000.

The Bank has secured and unsecured federal funds borrowing lines available with correspondent banks totalling \$11,000,000 at December 31, 2017. The Bank had no outstanding borrowings against these lines at December 31, 2017. The Bank also has a borrowing line available with the Federal Reserve Discount Window totalling approximately \$3,479,000 at December 31, 2017, which is secured by a portion of the Bank's loan portfolio. The Bank had no outstanding borrowings against this line at December 31, 2017.

8. Benefit Plans:

The Bank has a defined contribution 401(k) profit sharing plan covering substantially all employees. Employer contributions are discretionary and are determined annually by the Board of Directors. Employer contributions were \$143,313 and \$137,811 in 2017 and 2016, respectively.

The Bank has a deferred cash incentive plan for the benefit of certain key employees and a directors' deferred compensation plan for the Bank's directors. Bank contributions to these plans totalled \$69,650 and \$69,300 in 2017 and 2016, respectively. The liability for benefits under these plans totalled \$313,803 and \$218,570 as of December 31, 2017 and 2016, respectively, and is included in other liabilities in the accompanying balance sheets.

9. Stock Option and Equity Compensation Plans:

The Bank has employee and nonemployee equity compensation plans (the Plans) that reserve shares of stock for issuance to employees and directors in the form of stock options, restricted stock, or restricted stock units (RSUs). Under the Plans, the exercise price (for options) or the fair value (for restricted stock and RSUs) of awards granted must equal the market price of the Bank's stock on the date of the grant. Options granted under the Plans have a maximum term of ten years. Vesting generally occurs over periods ranging from one to three years. At December 31, 2017 and 2016, there were 225,327 and 268,485 shares of common stock available for future grants under the Plans.

NOTES TO FINANCIAL STATEMENTS

The following table presents the activity related to stock options under the Plans for the years ended December 31:

	2017		2016	
	Options Outstanding	Weighted- average exercise price	Options Outstanding	Weighted- average exercise price
Balance, beginning of year	154,929	\$ 5.26	171,009	\$4.78
Granted:				
Directors	11,250	11.33	-	-
Employees	15,356	12.63	15,000	10.33
Exercised	(67,155)	3.82	(31,080)	5.81
Balance, end of year	114,380	\$ 7.70	154,929	\$5.26
Exercisable, end of year	71,119		125,179	

The total intrinsic value of stock options exercised was \$818,822 and \$153,942 for the years ended December 31, 2017 and 2016, respectively.

The following table presents additional information regarding stock options outstanding as of December 31, 2017:

Expiration	Weighted average exercise price per share	Weighted average remaining contractual life	December 31, 2017	
			Exercisable	Outstanding
2018	\$ 3.26	0.98	\$ 2,250	\$ 2,250
2019	2.96	1.00	7,200	7,200
2020	2.75	3.00	19,692	19,692
2021	2.47	3.25	5,040	5,040
2023	4.14	5.53	10,800	10,800
2025	9.54	7.35	16,875	28,500
2026	10.33	8.49	5,000	15,000
2027	12.10	9.20	4,262	25,898
			71,119	114,380
Aggregate intrinsic value			\$731,789	\$951,027

The fair value of options granted under the Plans are estimated on the date of the grant using the Black-Scholes option pricing model. The fair value of the grants is amortized on a straight line basis over the requisite vesting periods. The expected life of options granted represents the period of time that they are expected to be outstanding. The expected life is determined based on historical experience with similar options, giving consideration to the contractual terms and vesting schedules. Expected volatility was estimated at the date of grant based on the historical volatility of the Bank's common stock. Dividends during the expected life are assumed to be zero. The risk-free interest rate is derived from the observed short term U.S. Treasury yield at the time of the grant. The Black-Scholes model used the following assumptions for the stock options granted during the years indicated:

	Expected Life (years)	Expected Volatility	Expected Dividends	Risk Free Rate
2017	10.0	14.8%	0.00%	0.89%
2016	9.0	15.7%	0.00%	0.58%

The weighted average fair value of options granted in 2017 and 2016 was \$2.74 and \$2.14, respectively. As of December 31, 2017, the total unrecognized compensation expense related to options granted amounted to \$110,408, which is expected to be recognized during 2018-2021, a weighted average period of 1.5 years

NOTES TO FINANCIAL STATEMENTS

The fair value of restricted stock and RSUs awarded under the Plans is measured based on the number of shares granted and the market price of the Bank's common stock on the date of grant. This amount is recognized as an expense over the corresponding requisite service period. As of December 31, 2017, the total unrecognized compensation expense related to restricted stock awards granted amounted to \$195,920, which is expected to be recognized during 2018-2020. Weighted average years to vest for outstanding restricted stock grants as of December 31, 2017 is 0.6 years.

The following presents the Bank's restricted stock and RSU activity for the years ended December 31, 2017 and 2016:

	Number of Shares	Weighted Average Grant Date Fair Value
Unvested as of December 31, 2015	7,500	\$ 10.13
Granted	10,515	10.20
Vested	(8,441)	10.13
Forfeited	-	-
Unvested as of December 31, 2016	9,574	10.21
Granted	16,552	11.63
Vested	(8,992)	10.50
Forfeited	-	-
Unvested as of December 31, 2017	17,134	\$ 11.43

There were a total of 43,158 shares of restricted stock and options granted during 2017 of which 6,271 vested in 2017 and 36,887 are expected to vest during 2018-2021. There were 13,095 and 29,725 options that vested during the years ended December 31, 2017 and 2016 with a total fair value of \$32,238 and \$37,671, respectively. There were 8,992 and 8,441 shares of restricted stock that vested during years ended December 31, 2017 and 2016 with a total fair value of \$94,445 and \$79,865, respectively.

Weighted average shares outstanding at December 31 are as follows:

	2017	2016
Basic	3,923,063	3,521,549
Common stock equivalents attributable to stock based grants outstanding	41,043	67,613
Fully Diluted	3,964,106	3,589,162

10. Other Expense:

Other expense for the years ended December 31 is comprised of the following:

	2017	2016
Professional services	\$ 300,736	\$ 142,565
Advertising, marketing and public relations	298,032	191,634
Printing, supplies and postage	170,764	131,996
Regulatory assessments	170,372	177,824
Loan expenses and collection	144,306	105,194
Communications	113,376	92,938
Correspondent bank fees	45,702	54,552
Other operating expenses	214,844	193,707
Total other expense	\$ 1,458,132	\$ 1,090,410

NOTES TO FINANCIAL STATEMENTS
11. Income Taxes:

On December 22, 2017, the U.S. government enacted the *Tax Cuts and Jobs Act* (the Tax Act), which introduced significant changes to U.S. income tax law. The Tax Act, among other things lowered the U.S. corporate income tax rate from 35.0% to 21.0% effective January 1, 2018. The reduction of the corporate tax rate required the Bank to remeasure its deferred tax assets and liabilities based upon the lower federal tax rate of 21.0%. As a result, during the year ended December 31, 2017, the Bank recorded a one-time income tax expense of approximately \$411,000 in conjunction with writing down its net deferred tax assets.

The income tax provision consists of the following for the years ended December 31, 2017 and 2016:

	2017	2016
Current		
Federal	\$ 2,109,821	\$ 1,353,414
State	372,699	394,198
Deferred	155,772	(3,000)
Total income tax provision	<u>\$ 2,638,292</u>	<u>\$ 1,744,612</u>

The income tax provision results in effective tax rates that are different than the federal income tax statutory rate. The nature of the differences for the years ended December 31, 2017 and 2016 are as follows:

	2017	2016
Expected federal income tax provision at statutory rates	\$ 2,013,326	\$ 1,564,004
State taxes	297,262	230,737
Permanent differences	(97,940)	(37,553)
Net impact of the Tax Act	410,991	-
Other	14,653	(12,576)
Total income tax provision	<u>\$ 2,638,292</u>	<u>\$ 1,744,612</u>

The tax effects of temporary differences that give rise to deferred tax assets and liabilities as of December 31, 2017 and 2016 are as follows:

	2017	2016
Deferred tax assets:		
Allowance for loan losses	\$ 833,495	\$ 1,081,843
Accrued vacation	15,117	9,754
Reposessed assets	66,187	66,997
Deferred compensation	84,740	85,278
Share-based compensation	-	45,859
Unrealized losses on investment securities	1,852	2,736
Secondary accrued interest	23,307	3,173
Total deferred tax assets	<u>1,024,698</u>	<u>1,295,640</u>
Deferred tax liabilities:		
Depreciation	(30,933)	(64,964)
Loan origination costs	(60,276)	(98,538)
Prepaid expenses and other	(9,294)	(19,511)
Other	-	(32,660)
Total deferred tax liabilities	<u>(100,503)</u>	<u>(215,673)</u>
Total net deferred tax assets	<u>\$ 924,195</u>	<u>\$ 1,079,967</u>

NOTES TO FINANCIAL STATEMENTS

The Bank has determined that it is not required to establish a valuation allowance for the net deferred tax assets as of December 31, 2017 and 2016, as management believes it is more likely than not that the net deferred tax assets will be realized through reversals of existing taxable temporary differences and future taxable income.

The changes included in the Tax Act are broad and complex. The final transition impacts of the Tax Act may differ from those reflected in the accompanying financial statements, possibly materially, due to, among other things, changes in interpretations of the Tax Act, any legislative action to address questions that arise because of the Tax Act, and changes to accounting standards in response to the Tax Act.

12. Commitments and Contingencies:

In order to meet the financing needs of its clients, the Bank commits to extensions of credit and issues standby letters of credit. The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Commitments to extend credit are agreements to lend to a client as long as there is no violation of any conditions established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Standby letters of credit written are conditional commitments issued by the Bank to guarantee the performance of a client to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to clients.

To manage interest rate risk, the Bank enters into interest rate swaps that effectively convert fixed rate loans into variable rate instruments earning a margin over the one month or three month LIBOR rate. These fair value hedges have been structured to be perfectly effective, thus no ineffectiveness is recognized in earnings. Cash and investment securities at December 31, 2017 totalling \$4,734,240 are held by counterparties and are pledged as security for these interest rate swaps.

Financial instruments with off-balance-sheet risk at December 31 are as follows:

	2017	2016
Commitments to extend credit	\$ 73,108,563	\$ 59,173,828
Standby letters of credit	4,560,362	1,699,157
Interest rate swaps (receive variable - pay fixed, maturing 2017-2031):		
Principal amount of hedged loans	59,909,731	49,409,369
Fair value adjustment (included in other liabilities)	(75,303)	208,047
Total fair value of hedged loans	<u>\$ 59,834,428</u>	<u>\$ 49,617,416</u>

Due to the nature of its activities, the Bank is periodically subject to litigation arising in the ordinary course of business. In the opinion of management, liabilities arising from these actions, if any, will not have a material effect on the Bank's financial position, results of operations, and cash flows as of and for the year ended December 31, 2017.

NOTES TO FINANCIAL STATEMENTS

The Bank has entered into employment agreements with certain key employees, which provide for contingent payments upon a change in control of the Bank, as defined in the agreements.

13. Related Party Transactions:

In the normal course of business, the Bank has granted loans to officers and directors and to companies with which they are associated. Such loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated parties. Activity with respect to these loans during the years ended December 31 was as follows:

	2017	2016
Balance, beginning of year	\$ 4,056,272	\$ 4,930,054
Additions or renewals	5,045,337	-
Principal repayments	(855,093)	(873,782)
Balance, end of year	<u>\$ 8,246,516</u>	<u>\$ 4,056,272</u>

In addition, there were \$1,190,514 in commitments to extend credit to officers and directors, including related entities, at December 31, 2017 which are included as part of commitments in Note 12.

Deposits from officers and directors totalled \$5,810,364 and \$9,140,639 at December 31, 2017 and 2016, respectively.

14. Fair Value Measurements:

GAAP defines fair value, establishes a framework for measuring fair value, and requires certain disclosures about fair value measurements. The categories of fair value measurement prescribed by GAAP are as follows:

- Level 1: Fair value of the asset or liability is determined using unadjusted quoted prices in active markets for identical assets or liabilities.
- Level 2: Fair value of the asset or liability is determined using inputs other than quoted prices that are observable for the applicable asset or liability, either directly or indirectly, such as quoted prices for similar (as opposed to identical) assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.
- Level 3: Fair value of the asset or liability is determined using unobservable inputs that are significant to the fair value measurement and reflect management's own assumptions regarding the applicable asset or liability.

The following disclosures are made in accordance with provisions of GAAP. The use of different assumptions and estimation methods could have a significant effect on fair value amounts. Accordingly, the estimates of fair value herein are not necessarily indicative of the amounts that might be realized in a current market exchange.

NOTES TO FINANCIAL STATEMENTS

The carrying amount and estimated fair value of the Bank's financial instruments are as follows at the dates indicated:

December 31, 2017	Carrying Amount	Level I	Level II	Level III	Estimated Fair Value
Assets:					
Cash and cash equivalents	\$ 40,964,939	\$ 40,964,939	\$ -	\$ -	\$ 40,964,939
Investment securities available-for-sale	5,388,179	-	5,388,179	-	5,388,179
Hedged loans	59,834,428	-	59,834,428	-	59,834,428
Other loans, net of allowance for loan losses	216,668,415	-	220,049,589	338,589	220,388,178
Interest receivable	1,034,066	-	1,034,066	-	1,034,066
FHLB and PCBB stock	778,400	-	778,400	-	778,400
Cash surrender value of bank-owned life insurance	3,708,474	-	3,708,474	-	3,708,474
Liabilities:					
Demand and savings deposits	272,379,985	272,379,985	-	-	272,379,985
Time deposits	26,232,634	-	26,233,886	-	26,233,886
Repurchase agreements	136,378	-	136,378	-	136,378
Term borrowings	-	-	-	-	-
Interest rate swap agreements	(75,303)	-	(75,303)	-	(75,303)

December 31, 2016	Carrying Amount	Level I	Level II	Level III	Estimated Fair Value
Assets:					
Cash and cash equivalents	\$ 36,648,676	\$ 36,648,676	\$ -	\$ -	\$ 36,648,676
Investment securities available-for-sale	5,833,268	-	5,833,268	-	5,833,268
Hedged loans	49,617,416	-	49,617,416	-	49,617,416
Other loans, net of allowance for loan losses	177,350,242	-	182,240,245	272,726	182,512,971
Interest receivable	827,948	-	827,948	-	827,948
FHLB and PCBB stock	723,600	-	723,600	-	723,600
Cash surrender value of bank-owned life insurance	3,655,538	-	3,655,538	-	3,655,538
Liabilities:					
Demand and savings deposits	226,254,650	226,254,650	-	-	226,254,650
Time deposits	27,454,953	-	27,455,726	-	27,455,726
Repurchase agreements	1,631,664	-	1,631,664	-	1,631,664
Term borrowings	-	-	-	-	-
Interest rate swap agreements	208,047	-	208,047	-	208,047

The following methods were used to estimate the fair value of each class of financial instrument above:

Cash and Cash Equivalents – The fair value approximates carrying the amount.

Investment Securities Available-for-Sale – Fair value is estimated using quoted market prices for similar securities. All available-for-sale investment securities are measured at estimated fair value on a recurring basis at the dates indicated in the table above and are included within Level II.

Loans – Fair value of fixed-rate loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit characteristics and for the same remaining maturities. Variable rate loans not at contractual floors have carrying amounts that are a reasonable estimate of fair value.

Interest Receivable – Fair value approximates the carrying amount.

FHLB and PCBB stock – Fair value approximates the carrying amount.

Cash Surrender Value of Bank-owned Life Insurance – Fair value approximates the carrying amount.

NOTES TO FINANCIAL STATEMENTS

Deposits – Fair value of demand, interest-bearing demand and savings deposits is the amount payable on demand at the reporting date. Fair value of time deposits is estimated by discounting the future cash flows using the interest rates currently offered for deposits of similar remaining maturities. The estimated fair values of deposits do not take into account the benefit that results from the low-cost funding such deposits provide.

Repurchase Agreements – The carrying amount is a reasonable estimate of fair value because of the short-term nature of these borrowings.

Interest Rate Swap Agreements – Fair value of interest rate swap agreements is estimated based upon quoted prices for similar instruments in the over the counter swaps market. All interest rate swap agreements and hedged loans are measured at estimated fair value on a recurring basis at the dates indicated in the table above and are included within Level II.

Off-balance Sheet Financial Instruments – The majority of the Bank's commitments to extend credit have variable rates and are cancellable if the client's credit quality deteriorates. Therefore, the associated fair values are not significant and are not included in the tables above.

The following tables present assets that are measured at estimated fair value on a nonrecurring basis at the dates indicated:

		Estimated fair value measurements using		
	Total estimated fair value	Level I	Level II	Level III
December 31 2017				
Reposessed assets	\$ 1,031,060	\$ -	\$ -	\$ 1,031,060
Impaired loans	\$ 338,589	\$ -	\$ -	\$ 338,589
December 31, 2016				
Reposessed assets	\$ 1,016,304	\$ -	\$ -	\$ 1,016,304
Impaired loans	\$ 272,726	\$ -	\$ -	\$ 272,726
	Valuation technique	Significant unobservable inputs		
Reposessed assets	Market approach	Appraised value of collateral less selling costs		
Impaired loans	Market and income approach	Discounted cash flows or appraised value of collateral less selling costs		

The Bank considers third party appraisals in determining the fair value of reposessed assets. Appraisals are adjusted by the Bank in consideration of economic and market conditions that could impact the value of the assets.

The fair values presented above represent management's best estimates based on a range of methodologies and assumptions. Where appropriate, expected cash flows are discounted using an applicable rate considering the time of collection, credit risk, and the discount for the uncertainty of the flows.

There were no transfers to or from Level III during 2017 or 2016.

15. Regulatory Matters:

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum ratios (set forth in the following table below) of Total Tier 1 and Common Equity Tier I capital to risk-weighted assets, and of Tier I capital to leverage assets, all as defined in the regulations. As of December 31, 2017, the most recent notification from the FDIC categorized the Bank as “Well Capitalized” as defined by regulations. To be categorized as “Well Capitalized”, the Bank must maintain minimum Total risk-based, Tier I and Common Equity Tier 1 risk-based, and Tier I leverage ratios as set forth in the table below. There are no conditions or events since that notification that management believes have changed the Bank’s category.

The Bank’s actual capital amounts (in thousands) and ratios are as follows at the dates indicated:

	Actual		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2017						
Total capital (to risk-weighted assets)	\$ 38,254	12.90%	\$ 23,724	8.00%	\$ 29,655	10.00%
Tier I capital (to risk-weighted assets)	\$ 34,542	11.65%	\$ 17,793	6.00%	\$ 23,724	8.00%
Common Equity Tier I (to risk-weighted assets)	\$ 34,542	11.65%	\$ 13,345	4.50%	\$ 19,276	6.50%
Tier I capital (to leverage assets)	\$ 34,542	10.15%	\$ 13,616	4.00%	\$ 17,020	5.00%
December 31, 2016						
Total capital (to risk-weighted assets)	\$ 27,948	11.47%	\$ 19,485	8.00%	\$ 24,357	10.00%
Tier I capital (to risk-weighted assets)	\$ 24,899	10.22%	\$ 14,614	6.00%	\$ 19,485	8.00%
Common Equity Tier I (to risk-weighted assets)	\$ 24,899	10.22%	\$ 10,961	4.50%	\$ 15,832	6.50%
Tier I capital (to leverage assets)	\$ 24,899	9.34%	\$ 10,666	4.00%	\$ 13,332	5.00%

The Federal Deposit Insurance Corporation has not reviewed these financial statements for accuracy or relevance.

BOARD OF DIRECTORS



RICHARD M. ABRAHAM, MD

Dr. Abraham has been a practicing Emergency and Occupational Medicine physician with Cascade Medical Associates since 1979. He is also managing partner of Eugene/Thurston/Junction City/Roseburg/Veneta Urgent Care walk-in clinics and the medical director of Cascade Health Solutions Occupational Medicine Program. He is a founding Director of the Bank and also serves on the boards of Cascade Health Solutions and McKenzie Willamette Medical Center. He has previously served on the boards of MWMC Foundation, PacificSource, the Safety and Health Institute, and the Marist Foundation. Director since 2003.



PATRICIA O. BUEHLER, MD

Dr. Buehler joined Summit Bank Board of Directors in 2016. She is a surgeon specializing in cataract and Lasik surgery and an owner of two small businesses. Dr. Buehler is a managing partner of InFocus Eye Care, a specialty vision correction facility in Bend with 32 employees and an owner of the Bend Surgery Center which has 120 employees. She is active at St. Charles medical center, and is on the board of directors at the Bend Surgery Center, the Bend Surgery Center foundation and Lines for Life, a suicide prevention and substance abuse prevention organization. Director since 2016.



ALAN V. EVANS

Mr. Evans is a founder and president of Evans, Elder & Brown, Inc., a commercial real estate brokerage active in sales, leasing, and development of commercial properties. He is a founding Director of the Bank and also serves as vice chair of the Arts and Business Alliance of Eugene. Director since 2003.



DANIEL P. HOBIN

Mr. Hobin has more than 20 years of experience building technology companies and currently oversees the strategic direction of G5, a company located in Bend that is a leading provider of digital marketing in the property management sector. He joined the Bank Board of Directors in 2016. Mr. Hobin is a co-founder of the Bend Venture Conference and participates on the advisory board for Oregon State University Cascades. Director since 2016.



ROSS J. KARI

Mr. Kari retired as executive vice president and chief financial officer of Freddie Mac. He currently serves as a Trustee on the University of Oregon's Board of Trustees and is a director of Goldman Sachs BDC. Ross has served as chief financial officer of Fifth Third Bank, Safeco, and Wells Fargo Bank and also as executive vice president and chief operating officer for the Federal Home Loan Bank of San Francisco. Additionally, he served as a director and chair of the audit committee for KKR Financial Holdings LLC, a publicly traded specialty finance company. Director since 2015.



STEVEN J. KORTH

Mr. Korth is the director of real estate and development for his family business, McKay Investment Company. He has been a Director of the Bank since 2008 and has served on the boards of the Eugene Chamber of Commerce, Lane Metro Partnership, and the Oregon Community Foundation. He is also active in local government, having served on the Mayor of Eugene's Economic Development Committee, the Eugene Enterprise Zone Committee, and as a member of the Eugene School Districts "Shaping 4-J's Future" task force. Director since 2008.



ANN MARIE MEHLUM

Ms. Mehlum is the founding President & Chief Executive Officer of Summit Bank. Prior to re-joining Summit's Board, she served as Associate Administrator of the US Small Business Administration, where she oversaw SBA loan guarantee programs that provided access to capital for small businesses all over the country and a portfolio that exceeded \$100 billion. She has served on the FDIC Community Bank Advisory Council, the US Treasury CDFI Advisory Board and as President of the Oregon Bankers Association. Locally, she has served on non-profit boards including the United Way of Lane County and the Eugene Area Chamber of Commerce. In 2015, she was inducted into the State of Oregon Bankers Hall of Fame for lifetime contributions to the industry. Initial Director from 2004 to 2013. Current Director since 2017.

BOARD OF DIRECTORS



J. ANDREW MOORE

Mr. Moore is co-president of Bigfoot Beverages. He has been a Director of the Bank for more than seven years and also serves on the boards of the Oregon Beverage Association, the American Beverage Association, Cascade Health Solutions, and Pepsi Northwest Beverages. He previously served on the boards of the Pepsi-Cola Bottlers Association and the Eugene Country Club. Director since 2010.



DENNIS G. OREM

Mr. Orem is the CEO of Jerry's Home Improvement Centers located in Eugene and Springfield. He is a founding Director of the Bank and has been an active participant in local, regional, and national industry trade organizations including serving on the boards of the Western Building Materials Association, the Home Center Institute, and the Eugene Chamber of Commerce. Director since 2003.



ANDY J. STORMENT

Mr. Storment is a founding director of the Bank and current Board Vice Chair. He also manages investments in commercial real estate and operating companies primarily in the Northwest. He serves on the boards of Jerry's Home Improvement Centers and The Ford Family Foundation. Director since 2003.



CRAIG A. WANICHEK

Mr. Wanichek currently serves as the Bank's President and Chief Executive Officer. Mr. Wanichek joined the Bank in 2009 holding various Executive Management positions including Chief Credit Administrator prior to succeeding the Bank's founding CEO in 2013. Mr. Wanichek previously served in several management positions with a local NYSE-traded manufacturing company following seventeen years in commercial banking. Mr. Wanichek has served as chair of the Eugene Chamber of Commerce and Cascade Health. He is currently Secretary/Treasurer and on the Board of Directors for the Oregon Bankers Association. He also serves on the board of Greater Eugene, Inc. and is currently representing the state of Oregon on the Independent Community Bankers of America Federal Delegate Board. He is a graduate of the University of Oregon with a Bachelor's degree in Economics. Director since 2013.



R. PAUL WEINHOLD

Mr. Weinhold is the President and Chief Executive Officer of the University of Oregon Foundation. He is a founding Director of the Bank and currently serves as the Board Chair. He has served in leadership roles for a variety of local non-profits. Prior to joining the University of Oregon Foundation, he spent more than twenty years in leadership roles in the commercial insurance industry. He previously served on the Board of the Oregon Urology Foundation. Director since 2003.



JOHN R. YORK, MD

Dr. York is the retired president of Women's Care Associates. He is a founding Director of the Bank. He previously served on the boards of Trillium Holdings, Agate Resources, PacificSource, Medical and Surgical Specialists, and was the OBGYN department chair for PeaceHealth. Director since 2003.

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SUMMIT BANK TEAM

EUGENE / SPRINGFIELD OFFICE

SHELLY ADAIR, EFG Account Collections
LINDA ALGER, EFG Account Manager
RACHEL ARBOGAST, Operations Specialist
MARY BARTLETT, VP and Business Client Advisor
JENNIFER BENNETT, VP Marketing and Business Development
MEGAN BROWN, HR Specialist
PIOTREK BUCIARSKI, VP and Corporate Business Development
TRACI CARLSON, Support Specialist I
CAROLYN COLE, VP and Business Client Advisor
RACHAEL CRAWFORD, Client Service Representative
MACAELA CROWLEY, Client Service Representative
VICKIE CUSSINS, Corporate Secretary and Administrative Officer
DARRYL DARE, VP and Technology Support Manager
JAYSON DAVIS, VP and Business Client Advisor
M. (MICKEY) FENTON, SPHR, HR Director
DARVIN FOWLER, VP and Business Client Advisor
RODNEY GOEBEL, Courier
SCOTT GOLDSTEIN, SVP and Corp. Cashier/Chief Financial Officer
MARYANN GONZALES, SBA Portfolio Associate
CHRIS HEMMINGS, VP Controller and Senior Operations Manager
OLIVIA HEMMINGS, Business Client Services Specialist
CASEY HILL, SVP and Chief Credit Officer
MEGAN HORVATH, Portfolio Manager
ASHLEY HORNER, VP and SBA Program Administrator
CLAYTON JIMENEZ, Associate Business Client Advisor
JAMES JOHNSON, Equipment Finance Program Manager
CHRIS KLINE, VP and Business Client Advisor

DAAN MAASLAND, Associate Business Client Advisor
MICHAELA MARCOTTE, HR Director
EMILY McGINNIS, Client Service Representative
HANS McKNIGHT, Support Specialist II
VICKI MERAY, Business Client Services Specialist
J. MICHAEL MERCER, SVP and Director MBG
KATHY METZLER, Business Client Services Specialist
LEAH MORTENSEN, Business Client Services Specialist
SUZETTE MOLINSKI, AVP and EFG Senior Account Manager
TANNER NELSON, SBA Portfolio Associate
JACK OMLIN, Support Specialist II
KRISTINA PARKER, SBA Portfolio Advisor
CHASE PEARSON, Associate Business Client Advisor
PAM PLILER, AVP Compliance/Risk Manager and BSA Officer
SEAN RUIZ, Technology Support Specialist
KIM SCOFIELD, AVP and Business Client Services Manager
KYLE SHAVERE, Associate Business Client Advisor
MARC STEINBAUGH, VP and Business Relationship Manager
CARRIE STAMOS, EFG Account Manager
ROBYN STUWE, EFG Account Support Specialist
GENEVIEVE SUMNALL, VP and Director Treasury Mgmt.
KIMBERLEE VOORHIES, Business Client Services Specialist
CRAIG WANICHEK, President and Chief Executive Officer
WILLIAM WHALEN, SVP and Chief Lending Officer
RENDAL WOLFORD, Central Ops. and eBanking Supervisor
KIMBERLY WORLEY, Senior Client Services Advisor
ANGIE ZASH, Senior Staff Accountant

CENTRAL OREGON OFFICE

RACHAEL BAKER, Associate Business Client Advisor
JOHN BOYLEN, VP and Business Client Advisor
CARLY CARMICHAEL, AVP and Business Client Advisor
MICHELLE CROSS, Associate Business Client Advisor
JILL CUMMINGS, AVP and Market Development Officer
MICHAEL HUDSON, Client Services Officer

SARAH MILLER, Client Service Representative
GARY O'CONNELL, SVP and Central Oregon Market President
MARY RAISANEN, Senior Client Services Advisor
CARLEE STILTNER, Associate Business Client Advisor
BEN WATSON, AVP and Business Client Advisor
MINDY YORK, Business Client Courier

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