

**COMMUNITY FIRST  
BANCORPORATION, INC.  
AND SUBSIDIARIES  
KENNEWICK, WA**

**AUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**AND OTHER FINANCIAL INFORMATION**

**DECEMBER 31, 2018 AND 2017**

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



## INDEPENDENT AUDITOR'S REPORT

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The Board of Directors and Shareholders  
of Community First Bancorporation, Inc.  
Kennewick, WA

We have audited the accompanying consolidated financial statements of Community First Bancorporation, Inc. and Subsidiaries, which comprise the balance sheets as of December 31, 2018 and 2017 and the related statements of income, comprehensive income, changes in shareholders' equity and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with the 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor's Responsibility**

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

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

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

### **Opinion**

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Community First Bancorporation, Inc. and Subsidiaries as of December 31, 2018 and 2017 and the results of their operations and their cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

## Other Matters

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The other financial information on pages 46-52 is presented for the purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the other financial information is fairly stated in all material respects in relation to the financial statements taken as a whole.

*Stovall, Grandey & Allen, LLP*

STOVALL, GRANDEY & ALLEN, L.L.P.  
Fort Worth, Texas  
March 25, 2019

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**  
**DECEMBER 31, 2018 AND 2017**  
(Dollars in Thousands)

	<b>2018</b>	<b>2017</b>
<b>ASSETS</b>		
Cash and cash equivalents:		
Cash and due from banks - Note 3	\$ 6,635	\$ 9,230
Interest-bearing deposits in financial institutions maturing in less than three months	34,995	30,748
Total cash and cash equivalents	41,630	39,978
Interest-bearing deposits in financial institutions maturing in more than three months	984	5,168
Investment securities - Note 4	71,280	70,332
Federal Home Loan Bank stock, at cost - Note 2	366	348
Loans held-for-sale - Note 5	1,176	-
Loans, net of deferred loan fees and allowance for loan losses - Note 5	190,156	172,482
Premises and equipment, net of accumulated depreciation - Note 6	6,918	5,637
Bank-owned life insurance	6,410	6,238
Goodwill - Note 7	2,473	2,473
Accrued interest receivable	1,104	964
Other assets	1,747	1,450
<b>Total Assets</b>	<b>\$ 324,244</b>	<b>\$ 305,070</b>
 <b>LIABILITIES</b>		
Deposits - Note 8	\$ 290,759	\$ 273,417
Other liabilities:		
Accrued interest payable	27	20
Accrued expenses and other liabilities	300	364
Total other liabilities	327	384
<b>Total Liabilities</b>	<b>291,086</b>	<b>273,801</b>
 Commitments and contingencies - Notes 6, 11, 12, 13, 14 and 15		
 <b>SHAREHOLDERS' EQUITY</b>		
Common stock, \$1 par value:		
Authorized - 1,000,000 shares		
Issued and outstanding - 521,247 and 509,266 shares at December 31, 2018 and 2017, respectively	521	509
Additional paid-in capital	14,850	14,245
Retained earnings	18,418	16,479
Accumulated other comprehensive income (loss)	(631)	36
<b>Total Shareholders' Equity</b>	33,158	31,269
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 324,244</b>	<b>\$ 305,070</b>

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

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**  
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**  
(Dollars in Thousands, except for per share amounts)

	<b>2018</b>	<b>2017</b>
<b>Interest income</b>		
Interest and fees on loans	\$ 8,856	\$ 7,967
Interest on investment securities	1,538	1,349
Interest on federal funds sold and interest-bearing deposits with financial institutions	410	287
Total interest income	10,804	9,603
<b>Interest expense</b>		
On deposits	455	354
On borrowed funds	22	10
Total interest expense	477	364
Net interest income	10,327	9,239
Provision for loan losses - Note 5	203	80
Net interest income after provision for loan losses	10,124	9,159
<b>Non-interest income</b>		
Service charges and fees on deposit accounts	309	295
Mortgage broker fees	14	8
Earnings on bank-owned life insurance	172	176
Gain on sales of investment securities (includes \$33,000 and \$32,000 of accumulated other comprehensive income reclassifications for 2018 and 2017, respectively, for unrealized gains on available-for-sale securities)	19	37
Net gain on sales of loans	630	58
Net loss on sales of premises and equipment	-	(2)
Income from fiduciary activities	3,771	3,345
Other	997	502
Total non-interest income	5,912	4,419
<b>Non-interest expense</b>		
Salaries and employee benefits	8,477	6,581
Occupancy	703	581
Furniture and equipment	461	343
Data processing	438	530
Professional fees	343	338
Other operating expenses	2,127	1,516
Total non-interest expense	12,549	9,889
<b>Net Income</b>	\$ 3,487	\$ 3,689
<b>Basic earnings per share of common stock</b>	\$ 6.74	\$ 7.27
<b>Average shares of common stock outstanding</b>	517,596	507,278

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

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**  
**(Dollars in Thousands)**

	<b>2018</b>	<b>2017</b>
<b>Net Income</b>	\$ 3,487	\$ 3,689
<b>Other Comprehensive Loss</b>		
Securities available-for-sale:		
Reclassification adjustment for net realized gains on sales during the year	(33)	(32)
Change in net unrealized gains/losses during the year	(634)	25
Other comprehensive loss	(667)	(7)
<b>Comprehensive Income</b>	\$ 2,820	\$ 3,682

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

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**  
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**  
(Dollars in Thousands)

	<u>Common Stock</u>	<u>Additional Paid-In Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Total</u>
<b>Balance at January 1, 2017</b>	\$ 503	\$ 13,873	\$ 14,310	\$ 43	\$ 28,729
Sale of stock	3	222			225
Exercise of stock options	2	96			98
Restricted stock compensation expense		1			1
Directors stock compensation expense	1	53			54
Comprehensive income (loss) for the year ended December 31, 2017			3,689	(7)	3,682
Dividends paid - \$3.00 per share			<u>(1,520)</u>		<u>(1,520)</u>
<b>Balance at December 31, 2017</b>	509	14,245	16,479	36	31,269
Sale of stock	5	384			389
Purchase of stock	(3)	(191)			(194)
Stock option expense		1			1
Exercise of stock options	5	260			265
Restricted stock compensation expense	4	86			90
Directors stock compensation expense	1	65			66
Comprehensive income (loss) for the year ended December 31, 2018			3,487	(667)	2,820
Dividends paid - \$3.00 per share			<u>(1,548)</u>		<u>(1,548)</u>
<b>Balance at December 31, 2018</b>	<u>\$ 521</u>	<u>\$ 14,850</u>	<u>\$ 18,418</u>	<u>\$ (631)</u>	<u>\$ 33,158</u>

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



**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**  
(Dollars in Thousands)

	<b>2018</b>	<b>2017</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$ 3,487	\$ 3,689
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	558	409
Provision for loan losses	203	80
Net amortization on investment securities	704	558
Stock option compensation expense	1	-
Restricted stock compensation expense	90	1
Directors stock compensation expense	66	54
Earnings on bank-owned life insurance	(172)	(176)
Originations of loans held-for-sale	(34,310)	(3,492)
Proceeds from sales of loans held-for-sale	33,764	3,942
Net gain on sales of loans	(630)	(58)
Gain on sales of investment securities	(19)	(37)
Net loss on sales of premises and equipment	-	2
Increase in net deferred loan fees	113	54
Increase in accrued interest receivable	(140)	(146)
Increase (decrease) in accrued interest payable	7	(7)
Other	(447)	(274)
Total adjustments	(212)	910
<b>Net Cash Provided by Operating Activities</b>	<b>3,275</b>	<b>4,599</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Decrease in interest-bearing deposits in financial institutions maturing in more than three months	4,184	3,561
Purchases of investment securities:		
Available-for-sale	(17,907)	(12,862)
Proceeds from maturities and calls of investment securities:		
Available-for-sale	11,135	9,365
Proceeds from principal paydowns on investment securities:		
Available-for-sale	2,500	3,028
Proceeds from sales of investment securities:		
Available-for-sale	1,973	2,642
Purchases of FHLB stock	(1,817)	(68)
Proceeds from redemptions of FHLB stock	1,799	63
Net increase in loans made to customers	(17,990)	(18,418)
Proceeds from sales of premises and equipment	-	1
Purchases of premises and equipment	(1,753)	(3,128)
<b>Net Cash Used by Investing Activities</b>	<b>\$ (17,876)</b>	<b>\$ (15,816)</b>

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

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS, Continued**  
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**  
(Dollars in Thousands)

	<b>2018</b>	<b>2017</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net increase in demand deposits, interest-bearing transaction accounts and savings	\$ 17,103	\$ 15,203
Net increase (decrease) in time deposits	238	(2,449)
Repayment of FHLB borrowings	-	(500)
Proceeds from sales of common stock	389	225
Proceeds from stock options exercised	265	98
Purchase of common stock	(194)	-
Dividends paid	(1,548)	(1,520)
<b>Net Cash Provided by Financing Activities</b>	<b>16,253</b>	<b>11,057</b>
<b>Net increase (decrease) in cash and cash equivalents</b>	1,652	(160)
<b>Cash and cash equivalents at beginning of year</b>	39,978	40,138
<b>Cash and cash equivalents at end of year</b>	\$ 41,630	\$ 39,978
 <b>SUPPLEMENTAL SCHEDULE OF OPERATING AND INVESTING ACTIVITIES:</b>		
Interest paid	\$ 470	\$ 371

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 1      History**

Community First Bancorporation, Inc. was formed August 6, 2004 to serve as a bank holding company. The Corporation was activated January 1, 2005, when Community First Bancorporation, Inc. and Community First Bank entered into a Share Exchange Agreement in order to effect the acquisition of 100 percent of the issued and outstanding common stock of the Bank. Each eligible Bank Shareholder received one share of Corporation stock in exchange for each share of Bank stock owned.

In order to effect a conversion to a Subchapter S corporation, there was a 1-for-1,000 reverse stock split in 2005. During 2005, Community First Merger Corporation, Inc. was formed in order to effectuate the Subchapter S conversion. Effective January 1, 2006, Community First Bancorporation, Inc. and Community First Merger Corporation, Inc., a Subchapter S corporation, merged. After this merger, a 1,000-for-1 stock split occurred, which restored the number of shares to the original amounts prior to the reverse stock split.

Effective January 1, 2016, HFG Trust, LLC, a wholly owned subsidiary of the Bank was established. At this same time, HFG Holdings, LLC, a newly established merger subsidiary of the Corporation, and Haberling Financial Group, Inc. merged. After the merger, HFG Holdings, LLC was merged into HFG Trust, LLC. Pursuant to the merger agreement, 41,600 shares of common stock in the Corporation were issued to shareholders of Haberling Financial Group, Inc. Haberling Financial Group, Inc. was principally owned by a director of the Corporation. Refer to Note 10 for additional information.

**Note 2      Summary of Significant Accounting Policies**

The consolidated financial statements of the Corporation include its accounts and those of its one hundred percent (100%) owned subsidiary, Community First Bank (“Bank”) and the Bank’s one hundred percent (100%) owned subsidiary, HFG Trust, LLC (“HFG”). The accounting and reporting policies of all three entities are in accordance with accounting principles generally accepted in the United States of America. All dollar amounts, except per share information, are stated in thousands.

Principles of Consolidation

In the consolidated financial statements, all significant intercompany accounts and transactions have been eliminated upon consolidation.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 2      Summary of Significant Accounting Policies, continued**

Nature of Operations

Community First Bancorporation, Inc. is a bank holding company whose principal activity is the ownership and management of its wholly-owned subsidiary, Community First Bank. Community First Bank operates five offices in Kennewick, Connell, Pasco and Richland, Washington. Community First Bank provides loan services to and accepts deposits from customers, who are predominately small- and middle-market businesses and middle-income individuals, in Southeastern Washington State. Funding sources are deposits from customers, public entities and borrowings from various sources. The Bank operates under a state bank charter and provides full banking services. The Bank is subject to regulation by the Washington State Department of Financial Institutions and the Federal Deposit Insurance Corporation. HFG Trust, LLC is a wholly-owned subsidiary of the Bank and provides financial management and trust services to a variety of customers at its office in Kennewick, Washington. At December 31, 2018 and 2017, HFG Trust, LLC had assets under management for its customers totaling \$627,610,000 and \$540,241,000, respectively.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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 determination of the adequacy of the allowance for loan losses is based on estimates that are particularly susceptible to significant changes in the economic environment and market conditions. In connection with the determination of the estimated losses on loans, management obtains independent appraisals for significant collateral.

The Corporation's loans are generally secured by specific items of collateral including real property, consumer assets and business assets. Although the Corporation has a diversified loan portfolio, a substantial portion of its debtors' ability to honor their contracts is dependent on local economic conditions.

While management uses available information to recognize losses on loans, further reductions in the carrying amounts of loans may be necessary based on changes in local economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the estimated losses on loans. Such agencies may require the Corporation to recognize additional losses based on their judgments about information available to them at the time of their examination. Because of these factors, it is reasonably possible that the estimated losses on loans may change materially in the near term. However, the amount of the change that is reasonably possible cannot be estimated.

Cash and Cash Equivalents and Cash Flows

For the purpose of presentation in the Statements of Cash Flows, cash and cash equivalents are defined as those amounts included in cash and amounts due from depository institutions, interest-bearing deposits maturing in three months or less and federal funds sold. The Corporation reports net cash flows from customer loan transactions, deposit transactions and short-term borrowings.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 2**      **Summary of Significant Accounting Policies, continued**

Investment Securities

The Corporation accounts for investment securities according to authoritative guidance issued by the Financial Accounting Standards Board (FASB). Under the provisions of the FASB authoritative guidance, debt securities that management has the ability and intent to hold to maturity are classified as held-to-maturity and carried at amortized cost. The amortization of premiums and accretion of discounts are recognized in interest income using methods approximating the interest method over the period to maturity.

Debt securities not classified as held-to-maturity are classified as available-for-sale. Securities available-for-sale are carried at fair value with unrealized gains and losses reported in other comprehensive income (loss). Realized gains (losses) on securities available-for-sale are included in other income and, when applicable, are reported as a reclassification adjustment in other comprehensive income (loss). Gains and losses on sales of securities are determined on the specific-identification method.

Declines in the fair value of individual held-to-maturity and available-for-sale securities below their amortized cost that are other than temporary result in writedowns of the individual securities to their fair value. The related writedowns are included in earnings as realized losses. In estimating other than temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer and (3) the intent and ability of the Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Federal Home Loan Bank Stock

At December 31, 2018 and 2017, the Corporation had \$366,000 and \$348,000, respectively, recorded for stock in the Federal Home Loan Bank (FHLB). As a member of the FHLB system, the Corporation is required to maintain an investment in capital stock of the FHLB in an amount equal to the greater of .5% of its outstanding mortgage related assets or 4.5% of advances from the FHLB. The recorded amount of FHLB stock equals its fair value because the shares can only be redeemed by the FHLB at the \$100 per share par value. This stock is classified as a restricted investment security, carried at cost and evaluated annually for impairment. During 2018 and 2017, no impairment loss was recorded.

Loans Held-for-Sale

Mortgage loans originated for sale in the foreseeable future in the secondary market are carried at the lower of aggregate cost or estimated market value. Gains and losses on sales of loans are recognized at the settlement date and are determined by the difference between the sales proceeds and the carrying value of the loans. Sales are made without recourse. Net unrealized losses, if any, are recognized through a valuation allowance established by charges to income.

The Corporation issues various representations and warranties associated with the sale of loans. During 2018 and 2017, there were no losses incurred regarding these representations and warranties.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 2      Summary of Significant Accounting Policies, continued**

Loans

Loans are stated at the principal amount outstanding less net deferred loan fees and the allowance for loan losses. Interest income on loans is recognized based upon the principal amounts outstanding. Generally the accrual of interest on loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due or when they are past due 90 days as to either principal or interest, unless they are well secured and in the process of collection. When interest accrual is discontinued, all unpaid accrued interest is reversed against current income. If management determines that the ultimate collectability of principal is in doubt, cash receipts on nonaccrual loans are applied to reduce the principal balance on a cash-basis method, until the loans qualify for return to accrual status or principal is paid in full. Loans are returned to accrual status when all principal and interest amounts contractually due are brought current and future payments are reasonably assured. Past due status is determined based on contractual terms.

Loan Origination Fees and Costs

Loan origination fees and costs are deferred and amortized into income as an adjustment to yield over the life of the related loan.

Allowance for Loan Losses

The allowance for loan losses is comprised of amounts charged against income in the form of the provision for loan losses, less charged-off loans, net of recoveries. Loans are charged against the allowance for loan losses when management believes that collection of the principal is unlikely. Subsequent recoveries, if any, are credited to the allowance for loan losses.

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

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as doubtful, substandard or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

A loan is considered impaired when, based on current information and events, it is probable that the Corporation will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 2      Summary of Significant Accounting Policies, continued**

Allowance for Loan Losses, continued

scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price or the fair value of the collateral if the loan is collateral dependent. Large groups of smaller balance homogenous loans are collectively evaluated for impairment; accordingly, the Corporation does not separately identify individual consumer and residential loans for impairment disclosures, unless such loans are subject to a restructuring agreement.

Periodically, regulatory agencies review the Corporation's allowance for loan losses as an integral part of their examination process, and may require the Corporation to make additions to the allowance based on their judgment about information available to them at the time of their examination.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Depreciation expense is computed using the straight-line method based upon the estimated useful lives of the assets, which range from 3 to 7 years for furniture and equipment, and 30 to 40 years for buildings and improvements. Leasehold improvements are amortized over the term of the lease or the estimated useful life of the improvement, whichever is less.

Maintenance and repairs are charged to operating expenses. Renewals and betterments are added to the asset accounts and depreciated over the periods benefited. Depreciable assets sold or retired are removed from the asset and related accumulated depreciation accounts and any gain or loss is reflected in the income and expense accounts. These assets are reviewed for impairment when events indicate their carrying value may not be recoverable. If management determines that an impairment exists, the asset is reduced with an offsetting charge to expense.

Other Real Estate Owned

Other real estate owned is foreclosed property held pending disposition and is initially recorded at fair value less estimated selling costs when acquired, establishing a new cost basis. At foreclosure, if the fair value of the real estate acquired less estimated selling costs is less than the Corporation's recorded investment in the related loan, a writedown is recognized through a charge to the allowance for loan losses. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. Valuations are periodically performed by management, and any subsequent writedowns are recorded as a charge to income, if necessary, to reduce the carrying value of the property to its fair value less estimated selling costs. Sales of other real estate owned are accounted for according to authoritative guidance issued by the FASB.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 2**     **Summary of Significant Accounting Policies, continued**

Goodwill

As a result of the HFG acquisition which is discussed in Note 1, goodwill was recorded by the Corporation. Goodwill represents the excess of the purchase price over the fair value of net assets acquired in business combinations under the purchase method of accounting. The Corporation has adopted authoritative guidance issued by the FASB. Under this guidance, goodwill is periodically assessed for impairment when events or circumstances indicate that the carrying value of the asset may not be recoverable. The Corporation bases its evaluation on such impairment factors as the nature of the assets, the future economic benefit of the assets, any historical or future profitability measurements, as well as other external market conditions or factors that may be present. Refer to Note 7 for additional information.

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 Corporation, (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 Corporation does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Reserve for Unfunded Commitments

The Corporation has established a reserve for possible losses associated with commitments to lend funds under existing agreements. Management determines the adequacy of the reserve for unfunded commitments by evaluating the outstanding commitment levels, the expected conversion to loans, historical loss estimates and other relevant factors. This evaluation is inherently subjective and actual losses may vary from current estimates. Changes in the reserve are reported in earnings in the periods they become known. The reserve for unfunded commitments is included in accrued expenses and other liabilities in the accompanying consolidated balance sheets. At December 31, 2018 and 2017, this reserve totaled \$50,000.

Federal Income Taxes

Effective January 1, 2006, the shareholders of the Corporation elected to be taxed as a Subchapter "S" Corporation under Internal Revenue Service Code Section 1362. In lieu of corporate income taxes, the shareholders of a Subchapter S Corporation are taxed on their proportionate share of the Corporation's taxable income.

The Corporation, the Bank and HFG join in filing federal income tax returns.

The Companies maintain their records for financial reporting on the accrual basis of accounting. The Companies maintain their records for income tax reporting on the cash basis of accounting.



**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**Note 2**      **Summary of Significant Accounting Policies, continued**

Federal Income Taxes, continued

In accordance with authoritative guidance issued by the FASB, the Corporation performed an evaluation to determine if there were any uncertain tax positions that would have an impact on the consolidated financial statements. No uncertain tax positions were identified. The December 31, 2015 through December 31, 2018 tax years remain subject to examination by the Internal Revenue Service. The Corporation does not believe that any reasonably possible changes will occur within the next 12 months which will have a material impact on the consolidated financial statements. The Corporation records incurred penalties and interest in other non-interest expense. There were no penalties and interest assessed by taxing authorities during 2018 or 2017.

Stock-Based Compensation

The Corporation has stock-based employee and director compensation plans which are more fully described in Note 16. The Corporation has adopted authoritative guidance issued by the FASB regarding accounting for stock compensation expense. As a result of adopting the FASB authoritative guidance, the Corporation's net income is \$157,000 and \$55,000 lower for the years ended December 31, 2018 and 2017, respectively.

Comprehensive Income

The Corporation has adopted authoritative guidance issued by the FASB. The FASB authoritative guidance establishes standards for reporting and display of comprehensive income and its components. The Corporation reports comprehensive income in the statement of comprehensive income.

Advertising Costs

Advertising costs are expensed as incurred. Advertising costs in the amount of \$67,000 and \$58,000 were expensed during 2018 and 2017, respectively.

Fair Values of Financial Instruments

Authoritative guidance issued by the FASB requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instruments. The FASB authoritative guidance excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Corporation.

The following methods and assumptions were used by the Corporation in estimating its fair value disclosures for financial instruments:

**Cash and Due From Banks:** The carrying amounts reported in the balance sheet for cash and due from banks approximate those assets' fair values.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**Note 2 Summary of Significant Accounting Policies, continued**

Fair Values of Financial Instruments, continued

**Interest-Bearing Deposits:** Fair values for interest-bearing deposits are estimated using a discounted cash flow analysis that applies interest rates currently being offered on similar deposits to a schedule of aggregated contractual maturities on such deposits.

**Investment Securities:** Fair values for investment securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

**Federal Home Loan Bank Stock:** The carrying amount reported in the balance sheet for FHLB stock approximates its fair value.

**Loans Held-for-Sale:** Fair values for loans held-for-sale are based on their estimated market price.

**Loans:** For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying amounts. The fair values for other loans (for example, fixed rate commercial real estate and rental property mortgage loans and commercial and industrial loans) are estimated using discounted cash flow analysis, based on interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Loan fair value estimates include judgments regarding future expected loss experience and risk characteristics. Fair values for impaired loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable. The carrying amount of accrued interest receivable approximates its fair value.

**Bank-Owned Life Insurance:** The carrying amount reported in the balance sheet for bank-owned life insurance approximates its fair value.

**Deposits:** The fair values disclosed for demand deposits (for example, interest-bearing checking accounts and savings accounts) are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). The fair values for time deposits are estimated using a discounted cash flow calculation that applies interest rates currently being offered on time deposits to a schedule of aggregated contractual maturities on such time deposits. The carrying amount of accrued interest payable approximates its fair value.

**FHLB Advances:** The fair values of FHLB advances are estimated using discounted cash flow analyses based on the current incremental borrowing rates for similar types of borrowing arrangements.

Book Value and Tangible Book Value per Share

Book value per share is calculated by dividing the total shareholders' equity shown on the consolidated balance sheets by the number of shares outstanding as of year-end. Tangible book value per share is calculated by dividing the total shareholders' equity less goodwill shown on the consolidated balance sheets by the number of shares outstanding as of year-end. At December 31, 2018 and 2017, the book value per share is \$63.61 and \$61.40, respectively. At December 31, 2018 and 2017, the tangible book value per share is \$58.87 and \$56.54, respectively.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**Note 2**      **Summary of Significant Accounting Policies, continued**

Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before the consolidated financial statements are available to be issued. The Corporation recognizes in the consolidated financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing the consolidated financial statements. The Corporation's consolidated financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date and before the consolidated financial statements are available to be issued. The Corporation has evaluated subsequent events from December 31, 2018 through March 25, 2019, the date the financial statements were available to be issued. The Corporation did not note any subsequent events requiring disclosure or adjustment to these consolidated financial statements.

New Accounting Standards

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This guidance is a comprehensive new revenue recognition standard that will supersede substantially all existing revenue recognition guidance. The new standard's core principle is that a corporation will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the corporation expects to be entitled in exchange for those goods or services. In doing so, corporations will need to use more judgment and make more estimates than under existing guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. On July 9, 2015, the FASB agreed to delay the effective date of the standard by one year. Therefore, the new standard will be effective for annual reporting periods beginning after December 31, 2018. Implementation of this standard is not expected to have a significant impact on the Corporation's consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, *Financial Instruments – Overall: Recognition and Measurement of Financial Assets and Financial Liabilities*. The amendment has a number of provisions including the requirements that public business entities use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, a separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (i.e. securities or loans receivables), and eliminating the requirement for public business entities to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The amendment is effective for annual and interim reporting periods beginning after December 15, 2018. The Corporation is evaluating the potential impact of the amendment on the Corporation's consolidated financial statements.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**Note 2      Summary of Significant Accounting Policies, continued**

New Accounting Standards, continued

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)* intended to improve financial reporting regarding leasing transactions. The new standard affects all companies and organizations that lease assets. The standard will require organizations to recognize on the statement of financial condition the assets and liabilities for the rights and obligations created by those leases if the lease terms are more than 12 months. The guidance also will require qualitative and quantitative disclosures providing additional information about the amounts recorded in the financial statements. The amendments in this update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Corporation is evaluating the potential impact of the amendment on the Corporation's consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326)* intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The standard requires an organization to measure all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. The standard also requires enhanced disclosures to help investors and other financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio.

These disclosures include qualitative and quantitative requirements that provide additional information about the amounts recorded in the financial statements. Additionally, the standard amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The amendments in this update are effective for fiscal years beginning after December 15, 2021, including interim periods within those fiscal years. All entities may adopt the amendments in this update earlier as of the fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. An entity will apply the amendments in this update through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (that is, a modified-retrospective approach). The Corporation believes the amendments in this update will have an impact on the Corporation's consolidated financial statements and is working to evaluate the significance of that impact.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. This amendment provides guidance on eight specific cash flow issues, including debt prepayment or debt extinguishment costs, settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies, distributions received from equity method investees, beneficial interests in securitization transactions and separately identifiable cash flows and application of the predominance principle. The amendments in this update are effective for public business entities for fiscal years beginning after December 15, 2017. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2018. Early adoption is permitted. Implementation of this standard is not expected to have a significant impact on the Corporation's consolidated financial statements.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 2**      **Summary of Significant Accounting Policies, continued**

New Accounting Standards, continued

In January 2017, the FASB issued ASU No. 2017-04, *Intangibles – Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*. This amendment simplifies how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. Under this amendment, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. The amendments in this update should be applied on a prospective basis. The amendments in this update are effective for a public entity that is a SEC filer for fiscal years beginning after December 15, 2019. The amendments in this update are effective for a public entity that is not a SEC filer for fiscal years after December 15, 2020. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2021. Implementation of this standard is not expected to have a significant impact on the Corporation's consolidated financial statements.

In March 2017, the FASB issued ASU No. 2017-08, *Receivables – Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities*. The amendments in this update shorten the amortization period for certain callable debt securities held at a premium. Specifically, the amendments require the premium to be amortized to the earliest call date. The amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity. For public entities, the amendments in this update are effective for fiscal years beginning after December 15, 2018. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2019. Early adoption is permitted. The amendments of this update are applied on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. The Corporation is evaluating the potential impact to the consolidated financial statements regarding implementation of this amendment.

In May 2017, the FASB issued ASU No. 2017-09, *Compensation – Stock Compensation (Topic 718)*. The amendments in this update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. This amendment requires an entity to account for the effects of a modification unless all of the following are met: (1) The fair value of the modified award is the same as the fair value of the original award immediately before the original award is modified; (2) The vesting conditions of the modified award are the same as the vesting conditions of the original award immediately before the original award is modified; and (3) The classification of the modified award as an equity instrument or a liability instrument is the same as the classification of the original award immediately before the original award is modified. The amendments in this update are effective for all entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2017. Early adoption is permitted. This amendment became effective in 2018 and did not have a significant impact on the Corporation's consolidated financial statements.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 3     Restrictions on Cash and Due From Banks**

The Corporation is required to maintain reserve funds in cash or on deposit with the Federal Reserve Bank. The required reserve at December 31, 2018 and 2017 was \$7,196,000 and \$5,021,000, respectively.

**Note 4     Investment Securities**

The amortized cost and fair values of investment securities at December 31, 2018 are as follows (in thousands):

	<b>December 31, 2018</b>			
	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>
<b>Available-for-sale:</b>				
U.S. Treasury notes	\$ 20,950	\$ -	\$ (268)	\$ 20,682
U.S. Government agencies	8,348	-	(48)	8,300
U.S. Government agency mortgage-backed securities	705	4	(22)	687
Collateralized mortgage obligations	6,611	1	(161)	6,451
Obligations of state and political subdivisions	35,296	116	(253)	35,159
Other investments	1	-	-	1
<b>Total available-for-sale securities</b>	<b>\$ 71,911</b>	<b>\$ 121</b>	<b>\$ (752)</b>	<b>\$ 71,280</b>

The balance sheet as of December 31, 2018 reflects the fair value of available-for-sale securities in the amount of \$71,280,000. A net unrealized loss of \$631,000 is in the available-for-sale investment securities balance. The unrealized loss is included in shareholders' equity.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 4 Investment Securities, continued**

The amortized cost and fair values of investment securities at December 31, 2017 are as follows (in thousands):

	<b>December 31, 2017</b>			
	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>
<b>Available-for-sale:</b>				
U.S. Treasury notes	\$ 21,950	\$ -	\$ (119)	\$ 21,831
U.S. Government agencies	8,431	20	(32)	8,419
U.S. Government agency mortgage-backed securities	935	4	(13)	926
Collateralized mortgage obligations	8,863	23	(85)	8,801
Obligations of state and political subdivisions	30,116	348	(110)	30,354
Other investments	1	-	-	1
<b>Total available-for-sale securities</b>	<b>\$ 70,296</b>	<b>\$ 395</b>	<b>\$ (359)</b>	<b>\$ 70,332</b>

The balance sheet as of December 31, 2017 reflects the fair value of available-for-sale securities in the amount of \$70,332,000. A net unrealized gain of \$36,000 is in the available-for-sale investment securities balance. The unrealized gain is included in shareholders' equity.

The amortized cost and fair value of debt securities at December 31, 2018, by contractual maturity, are shown below (in thousands). Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Mortgage-backed securities and collateralized mortgage obligations are shown separately, since they are not due at a single maturity date.

	<b>Available-for-Sale</b>	
	<b>Amortized Cost</b>	<b>Fair Value</b>
<b>Amounts maturing in:</b>		
One year or less	\$ 14,131	\$ 14,086
After one year through five years	31,373	31,031
After five years through ten years	9,792	9,724
After ten years	9,299	9,301
	<u>64,595</u>	<u>64,142</u>
U.S. Government agency mortgage-backed securities	705	687
Collateralized mortgage obligations	6,611	6,451
<b>Totals</b>	<b>\$ 71,911</b>	<b>\$ 71,280</b>

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**Note 4 Investment Securities, continued**

Investment securities with fair market values of \$15,044,000 and \$4,862,000 at December 31, 2018 and 2017, respectively, were pledged to secure public deposits and for other purposes as required or permitted by law.

During 2018 and 2017, the Corporation received proceeds totaling \$1,973,000 and \$2,642,000, respectively, from sales of available-for-sale investment securities. These sales resulted in gross realized gains of \$19,000 and \$37,000, respectively. During 2018 and 2017, the Corporation received proceeds totaling \$1,799,000 and \$63,000, respectively, from the redemptions of Federal Home Loan Bank (FHLB) stock. The FHLB stock was redeemed at par value, so there were no realized gains or losses on these redemptions.

Information pertaining to securities with gross unrealized losses at December 31, 2018 and 2017, aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows (in thousands):

	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
<b>December 31, 2018:</b>						
Federal agencies	\$ 8,122	\$ (45)	\$ 27,862	\$ (454)	\$ 35,984	\$ (499)
Municipals	10,637	(45)	13,988	(208)	24,625	(253)
Total	\$ 18,759	\$ (90)	\$ 41,850	\$ (662)	\$ 60,609	\$ (752)
<b>December 31, 2017:</b>						
Federal agencies	\$ 28,224	\$ (151)	\$ 5,466	\$ (98)	\$ 33,690	\$ (249)
Municipals	10,842	(66)	1,979	(44)	12,821	(110)
Total	\$ 39,066	\$ (217)	\$ 7,445	\$ (142)	\$ 46,511	\$ (359)

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer and (3) the intent and ability of the Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

At December 31, 2018, the 77 debt securities with unrealized losses have depreciated 1.23% from the Corporation's amortized cost basis. These securities are primarily guaranteed by either the U.S. Government or other governments. The unrealized losses relate principally to current interest rates for similar types of securities. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred and the results of reviews of the issuer's financial condition. As management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available-for-sale, no declines are deemed to be other-than-temporary.



**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 5      Loans and Allowance for Loan Losses**

An analysis of loan categories at December 31, 2018 and 2017 is as follows (in thousands):

	<u>2018</u>	<u>2017</u>
Commercial, agricultural and industrial loans	\$ 21,435	\$ 20,398
Real estate (RE) loans:		
Construction, land and land development	22,896	18,943
Residential 1-4 family	31,021	24,626
Commercial RE	115,612	106,185
Consumer loans	2,643	3,980
Overdrafts	<u>36</u>	<u>362</u>
	193,643	174,494
Less: Net deferred loan fees	(378)	(265)
Allowance for loan losses	<u>(1,933)</u>	<u>(1,747)</u>
Loans, Net	<u>\$ 191,332</u>	<u>\$ 172,482</u>

At December 31, 2018, Residential 1-4 family loans shown above include mortgage loans held-for-sale totaling \$1,176,000. At December 31, 2017, there were no Residential 1-4 family loans held-for-sale.

At December 31, 2018 and 2017, there were no Residential 1-4 family loans in process of foreclosure.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**Note 5      Loans and Allowance for Loan Losses, continued**

Transactions in the allowance for loan losses in 2018 are summarized as follows (in thousands):

	<u>Commercial, Agricultural and Industrial</u>	<u>Construction, Land and Land Development</u>	<u>Residential 1-4 Family</u>	<u>Commercial Real Estate</u>	<u>Consumer and Other</u>	<u>Unallocated</u>	<u>2018 Total</u>
<b><u>Allowance for Loan Losses:</u></b>							
Balance, beginning of year	\$ 93	\$ 14	\$ 223	\$ 62	\$ 44	\$ 1,311	\$ 1,747
Provisions, charged (credited) to income	<u>(22)</u>	<u>(8)</u>	<u>(147)</u>	<u>(25)</u>	<u>-</u>	<u>405</u>	<u>203</u>
	<u>71</u>	<u>6</u>	<u>76</u>	<u>37</u>	<u>44</u>	<u>1,716</u>	<u>1,950</u>
Loans charged-off	(19)	-	-	-	(1)	-	(20)
Recoveries of loans previously charged-off	<u>2</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1</u>	<u>-</u>	<u>3</u>
Net charge-offs	<u>(17)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(17)</u>
Balance, end of year	<u>\$ 54</u>	<u>\$ 6</u>	<u>\$ 76</u>	<u>\$ 37</u>	<u>\$ 44</u>	<u>\$ 1,716</u>	<u>\$ 1,933</u>
Ending balance: Individually evaluated for impairment	\$ 16	\$ -	\$ 60	\$ -	\$ -	\$ -	\$ 76
Ending balance: Collectively evaluated for impairment	<u>38</u>	<u>6</u>	<u>16</u>	<u>37</u>	<u>44</u>	<u>1,716</u>	<u>1,857</u>
Balance, end of year	<u>\$ 54</u>	<u>\$ 6</u>	<u>\$ 76</u>	<u>\$ 37</u>	<u>\$ 44</u>	<u>\$ 1,716</u>	<u>\$ 1,933</u>
<b><u>Loans:</u></b>							
Ending balance: Individually evaluated for impairment	\$ 32	\$ -	\$ 627	\$ 505	\$ 2	\$ -	\$ 1,166
Ending balance: Collectively evaluated for impairment	<u>21,403</u>	<u>22,896</u>	<u>30,394</u>	<u>115,107</u>	<u>2,677</u>	<u>-</u>	<u>192,477</u>
Ending balance total loans	<u>\$ 21,435</u>	<u>\$ 22,896</u>	<u>\$ 31,021</u>	<u>\$ 115,612</u>	<u>\$ 2,679</u>	<u>\$ -</u>	<u>\$ 193,643</u>

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**Note 5      Loans and Allowance for Loan Losses, continued**

Transactions in the allowance for loan losses in 2017 are summarized as follows (in thousands):

	<u>Commercial, Agricultural and Industrial</u>	<u>Construction, Land and Land Development</u>	<u>Residential 1-4 Family</u>	<u>Commercial Real Estate</u>	<u>Consumer and Other</u>	<u>Unallocated</u>	<u>2017 Total</u>
<b><u>Allowance for Loan Losses:</u></b>							
Balance, beginning of year	\$ 96	\$ 4	\$ 195	\$ 74	\$ 44	\$ 1,274	\$ 1,687
Provisions, charged (credited) to income	<u>15</u>	<u>10</u>	<u>28</u>	<u>(12)</u>	<u>2</u>	<u>37</u>	<u>80</u>
	<u>111</u>	<u>14</u>	<u>223</u>	<u>62</u>	<u>46</u>	<u>1,311</u>	<u>1,767</u>
Loans charged-off	(18)	-	-	-	(4)	-	(22)
Recoveries of loans previously charged-off	-	-	-	-	2	-	2
Net charge-offs	<u>(18)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(2)</u>	<u>-</u>	<u>(20)</u>
Balance, end of year	<u>\$ 93</u>	<u>\$ 14</u>	<u>\$ 223</u>	<u>\$ 62</u>	<u>\$ 44</u>	<u>\$ 1,311</u>	<u>\$ 1,747</u>
Ending balance: Individually evaluated for impairment	\$ 10	\$ -	\$ 205	\$ -	\$ -	\$ -	\$ 215
Ending balance: Collectively evaluated for impairment	<u>83</u>	<u>14</u>	<u>18</u>	<u>62</u>	<u>44</u>	<u>1,311</u>	<u>1,532</u>
Balance, end of year	<u>\$ 93</u>	<u>\$ 14</u>	<u>\$ 223</u>	<u>\$ 62</u>	<u>\$ 44</u>	<u>\$ 1,311</u>	<u>\$ 1,747</u>
<b><u>Loans:</u></b>							
Ending balance: Individually evaluated for impairment	\$ 69	\$ -	\$ 988	\$ 627	\$ 10		\$ 1,694
Ending balance: Collectively evaluated for impairment	<u>20,329</u>	<u>18,943</u>	<u>23,638</u>	<u>105,558</u>	<u>4,332</u>		<u>172,800</u>
Ending balance total loans	<u>\$ 20,398</u>	<u>\$ 18,943</u>	<u>\$ 24,626</u>	<u>\$ 106,185</u>	<u>\$ 4,342</u>		<u>\$ 174,494</u>

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 5    Loans and Allowance for Loan Losses, continued**

Federal regulations require that the Corporation periodically evaluate the risks inherent in its loan portfolio. In addition, the Corporation's regulatory agencies have authority to identify problem loans and, if appropriate, require them to be reclassified. There are three classifications for problem loans: Substandard, Doubtful and Loss. Substandard loans have one or more defined weaknesses and are characterized by the distinct possibility that the Corporation will sustain some loss if the deficiencies are not corrected. Doubtful loans have the weaknesses of loans classified as "Substandard," with additional characteristics that suggest the weaknesses make collection or recovery in full after liquidation of collateral questionable on the basis of currently existing facts, conditions and values. There is a high possibility of loss in loans classified as "Doubtful." A loan classified as "Loss" is considered uncollectible and of such little value that continued classification of the credit as a loan is not warranted. If a loan or a portion thereof is classified as "Loss," it must be charged-off, meaning the amount of the loss is charged against the allowance for loan losses, thereby reducing that reserve. The Corporation also classifies some loans as "Watch" or "Other Assets Especially Mentioned" ("OAEM"). Loans classified as Watch are performing assets and classified as pass credits but have elements of risk that require more monitoring than other performing loans. Loans classified as OAEM are assets that continue to perform but have shown deterioration in credit quality and require close monitoring.

Loans by credit quality risk rating at December 31, 2018 and 2017 are as follows (in thousands):

	<u>Pass</u>	<u>Other Assets Especially Mentioned</u>	<u>Sub- Standard</u>	<u>Doubtful</u>	<u>Total</u>
<b>December 31, 2018:</b>					
Commercial, agricultural and industrial loans	\$ 18,668	\$ 2,711	\$ 56	\$ -	\$ 21,435
Real estate (RE) loans:					
Construction, land and land development	22,768	128	-	-	22,896
Residential 1-4 family	29,050	1,339	632	-	31,021
Commercial RE	110,081	3,361	2,170	-	115,612
Consumer and other loans	<u>2,643</u>	<u>11</u>	<u>25</u>	<u>-</u>	<u>2,679</u>
Subtotal	<u>\$ 183,210</u>	<u>\$ 7,550</u>	<u>\$ 2,883</u>	<u>\$ -</u>	193,643
Less: Net deferred loan fees					<u>(378)</u>
Total loans					<u>\$ 193,265</u>
<b>December 31, 2017:</b>					
Commercial, agricultural and industrial loans	\$ 19,627	\$ 271	\$ 500	\$ -	\$ 20,398
Real estate (RE) loans:					
Construction, land and land development	18,048	643	252	-	18,943
Residential 1-4 family	23,389	532	705	-	24,626
Commercial RE	101,930	1,563	2,692	-	106,185
Consumer and other loans	<u>4,266</u>	<u>15</u>	<u>61</u>	<u>-</u>	<u>4,342</u>
Subtotal	<u>\$ 167,260</u>	<u>\$ 3,024</u>	<u>\$ 4,210</u>	<u>\$ -</u>	174,494
Less: Net deferred loan fees					<u>(265)</u>
Total loans					<u>\$ 174,229</u>

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**Note 5 Loans and Allowance for Loan Losses, continued**

An analysis of nonaccrual loans by category at December 31, 2018 and 2017 is as follows (in thousands):

	<u>2018</u>	<u>2017</u>
Commercial, agriculture and industrial loans	\$ -	\$ 5
Real estate (RE) loans:		
Commercial RE	278	359
Consumer and other loans	<u>2</u>	<u>-</u>
Total nonaccrual loans	<u>\$ 280</u>	<u>\$ 364</u>

At December 31, 2018 and 2017, a summary of information pertaining to impaired loans is as follows (in thousands):

	<u>Unpaid Contractual Principal Balance</u>	<u>Recorded Investment with No Allowance</u>	<u>Recorded Investment with Allowance</u>	<u>Total Recorded Investment</u>	<u>Related Allowance</u>	<u>Average Recorded Investment</u>	<u>Interest Income Recognized</u>
<b>December 31, 2018:</b>							
Commercial, agriculture and industrial loans	\$ 63	\$ -	\$ 32	\$ 32	\$ 16	\$ 51	\$ 2
Real estate (RE) loans:							
Residential 1-4 family	627	-	627	627	60	807	33
Commercial RE	623	-	505	505	-	566	15
Consumer and other loans	<u>2</u>	<u>2</u>	<u>-</u>	<u>2</u>	<u>-</u>	<u>6</u>	<u>-</u>
Total	<u>\$ 1,315</u>	<u>\$ 2</u>	<u>\$ 1,164</u>	<u>\$ 1,166</u>	<u>\$ 76</u>	<u>\$ 1,430</u>	<u>\$ 50</u>
<b>December 31, 2017:</b>							
Commercial, agriculture and industrial loans	\$ 93	\$ -	\$ 69	\$ 69	\$ 10	\$ 96	\$ 4
Real estate (RE) loans:							
Residential 1-4 family	988	-	988	988	205	1,215	53
Commercial RE	715	-	627	627	-	562	11
Consumer and other loans	<u>10</u>	<u>-</u>	<u>10</u>	<u>10</u>	<u>-</u>	<u>14</u>	<u>1</u>
Total	<u>\$ 1,806</u>	<u>\$ -</u>	<u>\$ 1,694</u>	<u>\$ 1,694</u>	<u>\$ 215</u>	<u>\$ 1,887</u>	<u>\$ 69</u>

The Corporation has no commitments to loan additional funds to borrowers whose loans are impaired.

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**Note 5    Loans and Allowance for Loan Losses, continued**

Troubled Debt Restructurings

The restructuring of a loan is considered a “troubled debt restructuring” if both (i) the borrower is experiencing financial difficulties and (ii) the creditor has granted a concession. Concessions may include interest rate reductions or below market interest rates, principal forgiveness, restructuring amortization schedules and other actions intended to minimize potential losses.

There were no troubled debts restructured during 2018. Troubled debt restructurings during 2017 are set forth in the following table (in thousands, except for number of contracts):

<b>December 31, 2017:</b>	<b>Number of Contracts</b>	<b>Balance at Restructuring Date</b>	<b>Balance at December 31, 2017</b>
Commercial, agriculture and industrial loans	1	\$        62	\$        52
Real estate (RE) loans:			
Commercial RE	1	211	192
Total troubled debt restructurings	<u>2</u>	<u>\$        273</u>	<u>\$        244</u>

Concessions granted on these loans include reduction of interest rates and restructuring payments to match borrower’s cash flow. At December 31, 2018 and 2017, all loans restructured were paying in accordance to the restructured terms.

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**Note 5    Loans and Allowance for Loan Losses, continued**

The following table illustrates an age analysis of past due loans as of December 31, 2018 and 2017 (in thousands):

	<b>30-89 Days Past Due</b>	<b>90 Days or More Past Due</b>	<b>Total Past Due</b>	<b>Current</b>	<b>Total Loans</b>	<b>Recorded Investment 90 Days or More Past Due and Still Accruing</b>
<b>December 31, 2018:</b>						
Commercial, agricultural and industrial loans	\$ 43	\$ -	\$ 43	\$ 21,392	\$ 21,435	\$ -
Real estate (RE) loans:						
Construction, land and land development	-	-	-	22,896	22,896	-
Residential 1-4 family	54	-	54	30,967	31,021	-
Commercial RE	151	-	151	115,461	115,612	-
Consumer and other loans	-	-	-	2,679	2,679	-
Less: Net deferred loan fees	-	-	-	(378)	(378)	-
<b>Total</b>	<b>\$ 248</b>	<b>\$ -</b>	<b>\$ 248</b>	<b>\$ 193,017</b>	<b>\$ 193,265</b>	<b>\$ -</b>
<b>December 31, 2017:</b>						
Commercial, agricultural and industrial loans	\$ 455	\$ -	\$ 455	\$ 19,943	\$ 20,398	\$ -
Real estate (RE) loans:						
Construction, land and land development	971	-	971	17,972	18,943	-
Residential 1-4 family	120	-	120	24,506	24,626	-
Commercial RE	-	25	25	106,160	106,185	-
Consumer and other loans	-	-	-	4,342	4,342	-
Less: Net deferred loan fees	-	-	-	(265)	(265)	-
<b>Total</b>	<b>\$ 1,546</b>	<b>\$ 25</b>	<b>\$ 1,571</b>	<b>\$ 172,658</b>	<b>\$ 174,229</b>	<b>\$ -</b>

The Corporation grants commercial, consumer and real estate loans to customers within Southeastern Washington State. A substantial portion of its debtors' ability to honor their contracts is dependent upon the commercial and real estate economic sectors in that geographic area.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
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**Note 6 Premises and Equipment**

The investment in premises and equipment at December 31, 2018 and 2017 is as follows (in thousands):

	<u>2018</u>	<u>2017</u>
Land	\$ 1,050	\$ 1,050
Buildings	5,797	4,737
Leasehold improvements	545	507
Furniture and equipment	2,554	1,825
Premises and equipment in process	<u>115</u>	<u>208</u>
	10,061	8,327
Less accumulated depreciation and amortization	<u>(3,143)</u>	<u>(2,690)</u>
Premises and equipment, net	<u>\$ 6,918</u>	<u>\$ 5,637</u>

Depreciation and amortization on premises and equipment charged to expense totaled \$471,000 and \$350,000 for the years ended December 31, 2018 and 2017, respectively. Computer software, net of accumulated amortization, is included in Other Assets. Amortization on computer software charged to expense totaled \$87,000 and \$59,000 for the years ended December 31, 2018 and 2017, respectively.

The Corporation owns the building that houses its main branch and leases the land and a sign from a director. The lease is classified as an operating lease with an initial term of ten years and minimum annual rents of \$28,000, with cost of living increases annually. The initial lease term expired February 28, 2012 and was renewed through February 28, 2017. During 2017, this lease was renewed through February 28, 2022. The land lease contains renewal clauses from five to twenty years and escalation clauses based on increases in the Consumer Price Index. As of December 31, 2018, this lease includes two more renewal options of five years each.

The Corporation has also entered into a lease agreement for the Richland branch facilities which opened in January 2006. The original lease was for a term of five years with a renewal option of another five years and provided for minimum annual rents of \$61,000. On December 31, 2010, the renewal option was exercised and expired December 31, 2015. During 2015, both parties agreed to renew this lease for an additional five years which extended the expiration date to December 31, 2020.

During 2015, the Corporation entered into a lease agreement with a director for its administrative offices. The initial term of this lease is December 1, 2015 through May 31, 2017 and includes a month-to-month lease clause through May 31, 2018. The monthly lease amount is \$1,650. During 2018, the administrative offices moved to the new Grandridge facility. Therefore, as of December 31, 2018, this office space is no longer being leased.

On December 18, 2015, the Corporation entered into a lease agreement with a director for the facilities that are used by HFG Trust, LLC, a subsidiary of the Bank. This lease has an effective date of January 1, 2016 through December 31, 2018 and includes options to renew and extend the term for an additional one, two or three years. The lease agreement provides for minimum annual rents of \$60,000 and has annual rent increases based on the Consumer Price Index. During 2018, HFG Trust, LLC relocated to the new Grandridge facility; therefore, this lease was not renewed.



**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
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**Note 6 Premises and Equipment, continued**

The Corporation recorded lease expense in the amount of \$216,000 and \$256,000 for the years ended December 31, 2018 and 2017, respectively. Included in the lease expense were amounts paid to a related parties in the amount of \$100,000 and \$146,000 for the years ended December 31, 2018 and 2017, respectively.

The minimum payments under the Corporation's leases required for the next five years are as follows (in thousands):

2019	\$	158
2020		161
2021		58
2022		10
2023		-
Total	\$	<u>387</u>

**Note 7 Goodwill**

As discussed in Note 1, the Corporation completed the HFG acquisition effective January 1, 2016. This acquisition resulted in goodwill being recorded which totaled \$2,473,000. In accordance with authoritative guidance issued by the FASB, the goodwill will not be amortized and will be evaluated for impairment at least annually. No impairment of goodwill was identified during 2018 or 2017.

**Note 8 Deposits**

The carrying amounts of deposits at December 31, 2018 and 2017 are as follows (in thousands):

	<u>2018</u>	<u>2017</u>
Demand	\$ 124,557	\$ 113,063
Interest-bearing transaction accounts	143,406	141,057
Savings	12,765	9,504
Time deposits less than \$250,000	8,014	8,251
Time deposits \$250,000 and over	<u>2,017</u>	<u>1,542</u>
Total deposits	<u>\$ 290,759</u>	<u>\$ 273,417</u>

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
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**Note 8 Deposits, continued**

Maturities of time deposits for each of the next five years are as follows (in thousands):

2019		\$	8,889
2020			368
2021			219
2022			313
2023			<u>242</u>
Total		\$	<u><u>10,031</u></u>

At December 31, 2018 and 2017, there were no brokered deposits or deposits obtained from customers outside the Corporation's primary market area.

**Note 9 Advances from Federal Home Loan Bank**

During 2008, the Corporation borrowed \$500,000 from the Federal Home Loan Bank. Interest is assessed at a fixed rate of 4.97%. Interest only payments are due monthly with principal and any unpaid interest due at the maturity date on May 9, 2018. During 2017, the Corporation repaid these borrowings. At December 31, 2018 and 2017, there were no outstanding balances due to the Federal Home Loan Bank.

**Note 10 Related Party Transactions**

During 2018 and 2017, the Corporation had transactions made in the ordinary course of business with certain of its officers, directors and principal shareholders. All loans included in such transactions were made on substantially the same terms, including interest rate and collateral, as those prevailing at the time for comparable transactions with other persons, and did not, in the opinion of management, involve more than normal credit risk or present other unfavorable features.

A summary of these transactions follows (in thousands):

	<u>Balance Beginning of Year</u>	<u>Additions</u>	<u>Amounts Collected</u>	<u>Balance End of Year</u>
For the year ended:				
<b>December 31, 2018</b>	\$ -	\$ 25	\$ (25)	\$ -
<b>December 31, 2017</b>	<u>\$ -</u>	<u>\$ 22</u>	<u>\$ (22)</u>	<u>\$ -</u>

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
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**Note 10 Related Party Transactions, continued**

The Corporation held deposits for certain of its officers, directors and principal shareholders in the amount of \$28,636,000 and \$28,637,000 at December 31, 2018 and 2017, respectively.

The Corporation has entered into lease agreements with related parties for various locations. Refer to Note 6 for additional information regarding these lease agreements.

**Note 11 Financial Instruments with Off-Balance-Sheet Risk**

In the normal course of business, there are outstanding various commitments and contingent liabilities, such as commitments to extend credit and standby letters of credit, which are not reflected in the financial statements. The Corporation's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual or notional amount of those instruments. The Corporation uses the same credit policies in making such commitments as it does for instruments that are included in the balance sheets.

Financial instruments whose contract amount represents credit risk were as follows (in thousands):

	<b>2018</b>	<b>2017</b>
Commitments to extend credit	\$ 41,236	\$ 33,994
Standby letters of credit	-	-

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Corporation's experience has been that approximately 70% of loan commitments are drawn upon by customers. The Corporation evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Corporation upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include accounts receivable, inventory, property and equipment and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the Corporation to guarantee the performance of a customer to a third party. Standby letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Corporation's policy for obtaining collateral, and the nature of such collateral, is essentially the same as that involved in making commitments to extend credit.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
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**Note 11 Financial Instruments with Off-Balance-Sheet Risk, continued**

The Corporation has guaranteed credit cards issued by another financial institution to some of the Corporation's customers. The Corporation has exposure to credit loss in the event that there is nonperformance by their customer.

The Corporation has not been required to perform on any financial guarantees during 2018 or 2017. The Corporation has not incurred any material losses on its commitments in 2018 or 2017.

**Note 12 Compensated Absences**

Employees of the Corporation are entitled to paid vacation, paid sick days and personal days off, depending on job classification, length of service and other factors. It is impracticable to estimate the amount of compensation for future absences, and accordingly, no liability has been recorded in the accompanying financial statements. The Corporation's policy is to recognize the costs of compensated absences when actually paid to employees.

**Note 13 Commitments and Contingent Liabilities**

The Corporation is subject to claims and lawsuits which arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the financial position of the Corporation.

The Bank participates in the Washington State Public Depository program. In February 2009, new standards were adopted which require institutions to collateralize uninsured public deposits at 100 percent. In June 2016, resolution 2016-1 was adopted which reduced the collateral requirement from 100 percent of uninsured public deposits to 50 percent for well-capitalized public depository banks. At December 31, 2018 and 2017, the Corporation had pledged investment securities with a carrying amount of \$15,001,000 and \$4,810,000, respectively, to secure public deposits. Refer to Note 4 for additional information.

The Corporation has entered into employment agreements with certain advisors of HFG Trust, LLC which provides for the award of phantom units that entitle the advisor to receive a payment equal to different percentages of the Modified Net Income of HFG Trust, LLC each fiscal year that they are employed by HFG Trust, LLC. The agreement also provides for the redemption of the phantom units upon termination of employment which occurs on the first of (1) termination of the advisor's employment with HFG Trust, LLC for any reason or (2) advisor reaching the age of 66. Payment for the redemption of the phantom units will be made on the 1<sup>st</sup> day of May of the calendar year following the year of termination by delivery of (1) shares of common stock of the Corporation equal to 66.7% of the redemption price and (2) a lump sum payment equal to 33.3% of the redemption price. Each phantom unit is entitled to one percent of the formula value of HFG as of the close of business on the last day of the fiscal year that termination occurs. The formula value of HFG is defined as an amount equal to the measurement year gross revenue multiplied by the net operating percentage (the average modified net income as a percentage of gross revenue over three years) multiplied by the earnings multiple (which shall not be less than 6.5 or greater than 8.5).

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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**Note 14**    **Lines of Credit**

The Corporation has established an unsecured line of credit in the amount of \$3,000,000 for overnight purchase of federal funds. This line may be cancelled without prior notification. There were no outstanding balances on this line of credit at December 31, 2018 and 2017.

The Corporation also has a credit line with the Federal Home Loan Bank of Des Moines totaling 45% of assets which had available borrowings of \$136,563,000 at December 31, 2018 assuming assets are pledged accordingly. There were no outstanding balances on this line of credit at December 31, 2018 and 2017. This line is collateralized by pledged loans and investment securities with a carrying amount of \$27,296,000 and \$6,000, respectively, at December 31, 2018. Refer to Note 9 for additional information on this line of credit.

**Note 15**    **Concentration of Credit Risk**

The Corporation maintains its cash accounts with several correspondent banks. Generally, accounts are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 per bank. At December 31, 2018, the Corporation had no uninsured deposits in other financial institutions. At December 31, 2017, the Corporation had uninsured deposits in other financial institutions totaling \$2,550,000. Furthermore, federal funds sold are essentially uncollateralized loans to other financial institutions. Management regularly evaluates the credit risk associated with the counterparties to these transactions and believes that the Corporation is not exposed to any significant credit risks on cash and cash equivalents.

The Corporation has credit risk exposure, including off-balance-sheet credit risk exposure, as disclosed in Notes 5 and 11. Most of the Corporation's business activity is with customers located in the state of Washington. The ultimate collectability of a substantial portion of the loan portfolio is susceptible to changes in economic and market conditions in the region. The Corporation generally requires collateral on all real estate loans and typically maintains loan-to-value ratios of no greater than 75% to 80%. Loans are generally limited, by state banking regulations, to 20% of the Bank's shareholder's equity, excluding accumulated other comprehensive income (loss). The Corporation, as a matter of practice, generally does not extend credit to any single borrower or group of related borrowers in excess of \$5,000,000.

The contractual amounts of credit related financial instruments such as commitments to extend credit and letters of credit represent the amounts of potential accounting loss should the contract be fully drawn upon, the customer defaults and the value of any existing collateral becomes worthless. Letters of credit are granted primarily to commercial borrowers.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
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**Note 16 Stock Compensation Plans**

During 2009, the Board of Directors adopted the “2009 Employee Stock Option and Equity Compensation Plan”. This Plan was approved at the 2009 annual shareholders’ meeting. This Plan provides for stock awards in the form of stock options, restricted stock grants, restricted stock units and stock appreciation rights. The Plan allows for both incentive and non-qualified stock options to be granted. The Corporation may grant up to 65,000 shares under this Plan to certain key employees and directors. At December 31, 2018, there were 18,512 shares available for grant under this Plan. The exercise price of options and the value of other awards is equal to the fair market value of the Corporation’s stock on the date of grant. The maximum term of stock options is 10 years. Options are 100% vested five years after the grant date. The Corporation has entered into “Restricted Stock Award Agreements” with certain of its executive officers. These awards vest ratably over a period of two - ten years from the date of grant depending on the terms of the agreement.

A summary of the Corporation’s restricted stock awards and activity for the years ending December 31, 2018 and 2017 is presented below:

	<u>Restricted Shares</u>	<u>Weighted- Average Grant Date Fair Value</u>
Outstanding at January 1, 2017	105	\$ 57.70
Granted	-	-
Forfeited	-	-
Vested	<u>(105)</u>	<u>57.70</u>
Non-vested at December 31, 2017	<u>-</u>	<u>\$ -</u>
Outstanding at January 1, 2018	-	\$ -
Granted	3,600	80.50
Forfeited	-	-
Vested	<u>-</u>	<u>-</u>
Non-vested at December 31, 2018	<u>3,600</u>	<u>\$ 80.50</u>

Under the provisions of the Plan, grantees of restricted stock awards have all the rights of a shareholder (including voting, dividend and liquidation rights). Stock compensation expense totaling \$90,000 and \$1,000 was recorded during 2018 and 2017, respectively, relating to restricted stock awards. At December 31, 2018, there was unrecognized compensation expense relating to these awards totaling \$197,000 which will be recognized over 9 years.

During 2013, the Corporation approved a stock grant program for directors’ compensation. Under this program, the equivalent number of shares of the Corporation’s common stock will be issued at the beginning of each year based on the prior year’s stock compensation expense divided by the fair value of the Corporation’s common stock. During 2018 and 2017, stock compensation expense totaling \$66,000 and \$54,000, respectively, was recorded relating to directors’ compensation. During 2018 and 2017, 819 and 813 shares, respectively, were issued to directors relating to this program.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
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**Note 16 Stock Compensation Plans, continued**

Prior to the adoption of this Plan, the Corporation had two share-based compensation plans. Under these two stock option plans, the Corporation may grant both incentive and non-qualified options for up to 56,745 shares of its common stock to certain key employees and directors. The exercise price of each option equals the fair market value of the Corporation's stock on the date of grant, and an option's maximum term is 10 years. Options vest 20% annually for five years. These plans were terminated with the adoption of the "2009 Employee Stock Option and Equity Compensation Plan." The termination of these plans does not affect the terms of any outstanding options under these plans.

The compensation cost that has been charged against income for these plans was \$1,000 and \$-0- for the years ended December 31, 2018 and 2017, respectively. Since the Corporation made the Subchapter S election effective January 1, 2006, there is no tax benefit recognized in the income statement for share-based compensation arrangements for the years ended December 31, 2018 and 2017.

The Corporation accounts for stock-based awards to employees and directors using the fair value method, in accordance with accounting guidance issued by the FASB. The Corporation uses the Black-Scholes valuation model to estimate the fair value of stock option awards. The following assumptions are used in the Black-Scholes model: expected volatility, expected dividends, expected term and risk-free rate. Expected volatilities are based on the historical volatility of the Corporation's stock and other factors. The Corporation uses historical data to estimate option exercise and employee termination within the model. The expected term of options granted is determined from the output of the option valuation model and management's experience and represents the period of time that options granted are expected to be outstanding. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. The assumptions are determined at the date of grant and are not subsequently adjusted for actual. The following assumptions were used regarding the 2018 and 2017 grants of stock options:

	<u>2018</u>	<u>2017</u>
Expected volatility	7.27%	7.26%
Weighted-average volatility	7.27%	7.26%
Expected dividends	4.92%	4.93%
Expected term (in years)	10 yrs	10 yrs
Risk-free rate	2.75%	2.20%

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
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**Note 16 Stock Compensation Plans, continued**

A summary of option activity under the Plans as of December 31, 2018 and 2017, and changes during the years then ended, are presented below:

<u>Options</u>	<u>Shares</u>	<u>Weighted-Average Exercise Price</u>	<u>Weighted-Average Remaining Contractual Term</u>
Outstanding at January 1, 2017	19,000	\$ 56.71	
Granted	6,500	66.00	
Exercised	(2,238)	44.00	
Forfeited or expired	-	-	
Outstanding at December 31, 2017	<u>23,262</u>	<u>\$ 60.12</u>	<u>6.56</u>
Vested or expected to vest at December 31, 2017	<u>23,262</u>	<u>\$ 60.12</u>	<u>6.56</u>
Exercisable at December 31, 2017	<u>11,162</u>	<u>\$ 57.55</u>	<u>5.45</u>
Outstanding at January 1, 2018	23,262	\$ 60.12	
Granted	6,500	77.75	
Exercised	(5,062)	52.34	
Forfeited or expired	(1,200)	64.67	
Outstanding at December 31, 2018	<u>23,500</u>	<u>\$ 67.29</u>	<u>7.37</u>
Vested or expected to vest at December 31, 2018	<u>23,500</u>	<u>\$ 67.29</u>	<u>7.37</u>
Exercisable at December 31, 2018	<u>10,300</u>	<u>\$ 62.47</u>	<u>6.11</u>

During 2018 and 2017, there were 6,500 options granted. The proceeds from options exercised were \$265,000 and \$98,000 in 2018 and 2017, respectively.

A summary of the status of the Corporation's nonvested shares relating to stock options as of December 31, 2018, and changes during the year then ended, is presented below:

<u>Nonvested Shares</u>	<u>Shares</u>	<u>Weighted-Average Grant-Date Fair Value</u>
Nonvested at January 1, 2018	12,100	\$ .71
Granted	6,500	1.14
Vested	(4,200)	.75
Forfeited	(1,200)	.68
Nonvested at December 31, 2018	<u>13,200</u>	<u>\$ .91</u>



**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 16 Stock Compensation Plans, continued**

As of December 31, 2018, there was \$9,000 of total unrecognized compensation cost related to nonvested shares of stock options granted under the Plans. That cost is expected to be recognized over a weighted-average period of 4.25 years.

**Note 17 Employee Benefit Plan**

The Corporation established a KSOP plan in 2005 which has a 401(k) component and an ESOP component. The Corporation has the option to make discretionary matching contributions to this plan. Beginning in 2008 through 2013, the Corporation matched 50% of employee contributions to the 401(k) component of the plan up to a maximum match of \$1,500. Beginning in 2014, the Corporation matched 100% of the first 3% plus 50% of the next 2% of employee contributions to the 401(k) component of the plan up to a maximum match of \$3,000. The Corporation's discretionary contributions for the years ended December 31, 2018 and 2017 were \$147,000 and \$118,000, respectively. At December 31, 2018 and 2017, the ESOP component of this plan held 45,133 and 40,133 shares of the Corporation's stock, respectively.

**Note 18 Regulatory Matters**

Banks are 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 Bank's financial statements. Under the regulatory capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital adequacy guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification under the prompt corrective action guidelines are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios of: Total Risk-Based capital, Tier 1 capital and Common Equity Tier 1 capital to risk-weighted assets (as defined in the regulations), and Leverage capital, which is Tier 1 capital to adjusted total assets (as defined). Management believes as of December 31, 2018 and 2017 that the Bank meets all capital adequacy requirements to which it is subject.

The Bank's Tier 1 capital consists of shareholder's equity excluding unrealized gains and losses on securities available-for-sale and goodwill.

Community First Bank has been notified by its regulators that, as of its most recent regulatory examination, it is regarded as well capitalized under the regulatory framework for prompt corrective action. Such determination has been made based on the Bank's Common Equity Tier 1, Tier 1, total capital and leverage ratios. There have been no conditions or events since this notification that management believes would change the Bank's categorization as well capitalized under the ratios listed on the next page.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 18 Regulatory Matters, continued**

Beginning January 1, 2015, community banking organizations became subject to a new regulatory rule recently adopted by federal banking agencies (commonly referred to as Basel III). The new rule establishes a new regulatory capital framework that incorporates revisions to the Basel capital framework, strengthens the definition of regulatory capital, increases risk-based capital requirements and amends the methodologies for determining risk-weighted assets. These changes are expected to increase the amount of capital required by community banking organizations. Basel III includes a multiyear transition period from January 1, 2015 through December 31, 2019.

Management believes that, as of December 31, 2018 and 2017, the Bank would meet all capital adequacy requirements under the Basel III Capital rules on a fully phased-in basis as if such requirements were currently in effect; however, final rules are subject to regulatory discretion and could result in the need for additional capital levels in the future.

The Bank's actual and required capital amounts and ratios are as follows (dollars in thousands):

	<b>Actual</b>		<b>Minimum Required for Capital Adequacy Purposes</b>		<b>Required to be Well Capitalized under the Prompt Corrective Action Provisions</b>	
	<b>Amount</b>	<b>Ratio</b>	<b>Amount</b>	<b>Ratio</b>	<b>Amount</b>	<b>Ratio</b>
<b>As of December 31, 2018:</b>						
Total Risk-based Capital (to Risk-weighted Assets)	\$ 33,194	15.17%	\$ 17,509	8.00%	\$ 21,886	10.00%
Tier 1 Capital (to Risk-weighted Assets)	\$ 31,211	14.26%	\$ 13,132	6.00%	\$ 17,509	8.00%
Common Equity Tier 1 Capital (to Risk-weighted Assets)	\$ 31,211	14.26%	\$ 9,849	4.50%	\$ 14,226	6.50%
Leverage Capital (to Adjusted Total Assets)	\$ 31,211	9.71%	\$ 12,859	4.00%	\$ 16,074	5.00%
<b>As of December 31, 2017:</b>						
Total Risk-based Capital (to Risk-weighted Assets)	\$ 30,540	15.54%	\$ 15,719	8.00%	\$ 19,649	10.00%
Tier 1 Capital (to Risk-weighted Assets)	\$ 28,743	14.63%	\$ 11,789	6.00%	\$ 15,719	8.00%
Common Equity Tier 1 Capital (to Risk-weighted Assets)	\$ 28,743	14.63%	\$ 8,842	4.50%	\$ 12,772	6.50%
Leverage Capital (to Adjusted Total Assets)	\$ 28,743	9.72%	\$ 11,831	4.00%	\$ 14,789	5.00%

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 19 Fair Value Measurements**

The Corporation has adopted authoritative guidance issued by the FASB regarding fair value measurements for financial assets and financial liabilities. The authoritative guidance defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements.

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

The authoritative guidance issued by the FASB requires the use of valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement cost). Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. In that regard, the authoritative guidance establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

- **Level 1 Inputs:** Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.
- **Level 2 Inputs:** Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.
- **Level 3 Inputs:** Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 19 Fair Value Measurements, continued**

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality and the Corporation's creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time. The Corporation's valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Corporation's valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

**Securities Available-for-Sale:** U.S. Treasury securities are reported at fair value utilizing Level 1 inputs. Other securities classified as available-for-sale are reported at fair value utilizing Level 2 inputs. For these securities, the Corporation obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things.

**Impaired Loans:** Certain impaired loans are reported at the fair value of the underlying collateral if repayment is expected solely from the collateral. Collateral values are estimated using Level 2 inputs based on observable market data or Level 3 inputs based on customized discounting criteria.

**Other Real Estate Owned:** Other real estate owned represents foreclosed assets that are reported at the fair value less estimated selling costs of the underlying property. The fair values are estimated using Level 2 inputs based on observable market data or Level 3 inputs based on information obtained from customized discounting criteria.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 19 Fair Value Measurements, continued**

The following table summarizes financial assets measured at fair value on a recurring basis as of December 31, 2018 and 2017, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure the fair value (in thousands). At December 31, 2018 and 2017, there were no financial liabilities measured at fair value on a recurring basis.

	<u>Level 1 Inputs</u>	<u>Level 2 Inputs</u>	<u>Level 3 Inputs</u>	<u>Total Fair Value</u>
<b>December 31, 2018:</b>				
Available-for-Sale				
U.S. Treasury notes	\$ 20,682	\$ -	\$ -	\$ 20,682
U.S. Government agencies	-	8,300	-	8,300
U.S. Government agency mortgage-backed securities	-	687	-	687
Collateralized mortgage obligations	-	6,451	-	6,451
Obligations of states and political subdivisions	-	35,159	-	35,159
Other investments	-	1	-	1
Totals	<u>\$ 20,682</u>	<u>\$ 50,598</u>	<u>\$ -</u>	<u>\$ 71,280</u>
<b>December 31, 2017:</b>				
Available-for-Sale				
U.S. Treasury notes	\$ 21,831	\$ -	\$ -	\$ 21,831
U.S. Government agencies	-	8,419	-	8,419
U.S. Government agency mortgage-backed securities	-	926	-	926
Collateralized mortgage obligations	-	8,801	-	8,801
Obligations of states and political subdivisions	-	30,354	-	30,354
Other investments	-	1	-	1
Totals	<u>\$ 21,831</u>	<u>\$ 48,501</u>	<u>\$ -</u>	<u>\$ 70,332</u>

Certain financial assets are measured at fair value on a non-recurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). Financial assets measured at fair value on a non-recurring basis include certain impaired loans reported at the fair value of the underlying collateral if repayment is expected solely from the collateral. Collateral values are estimated using Level 2 inputs based on observable market data or Level 3 inputs based on customized discounting criteria.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 19 Fair Value Measurements, continued**

The following table summarizes financial assets measured at fair value on a non-recurring basis as of December 31, 2018 and 2017, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure the fair value (in thousands):

	<u>Level 1 Inputs</u>	<u>Level 2 Inputs</u>	<u>Level 3 Inputs</u>	<u>Total Fair Value</u>
<b>December 31, 2018:</b>				
Impaired loans	\$ -	\$ 1,166	\$ -	\$ 1,166
Less specific valuation allowance for possible loan losses	-	(76)	-	(76)
Impaired loans, net	<u>\$ -</u>	<u>\$ 1,090</u>	<u>\$ -</u>	<u>\$ 1,090</u>
<b>December 31, 2017:</b>				
Impaired loans	\$ -	\$ 1,694	\$ -	\$ 1,694
Less specific valuation allowance for possible loan losses	-	(215)	-	(215)
Impaired loans, net	<u>\$ -</u>	<u>\$ 1,479</u>	<u>\$ -</u>	<u>\$ 1,479</u>

Certain nonfinancial assets are measured at fair value on a non-recurring basis. Nonfinancial assets measured at fair value on a non-recurring basis include other real estate owned which, upon initial recognition, are remeasured and reported at fair value through a charge-off to the allowance for loan losses and certain other real estate owned, which subsequent to their initial recognition, are remeasured at fair value through a writedown included in other non-interest expense. The fair value of other real estate owned is estimated using Level 2 inputs based on observable market data or Level 3 inputs based on customized discounting criteria. At December 31, 2018 and 2017, there was no other real estate owned by the Corporation.

During 2018 and 2017, there were no charge-offs recorded at the time of foreclosure. During 2018 and 2017, there were no writedowns recorded subsequent to foreclosure. Charge-offs recognized upon loan foreclosures are generally offset by general or specific allocations of the allowance for loan losses and generally do not significantly impact the Corporation's provision for loan losses. Regulatory guidelines require the Corporation to reevaluate the fair value of other real estate owned on at least an annual basis.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2018 AND 2017**

**Note 20 Fair Values of Financial Instruments**

The estimated fair values of the Corporation's financial instruments that are reported in the Corporation's consolidated balance sheets at December 31, 2018 and 2017 are as follows (in thousands):

	2018		2017	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Financial assets:</b>				
Cash and due from banks	\$ 6,635	\$ 6,635	\$ 9,230	\$ 9,230
Interest-bearing deposits	35,979	35,976	35,916	35,916
Investment securities	71,280	71,280	70,332	70,332
FHLB stock	366	366	348	348
Loans held-for-sale	1,176	1,176	-	-
Loans, net	190,156	186,999	172,482	148,216
Bank-owned life insurance	6,410	6,410	6,238	6,238
Accrued interest receivable	1,104	1,104	964	964
<b>Financial liabilities:</b>				
Deposits	290,759	290,727	273,417	237,597
Accrued interest payable	27	27	20	20

The carrying amounts in the preceding table are included in the consolidated balance sheets under the applicable captions.

**OTHER FINANCIAL INFORMATION**



**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**CONSOLIDATING BALANCE SHEET**  
**DECEMBER 31, 2018**  
**(Dollars in Thousands)**

	COMMUNITY FIRST BANCORP.	COMMUNITY FIRST BANK	HFG TRUST, LLC	ELIMINATIONS	CONSOLIDATED BALANCES 2018
<b>ASSETS</b>					
Cash and due from banks	\$ 105	\$ 5,964	\$ 566	\$ -	\$ 6,635
Interest-bearing deposits in financial institutions maturing in less than three months	-	34,995	-	-	34,995
Total cash and cash equivalents	105	40,959	566	-	41,630
Interest-bearing deposits in financial institutions maturing in more than three months	-	984	-	-	984
Investment in subsidiary	33,053	3,970	-	(37,023)	-
Investment securities	-	71,279	1	-	71,280
Federal Home Loan Bank stock, at cost	-	366	-	-	366
Loans held-for-sale	-	1,176	-	-	1,176
Loans, net of deferred loan fees and allowance for loan losses	-	190,156	-	-	190,156
Premises and equipment, net of accumulated depreciation	-	6,829	89	-	6,918
Bank-owned life insurance	-	6,410	-	-	6,410
Goodwill	-	-	2,473	-	2,473
Accrued interest receivable	-	1,104	-	-	1,104
Other assets	-	791	956	-	1,747
<b>Total Assets</b>	<b>\$ 33,158</b>	<b>\$ 324,024</b>	<b>\$ 4,085</b>	<b>\$ (37,023)</b>	<b>\$ 324,244</b>
<b>LIABILITIES</b>					
Deposits	\$ -	\$ 290,759	\$ -	\$ -	\$ 290,759
Other liabilities:					
Accrued interest payable	-	27	-	-	27
Accrued expenses and other liabilities	-	185	115	-	300
Total other liabilities	-	212	115	-	327
<b>Total Liabilities</b>	<b>-</b>	<b>290,971</b>	<b>115</b>	<b>-</b>	<b>291,086</b>
<b>SHAREHOLDERS' EQUITY</b>					
Common stock, \$1 par value:					
Authorized - 1,000,000 shares					
Issued and outstanding - 521,247 shares	521	401	-	(401)	521
Additional paid-in capital	14,850	14,647	3,249	(17,896)	14,850
Retained earnings	18,418	18,636	721	(19,357)	18,418
Accumulated other comprehensive loss	(631)	(631)	-	631	(631)
<b>Total Shareholders' Equity</b>	<b>33,158</b>	<b>33,053</b>	<b>3,970</b>	<b>(37,023)</b>	<b>33,158</b>
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 33,158</b>	<b>\$ 324,024</b>	<b>\$ 4,085</b>	<b>\$ (37,023)</b>	<b>\$ 324,244</b>

See Independent Auditor's Report.

**COMMUNITY FIRST BANCORPORATION, INC. AND SUBSIDIARIES**  
**CONSOLIDATING STATEMENT OF INCOME**  
**FOR THE YEAR ENDED DECEMBER 31, 2018**  
(Dollars in Thousands)

	COMMUNITY FIRST BANCORP.	COMMUNITY FIRST BANK	HFG TRUST, LLC	ELIMINATIONS	CONSOLIDATED BALANCES 2018
<b>Interest income</b>					
Interest and fees on loans	\$ -	\$ 8,856	\$ -	\$ -	\$ 8,856
Interest on investment securities	-	1,538	-	-	1,538
Interest on federal funds sold and interest-bearing deposits with financial institutions	-	410	-	-	410
Total interest income	-	10,804	-	-	10,804
<b>Interest expense</b>					
On deposits	-	455	-	-	455
On borrowed funds	-	22	-	-	22
Total interest expense	-	477	-	-	477
Net interest income	-	10,327	-	-	10,327
Provision for loan losses	-	203	-	-	203
Net interest income after provision for loan losses	-	10,124	-	-	10,124
<b>Non-interest income</b>					
Service charges and fees on deposit accounts	-	309	-	-	309
Equity in undistributed income of subsidiary	2,328	263	-	(2,591)	-
Dividend income from subsidiary	1,200	-	-	(1,200)	-
Mortgage broker fees	-	14	-	-	14
Earnings on bank-owned life insurance	-	172	-	-	172
Gain on sales of investment securities (includes \$33,000 of accumulated other comprehensive income reclassifications for unrealized gains on available-for-sale securities)	-	19	-	-	19
Net gain on sales of loans	-	630	-	-	630
Income from fiduciary activities	-	-	3,771	-	3,771
Other	-	956	41	-	997
Total non-interest income	3,528	2,363	3,812	(3,791)	5,912
<b>Non-interest expense</b>					
Salaries and employee benefits	5	5,670	2,802	-	8,477
Occupancy	1	552	150	-	703
Furniture and equipment	49	363	49	-	461
Data processing	13	417	8	-	438
Professional fees	26	280	37	-	343
Other operating expenses	(53)	1,677	503	-	2,127
Total non-interest expense	41	8,959	3,549	-	12,549
<b>Net Income</b>	<b>\$ 3,487</b>	<b>\$ 3,528</b>	<b>\$ 263</b>	<b>\$ (3,791)</b>	<b>\$ 3,487</b>

See Independent Auditor's Report.

**COMMUNITY FIRST BANK  
BALANCE SHEETS  
(BANK ONLY)  
DECEMBER 31, 2018 AND 2017  
(Dollars in Thousands)**

	<b>2018</b>	<b>2017</b>
<b>ASSETS</b>		
Cash and cash equivalents:		
Cash and due from banks	\$ 5,964	\$ 8,746
Interest-bearing deposits in financial institutions maturing in less than three months	34,995	30,748
Total cash and cash equivalents	40,959	39,494
Interest-bearing deposits in financial institutions maturing in more than three months	984	5,168
Investment in subsidiary	3,970	3,707
Investment securities	71,279	70,331
Federal Home Loan Bank stock, at cost	366	348
Loans held-for-sale	1,176	-
Loans, net of deferred loans fees and allowance for loan losses	190,156	172,482
Premises and equipment, net of accumulated depreciation	6,829	5,588
Bank-owned life insurance	6,410	6,238
Accrued interest receivable	1,104	964
Other assets	791	502
<b>Total Assets</b>	<b>\$ 324,024</b>	<b>\$ 304,822</b>
 <b>LIABILITIES</b>		
Deposits	\$ 290,759	\$ 273,417
Other liabilities:		
Accrued interest payable	27	20
Accrued expenses and other liabilities	185	132
Total other liabilities	212	152
<b>Total Liabilities</b>	<b>290,971</b>	<b>273,569</b>
 <b>SHAREHOLDER'S EQUITY</b>		
Common stock, \$1 par value:		
Authorized - 1,000,000 shares		
Issued and outstanding - 400,630 shares	401	401
Additional paid-in capital	14,647	14,508
Retained earnings	18,636	16,308
Accumulated other comprehensive income (loss)	(631)	36
<b>Total Shareholder's Equity</b>	<b>33,053</b>	<b>31,253</b>
<b>Total Liabilities and Shareholder's Equity</b>	<b>\$ 324,024</b>	<b>\$ 304,822</b>

See Independent Auditor's Report.

**COMMUNITY FIRST BANK**  
**STATEMENTS OF INCOME**  
**(BANK ONLY)**  
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**  
**(Dollars in Thousands)**

	<b>2018</b>	<b>2017</b>
<b>Interest income</b>		
Interest and fees on loans	\$ 8,856	\$ 7,967
Interest on investment securities	1,538	1,349
Interest on federal funds sold and interest-bearing deposits with financial institutions	410	287
Total interest income	10,804	9,603
<b>Interest expense</b>		
On deposits	455	354
On borrowed funds	22	10
Total interest expense	477	364
Net interest income	10,327	9,239
Provision for loan losses	203	80
Net interest income after provision for loan losses	10,124	9,159
<b>Non-interest income</b>		
Service charges and fees on deposit accounts	309	295
Equity in undistributed income of subsidiary	263	381
Mortgage broker fees	14	8
Earnings on bank-owned life insurance	172	176
Gain on sales of investment securities (includes \$33,000 and \$32,000 of accumulated other comprehensive income reclassifications for 2018 and 2017, respectively for unrealized gains on available-for-sale securities)	19	37
Net gain on sales of loans	630	58
Net loss on sales of premises and equipment	-	(2)
Other	956	502
Total non-interest income	2,363	1,455
<b>Non-interest expense</b>		
Salaries and employee benefits	5,670	4,164
Occupancy	552	490
Furniture and equipment	363	322
Data processing	417	373
Professional fees	280	279
Other operating expenses	1,677	1,291
Total non-interest expense	8,959	6,919
<b>Net Income</b>	<b>\$ 3,528</b>	<b>\$ 3,695</b>

See Independent Auditor's Report.

**COMMUNITY FIRST BANK**  
**STATEMENTS OF CHANGES IN SHAREHOLDER'S EQUITY**  
**(BANK ONLY)**  
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**  
**(Dollars in Thousands)**

	<u>Common Stock</u>	<u>Additional Paid-In Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Total</u>
<b>Balance at January 1, 2017</b>	\$ 401	\$ 14,453	\$ 13,503	\$ 43	\$ 28,400
Restricted stock compensation expense		1			1
Directors stock compensation expense		54			54
Net income for the year ended December 31, 2017			3,695		3,695
Unrealized loss on available-for- sale securities				(7)	(7)
Dividends paid - \$2.22 per share			(890)		(890)
<b>Balance at December 31, 2017</b>	401	14,508	16,308	36	31,253
Stock option compensation expense		1			1
Restricted stock compensation expense		90			90
Directors stock compensation expense		48			48
Net income for the year ended December 31, 2018			3,528		3,528
Unrealized loss on available-for- sale securities				(667)	(667)
Dividends paid - \$3.00 per share			(1,200)		(1,200)
<b>Balance at December 31, 2018</b>	<u>\$ 401</u>	<u>\$ 14,647</u>	<u>\$ 18,636</u>	<u>\$ (631)</u>	<u>\$ 33,053</u>

See Independent Auditor's Report.

**COMMUNITY FIRST BANK**  
**STATEMENTS OF CASH FLOWS**  
**(BANK ONLY)**  
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**  
**(Dollars in Thousands)**

	<u>2018</u>	<u>2017</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$ 3,528	\$ 3,695
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	521	385
Provision for loan losses	203	80
Equity in undistributed income of subsidiary	(263)	(381)
Net amortization on investment securities	704	558
Stock option compensation expense	1	-
Restricted stock compensation expense	90	1
Directors stock compensation expense	48	54
Earnings on bank-owned life insurance	(172)	(176)
Originations of loans held-for-sale	(34,310)	(3,492)
Proceeds from sales of loans held-for-sale	33,764	3,942
Net gain on sales of loans	(630)	(58)
Gain on sales of investment securities	(19)	(37)
Net loss on sales of premises and equipment	-	2
Increase in net deferred loan fees	113	54
Increase in accrued interest receivable	(140)	(146)
Increase (decrease) in accrued interest payable	7	(7)
Other	(312)	(235)
Total adjustments	<u>(395)</u>	<u>544</u>
<b>Net Cash Provided by Operating Activities</b>	<u>3,133</u>	<u>4,239</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Decrease in interest-bearing deposits in financial institutions maturing in more than three months	4,184	3,561
Purchases of investment securities:		
Available-for-sale	(17,907)	(12,862)
Proceeds from maturities and calls of investment securities:		
Available-for-sale	11,135	9,365
Proceeds from principal paydowns on investment securities:		
Available-for-sale	2,500	3,028
Proceeds from sales of investment securities:		
Available-for-sale	1,973	2,642
Purchases of FHLB stock	(1,817)	(68)
Proceeds from redemptions of FHLB stock	1,799	63
Net increase in loans made to customers	(17,990)	(18,418)
Proceeds from sales of premises and equipment	-	1
Purchases of premises and equipment	<u>(1,686)</u>	<u>(3,123)</u>
<b>Net Cash Used by Investing Activities</b>	<u>\$ (17,809)</u>	<u>\$ (15,811)</u>

See Independent Auditor's Report.

**COMMUNITY FIRST BANK**  
**STATEMENTS OF CASH FLOWS, Continued**  
**(BANK ONLY)**  
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**  
**(Dollars in Thousands)**

	<b>2018</b>	<b>2017</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net increase in demand deposits, interest-bearing transaction accounts and savings	\$ 17,103	\$ 15,203
Net increase (decrease) in time deposits	238	(2,449)
Repayment of FHLB borrowings	-	(500)
Dividends paid	(1,200)	(890)
<b>Net Cash Provided by Financing Activities</b>	<b>16,141</b>	<b>11,364</b>
<b>Net increase in cash and cash equivalents</b>	1,465	11,364
<b>Cash and cash equivalents at beginning of year</b>	39,494	28,130
<b>Cash and cash equivalents at end of year</b>	\$ 40,959	\$ 39,494
 <b>SUPPLEMENTAL SCHEDULE OF OPERATING AND INVESTING ACTIVITIES:</b>		
Interest paid	\$ 470	\$ 371