COMMUNITY WEST BANCSHARES /
Form 10-Q
May 03, 2019

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

FORM 10-Q

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

For the quarterly period ended March 31, 2019 or

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

For the transition period from _________ to _________

Commission File Number: 000-23575

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

California	77-0446957
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

445 Pine Avenue, Goleta, California	93117
(Address of principal executive offices)	(Zip Code)

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

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). YES NO

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

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

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.
Common stock of the registrant issued and outstanding of 8,449,886 as of April 30, 2019.

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock	CWBC	NASDAQ

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

COMMUNITY WEST BANCSHARES
CONSOLIDATED BALANCE SHEETS

	March 31, 2019 (unaudited)	December 31, 2018
	(in thousands, except share amounts)	
Assets:		
Cash and due from banks	$ 1,900	$ 2,975
Federal funds sold	7	8
Interest-earning demand in other financial institutions	51,499	53,932
Cash and cash equivalents	53,406	56,915
Investment securities - available-for-sale, at fair value; amortized cost of $24,557 at March 31, 2019 and $25,222 at December 31, 2018	24,344	24,931
Investment securities - held-to-maturity, at amortized cost; fair value of $7,153 at March 31, 2019 and $7,269 at December 31, 2018	7,073	7,301
Investment securities - measured at fair value; amortized cost of $66 at March 31, 2019 and December 31, 2018.	145	121
Federal Home Loan Bank stock, at cost	2,714	2,714
Federal Reserve Bank stock, at cost	1,373	1,373
Loans:		
Held for sale, at lower of cost or fair value	46,995	48,355
Held for investment, net of allowance for loan losses of $8,648 at March 31, 2019 and $8,691 at December 31, 2018	714,423	711,197
Total loans	761,418	759,552
Premises and equipment, net	6,194	6,381
Other assets	25,727	18,003
Total assets	$ 882,394	$ 877,291
Liabilities:		
Deposits:		
Non-interest-bearing demand	$ 135,495	$ 108,161
Interest-bearing demand	287,095	270,431
Savings	15,128	14,641
Certificates of deposit ($250,000 or more)	91,580	93,439
Other certificates of deposit	205,431	229,334
Total deposits	734,729	716,006
Other borrowings	52,750	75,000
Other liabilities	18,462	10,134
Total liabilities	805,941	801,140
Stockholders' equity:		
Common stock — no par value, 60,000,000 shares authorized; 8,449,886 shares issued and outstanding at March 31, 2019 and 8,533,346 at December 31, 2018	42,173	42,964
Retained earnings	34,414	33,328
Accumulated other comprehensive (loss)	(134)	(141)

Total stockholders’ equity	76,453	76,151
Total liabilities and stockholders’ equity	$ 882,394	$ 877,291

See the accompanying notes.

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COMMUNITY WEST BANCSHARES
CONSOLIDATED INCOME STATEMENTS (unaudited)

	Three Months Ended March 31, 2019	2018
Interest income:	(in thousands, except per share amounts)	
Loans, including fees	$ 10,541	$ 9,651
Investment securities and other	484	337
Total interest income	11,025	9,988
Interest expense:		
Deposits	2,444	1,443
Other borrowings	358	195
Total interest expense	2,802	1,638
Net interest income	8,223	8,350
(Credit) provision for loan losses	(57)	(144)
Net interest income after provision for loan losses	8,280	8,494
Non-interest income:		
Other loan fees	258	296
Document processing fees	87	117
Service charges	139	116
Other	120	110
Total non-interest income	604	639
Non-interest expenses:		
Salaries and employee benefits	4,381	4,149
Occupancy, net	782	784
Professional services	381	304
Data processing	224	212
FDIC assessment	170	214
Depreciation	213	167
Advertising and marketing	129	170
Stock based compensation	95	116
Other	342	417
Total non-interest expenses	6,717	6,533
Income before provision for income taxes	2,167	2,600
Provision for income taxes	657	786
Net income	$ 1,510	$ 1,814
Earnings per share:		
Basic	$ 0.18	$ 0.22
Diluted	$ 0.18	$ 0.21
Weighted average number of common shares outstanding:		
Basic	8,491	8,209
Diluted	8,604	8,686
Dividends declared per common share	$ 0.050	$ 0.040

See the accompanying notes.

COMMUNITY WEST BANCSHARES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (unaudited)

	Three Months Ended March 31,	
	2019	2018
	(in thousands)	
Net income	$ 1,510	$ 1,814
Other comprehensive income, net:		
Unrealized (loss) income on securities available-for-sale (AFS), net (tax effect of ($5) and $27 for each respective period presented)	7	(39)
Net other comprehensive (loss) income	7	(39)
Comprehensive income	$ 1,517	$ 1,775

See the accompanying notes.

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COMMUNITY WEST BANCSHARES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (unaudited)

	Common Stock Shares	Common Stock Amount	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Stockholders' Equity
	(in thousands)				
Balance, December 31, 2018:	8,533	$42,964	$ (141)	$33,328	$ 76,151
Net income	—	—	—	1,510	1,510
Exercise of stock options	6	43	—	—	43
Stock based compensation	—	95	—	—	95
Common stock repurchase	(89)	(929)	—	—	(929)
Dividends on common stock	—	—	—	(424)	(424)
Other comprehensive income, net	—	—	7	—	7
Balance, March 31, 2019	8,450	$42,173	$ (134)	$34,414	$ 76,453

	Common Stock Shares	Common Stock Amount	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Stockholders' Equity
	(in thousands)				
Balance, December 31, 2017:	8,193	$42,604	$ 25	$27,441	$ 70,070
Net income	—	—	—	1,814	1,814
Exercise of stock options	23	78	—	—	78
Stock based compensation	—	116	—	—	116
Dividends on common stock	—	—	—	(328)	(328)
Other comprehensive income, net	—	—	(39)	—	(39)
Impact of ASU 2016-01 and 2018-02 as of January 1, 2018	—	—	(59)	59	—
Balance, March 31, 2018	8,216	$42,798	$ (73)	$28,986	$ 71,711

See the accompanying notes.

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COMMUNITY WEST BANCSHARES
CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

	Three Months Ended March 31,	
	2019	2018
	(in thousands)	
Cash flows from operating activities:		
Net income	$ 1,510	$ 1,814
Adjustments to reconcile net income to cash provided by operating activities:		
(Credit) provision for loan losses	(57)	(144)
Depreciation	213	167
Stock based compensation	95	116
Deferred income taxes	212	(164)
Net accretion of discounts and premiums for investment securities	20	29
Losses/(Gains) on:		
Sale of repossessed assets, net	—	26
Sale of assets, net	7	—
Loans originated for sale and principal collections, net	1,360	2,327
Changes in:		
Investment securities held at fair value	(24)	(18)
Other assets	401	438
Other liabilities	(22)	406
Servicing assets, net	8	46
Net cash provided by operating activities	3,723	5,043
Cash flows from investing activities:		
Principal pay downs and maturities of available-for-sale securities	582	832
Principal pay downs and maturities of held-to-maturity securities	225	452
Loan originations and principal collections, net	(3,169)	(13,412)
Purchase of premises and equipment, net	(33)	(292)
Proceeds from sale of other real estate owned and repossessed assets, net	—	214
Net cash used in investing activities	(2,395)	(12,206)
Cash flows from financing activities:		
Net increase in deposits	18,723	10,353
Net (decrease) increase in borrowings	(22,250)	20,000
Exercise of stock options	43	78
Cash dividends paid on common stock	(424)	(328)
Common stock repurchase	(929)	—
Net cash (used in) provided by financing activities	(4,837)	30,103
Net (decrease) increase cash and cash equivalents	(3,509)	22,940
Cash and cash equivalents at beginning of period	56,915	45,869
Cash and cash equivalents at end of period	$ 53,406	$ 68,809
Supplemental disclosure:		
Cash paid during the period for:		
Interest	$ 2,521	$ 219
Non-cash investing and financing activity:		
Transfers to other assets acquired through foreclosure, net	-	101
Operating lease right-of-use asset	(8,350)	—
Operating lease liability	8,350	—

See the accompanying notes.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

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

Basis of Presentation

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

Use of Estimates

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

Interim Financial Information

The accompanying unaudited consolidated financial statements as of and for the three months ended March 31, 2019 and 2018 have been prepared in a condensed format, and therefore do not include all of the information and footnotes required by GAAP for complete financial statements. These statements have been prepared on a basis that is substantially consistent with the accounting principles applied to our audited consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2018.

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

Reclassifications

Certain amounts in the consolidated financial statements as of December 31, 2018 and for the three months ended March 31, 2018 have been reclassified to conform to the current presentation. The reclassifications have no effect on net income, comprehensive income or stockholders' equity as previously reported.

Loans Held For Sale

Loans which are originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value determined on an aggregate basis. Valuation adjustments, if any, are recognized through a valuation allowance by charges to lower of cost or fair value provision. Loans held for sale are mostly comprised of commercial agriculture and Small Business Administration ("SBA"). The Company did not incur any lower of cost or fair value provision in the three months ended March 31, 2019 and 2018.

Loans Held for Investment and Interest and Fees from Loans

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

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

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

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

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

Impaired loans: A loan is considered impaired when, based on current information, it is probable that the Company will be unable to collect the scheduled payments of principal and/or interest under the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and/or interest payments. Loans that experience insignificant payment delays or payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays or payment shortfalls on a case-by-case basis. When determining the possibility of impairment, management considers the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. For collateral-dependent loans, the Company uses the fair value of collateral method to measure impairment. The collateral-dependent loans that recognize impairment are charged down to the fair value less costs to sell. All other loans are measured for impairment either based on the present value of future cash flows or the loan's observable market price.

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

Allowance for Loan Losses and Provision for Loan Losses

The Company maintains a detailed, systematic analysis and procedural discipline to determine the amount of the allowance for loan losses ("ALL"). The ALL is based on estimates and is intended to be appropriate to provide for probable losses inherent in the loan portfolio. This process involves deriving probable loss estimates that are based on migration analysis and historical loss rates, in addition to qualitative factors that are based on management's judgment. The migration analysis and historical loss rate calculations are based on the annualized loss rates utilizing a twelve-quarter loss history. Migration analysis is utilized for the Commercial Real Estate ("CRE"), Commercial, Commercial Agriculture, SBA, Home Equity Line of Credit ("HELOC"), Single Family Residential, and Consumer portfolios. The historical loss rate method is utilized primarily for the Manufactured Housing portfolio. The migration analysis takes into account the risk rating of loans that are charged off in each loan category. Loans that are considered Doubtful are typically charged off. The following is a description of the characteristics of loan ratings. Loan ratings are reviewed as part of our normal loan monitoring process, but, at a minimum, updated on an annual basis.

Substantially Risk Free – These borrowers have virtually no probability of default or loss given default and present no identifiable or potential adverse risk to the Company. Documented repayment is either backed by the full faith and credit of the United States Government, or secured by cash collateral. The collateral must be in the possession of the Company and free from potential claim. In addition, these credits will conform in all aspects to established loan policies and procedures, laws, rules, and regulations.

Nominal Risk – This rating is for the highest quality borrowers with nominal probability of default or loss given default from the transaction. Typically this is a borrower with a well-established record of financial performance, a strong equity position, abundant liquidity and excellent debt service ability. The Borrower's financial outlook is stable due to a broad range of operations or products and is able to weather an economic downturn without significant impact to liquidity or net worth. Typically, this borrower will be publicly owned or have access to public debt or equity, all investment grade. In addition, these credits will conform in all aspects to established loan policies and procedures, laws, rules, and regulations. Transaction can include marketable securities as collateral, properly margined.

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Pass/Management Attention Risk – The loans in the four remaining pass categories range from minimal risk to moderate risk to acceptable risk to management attention risk. Loans rated in the first three categories are acceptable loans, appropriately underwritten, bearing an ordinary risk of loss to the Company. Loans in the minimal and moderate risk categories are loans to quality borrowers with financial statements presenting a good primary source as well as an adequate secondary source of repayment. In the case of individuals, borrowers with this rating are quality borrowers demonstrating a reasonable level of secure income, a net worth adequate to support the loan and presenting a good primary source as well as an adequate secondary source of repayment. Loans rated acceptable risk in the management attention risk category indicate that although the borrower meets the criteria for a rating of acceptable risk or better, the credit possesses an identified and elevated risk level that should be resolved in a short period of time. Technical risks include, but are not limited to, inadequate or improperly executed documentation, which may be material, serious delays in the submission of financial reporting or covenant violations that are not indicative of a protracted trend.

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

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

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

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

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

Commercial, CRE and SBA Loans

Charge-offs on these loan categories are taken as soon as all or a portion of any loan balance is deemed to be uncollectible. A loan is considered impaired when, based on current information, it is probable that the Company will be unable to collect the scheduled payments of principal and/or interest under the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and/or interest payments. Loans that experience insignificant payment delays or payment shortfalls generally are not classified as impaired. Generally, loan balances are charged-down to the fair value of the collateral, if, based on a current assessment of the value, an apparent deficiency exists. In the event there is no perceived equity, the loan is charged-off in full. Unsecured loans which are delinquent over 90 days are, without clear support, also charged-off in full.

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

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

Consumer Loans

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

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

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

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

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

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

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

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

- Concentrations of credit
- International risk
- Trends in volume, maturity, and composition of loans
- Volume and trend in delinquency, nonaccrual, and classified assets
- Economic conditions
- Geographic distance
- Policy and procedures or underwriting standards
- Staff experience and ability

- Value of underlying collateral
- Competition, legal, or regulatory environment
- Results of outside exams and quality of loan review and Board oversight

Off Balance Sheet and Credit Exposure

In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the consolidated financial statements when they are funded. They involve, to varying degrees, elements of credit risk in excess of amounts recognized in the consolidated balance sheets. Losses would be experienced when the Company is contractually obligated to make a payment under these instruments and must seek repayment from the borrower, which may not be as financially sound in the current period as they were when the commitment was originally made. Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Company enters into credit arrangements that generally provide for the termination of advances in the event of a covenant violation or other event of default. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the party. The commitments are collateralized by the same types of assets used as loan collateral.

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

Foreclosed Real Estate and Repossessed Assets

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

Income Taxes

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

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

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

Earnings Per Share

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

Recent Accounting Pronouncements

Effective January 1, 2019, we adopted Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2016-02, Leases (Topic 842). This update amends the accounting requirements for leases by requiring recognition of lease liabilities and related right-of-use assets on the balance sheet. Lessees are required to recognize a lease liability measured on a discounted basis, which is the lessee's right to use, or control the use of, a specified asset for the lease term. We adopted Topic 842 using the modified retrospective approach as of the effective date, January 1, 2019. We have recorded the cumulative effects on our balance sheet as of the effective date. No adjustments were made to prior comparative periods. As a result of the adoption, there was no impact on net income. We recorded operating lease right-of-use assets of $8.4 million and lease liabilities of $8.4 million. As part of the adoption, we elected the package of practical expedients permitted under the transition guidance within Topic 842, which among other things, allowed us to carry forward the historical lease classifications. Leases with a term of 12 months or less are not recorded on the balance sheet. See Note 11, Leases for further information.

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

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In March 2017, the FASB issued updated guidance codified within ASU-2017-08, "Receivables – Nonrefundable Fees and Other Costs (Subtopic 310-20)," which is intended to enhance the accounting for the amortization of premiums for purchased callable debt securities. The standard is effective for the Company as of January 1, 2019. The Company adopted this guidance as of January 1, 2019, which did not have a material impact on the Company's Consolidated Financial Statements.

2. INVESTMENT SECURITIES

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

	March 31, 2019			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
Securities available-for-sale	(in thousands)			
U.S. government agency notes	$11,911	$ —	$ (143)	$11,768
U.S. government agency collateralized mortgage obligations ("CMO")	12,646	9	(79)	12,576
Total	$24,557	$ 9	$ (222)	$24,344
Securities held-to-maturity				
U.S. government agency mortgage backed securities ("MBS")	$7,073	$ 164	$ (84)	$7,153
Total	$7,073	$ 164	$ (84)	$7,153
Securities measured at fair value				
Equity securities: Farmer Mac class A stock	$66	$ 79	$ —	$145
Total	$66	$ 79	$ —	$145

	December 31, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
Securities available-for-sale	(in thousands)			
U.S. government agency notes	$12,225	$ —	$ (155)	$12,070
U.S. government agency collateralized mortgage obligations ("CMO")	12,931	9	(79)	12,861
Total	$25,156	$ 9	$ (234)	$24,931
Securities held-to-maturity				
U.S. government agency mortgage backed securities ("MBS")	$7,301	$ 118	$ (150)	$7,269
Total	$7,301	$ 118	$ (150)	$7,269
Securities measured at fair value	$66	$ 55	$ —	$121
Equity securities: Farmer Mac class A stock	$66	$ 55	$ —	$121
Total				

At March 31, 2019 and December 31, 2018, $31.4 million and $32.2 million of securities at carrying value, respectively, were pledged to the Federal Home Loan Bank ("FHLB"), as collateral for current and future advances.

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

	March 31, 2019									
	Less than One Year		One to Five Years		Five to Ten Years		Over Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Securities available-for-sale	(dollars in thousands)									
U.S. government agency notes	$1,947	2.6 %	$ 1,365	2.8 %	$ 8,457	3.3 %	$—	—	$11,769	3.1 %
U.S. government agency CMO	—	—	2,609	2.6 %	7,099	2.9 %	2,867	3.4 %	12,575	3.0 %
Total	$1,947	2.6 %	$ 3,974	2.7 %	$ 15,556	3.1 %	$ 2,867	3.4 %	$24,344	3.0 %
Securities held-to-maturity										
U.S. government agency MBS	$—	—	$ 2,183	4.6 %	$ 4,100	3.2 %	$ 790	3.6 %	$7,073	3.7 %
Total	$—	—	$ 2,183	4.6 %	$ 4,100	3.2 %	$ 790	3.6 %	$7,073	3.7 %
Securities measured at fair value										
Farmer Mac class A stock	$—	—	$ —	—	$ —	—	$—	—	$ 145	—
Total	$—	—	$ —	—	$ —	—	$—	—	$ 145	—

	December 31, 2018									
	Less than One Year		One to Five Years		Five to Ten Years		Over Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Securities available-for-sale	(dollars in thousands)									
U.S. government agency notes	$1,946	2.6 %	$ 1,388	2.6 %	$ 8,736	3.1 %	$—	—	$12,070	2.0 %
U.S. government agency CMO	—	—	2,717	2.5 %	7,284	2.8 %	2,860	3.2 %	12,861	1.9 %
Total	$1,946	2.6 %	$ 4,105	2.5 %	$ 16,020	3.0 %	$ 2,860	3.2 %	$24,931	2.0 %
Securities held-to-maturity										
U.S. government agency MBS	$—	—	$ 2,058	4.7 %	$ 4,449	3.2 %	$ 794	3.6 %	$7,301	3.3 %
Total	$—	—	$ 2,058	4.7 %	$ 4,449	3.2 %	$ 794	3.6 %	$7,301	3.3 %
Securities measured at fair value										
Farmer Mac class A stock	$—	—	$ —	—	$ —	—	$—	—	$ 121	—
Total	$—	—	$ —	—	$ —	—	$—	—	$ 121	—

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

	March 31, 2019		December 31, 2018	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Securities available-for-sale	(in thousands)			
Due in one year or less	$1,998	$ 1,947	$1,998	$ 1,946
After one year through five years	3,998	3,974	4,138	4,105
After five years through ten years	15,647	15,556	16,107	16,020
After ten years	2,914	2,867	2,913	2,860
Total	$24,557	$ 24,344	$25,156	$ 24,931
Securities held-to-maturity				
Due in one year or less	$—	$ —	$—	$ —
After one year through five years	2,183	2,275	2,058	2,153
After five years through ten years	4,100	4,053	4,449	4,323
After ten years	790	825	794	793
Total	$7,073	$ 7,153	$7,301	$ 7,269
Securities measured at fair value				
Farmer Mac class A stock	$66	$ 145	$66	$ 121
Total	$66	$ 145	$66	$ 121

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

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

	March 31, 2019					
	Less Than Twelve Months		More Than Twelve Months		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Securities available-for-sale	(in thousands)					
U.S. government agency notes	$6	$2,176	$ 137	$ 9,593	$143	$11,769
U.S. government agency CMO	18	5,940	61	3,215	79	9,155
Total	$24	$8,116	$ 198	$ 12,808	$222	$20,924
Securities held-to-maturity						
U.S. Government-agency MBS	$—	$—	$ 84	$ 2,619	$84	$2,619
Total	$—	$—	$ 84	$ 2,619	$84	$2,619
Securities measured at fair value						
Farmer Mac class A stock	$—	$—	$ —	$ —	$—	$—
Total	$—	$—	$ —	$ —	$—	$—

	December 31, 2018					
	Less Than Twelve Months		More Than Twelve Months		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Securities available-for-sale	(in thousands)					
U.S. government agency notes	$21	$4,001	$ 134	$ 8,070	$155	$12,071
U.S. government agency CMO	2	4,749	77	3,289	79	8,038
Equity securities: Farmer Mac class A stock	—	—	—	—	—	—
Total	$23	$8,750	$ 211	$ 11,359	$234	$20,109
Securities held-to-maturity						
U.S. Government-agency MBS	$10	$1,706	$ 140	$ 2,094	$150	$3,800
Total	$10	$1,706	$ 140	$ 2,094	$150	$3,800
Securities measured at fair value						
Farmer Mac class A stock	$—	$—	$ —	$ —	$—	$—
Total	$—	$—	$ —	$ —	$—	$—

As of March 31, 2019 and December 31, 2018, there were 14 and 21 securities, respectively, in an unrealized loss position. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers, among other things: (i) the length of time and the extent to which the fair value has been less than cost; (ii) the financial condition and near-term prospects of the issuer; and (iii) the Company's intent to sell an impaired security and if it is not more likely than not it will be required to sell the security before the recovery of its amortized basis.

The unrealized losses are primarily due to increases in market interest rates over the yields available at the time the underlying securities were purchased. The fair value is expected to recover as the bonds approach their maturity date, repricing date or if market yields for such investments decline. Management does not believe any of the securities are impaired due to reasons of credit quality. Accordingly, as of March 31, 2019 and December 31, 2018, management believes the impairments detailed in the table above are temporary and no other-than-temporary impairment loss has been realized in the Company’s consolidated income statements.

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3. LOANS HELD FOR SALE

SBA and Agriculture Loans

As of March 31, 2019 and December 31, 2018, the Company had approximately $12.8 million and $13.6 million, respectively, of SBA loans included in loans held for sale. As of March 31, 2019 and December 31, 2018, the principal balance of SBA loans serviced for others was $6.5 million and $7.2 million, respectively.

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

As of March 31, 2019 and December 31, 2018, the Company had $34.2 million and $34.8 million of USDA loans included in loans held for sale, respectively. As of March 31, 2019 and December 31, 2018, the principal balance of USDA loans serviced for others was $2.0 million.

4. LOANS HELD FOR INVESTMENT

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

	March 31, 2019	December 31, 2018
	(in thousands)	
Manufactured housing	$248,669	$ 247,114
Commercial real estate	369,206	365,809
Commercial	81,879	83,753
SBA	5,364	5,557
HELOC	6,585	6,756
Single family real estate	11,611	11,261
Consumer	67	46
	723,381	720,296
Allowance for loan losses	(8,648)	(8,691)
Deferred fees, net	(245)	(337)
Discount on SBA loans	(65)	(71)
Total loans held for investment, net	$714,423	$ 711,197

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

	March 31, 2019							
	Current	30-59 Days Past Due	60-89 Days Past Due	Over 90 Days Past Due	Total Past Due	Nonaccrual	Total	Recorded Investment Over 90 Days and Accruing
	(in thousands)							
Manufactured housing	$247,756	$ 699	$ —	$ —	$ 699	$ 214	$248,669	$ —

Commercial real estate:								
Commercial real estate	294,251	—	—	—	—	97	294,348	—
SBA 504 1st trust deed	20,691	251	—	—	251	—	20,942	—
Land	6,542	—	—	—	—	—	6,542	—
Construction	47,374	—	—	—	—	—	47,374	—
Commercial	76,783	305	—	—	305	4,791	81,879	—
SBA	4,332	247	—	—	247	785	5,364	—
HELOC	6,335	56	—	—	56	194	6,585	—
Single family real estate	11,611	—	—	—	—	—	11,611	—
Consumer	67	—	—	—	—	—	67	—
Total	$715,742	$ 1,558	$ —	$ —	$ 1,558	$ 6,081	$723,381	$ —

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	December 31, 2018							
	Current	30-59 Days Past Due	60-89 Days Past Due	Over 90 Days Past Due	Total Past Due	Nonaccrual	Total	Recorded Investment Over 90 Days and Accruing
	(in thousands)							
Manufactured housing	$246,456	$ 285	$ 144	$ —	$ 429	$ 229	$247,114	$ —
Commercial real estate:								
Commercial real estate	267,377	2,478	—	—	2,478	102	269,957	—
SBA 504 1st trust deed	20,835	—	322	—	322	—	21,157	—
Land	6,381	—	—	—	—	—	6,381	—
Construction	67,835	479	—	—	479	—	68,314	—
Commercial	78,857	15	—	—	15	4,881	83,753	—
SBA	4,741	—	—	—	—	816	5,557	—
HELOC	6,558	—	—	—	—	198	6,756	—
Single family real estate	11,221	16	—	24	40	—	11,261	—
Consumer	46	—	—	—	—	—	46	—
Total	$710,307	$ 3,273	$ 466	$ 24	$ 3,763	$ 6,226	$720,296	$ —

Allowance for Loan Losses

The following table summarizes the changes in the allowance for loan losses:

	Three Months Ended March 31,	
	2019	2018
	(in thousands)	
Beginning balance	$ 8,691	$ 8,420
Charge-offs	(17)	(6)
Recoveries	31	188
Net recoveries	14	182
Provision (credit)	(57)	(144)
Ending balance	$ 8,648	$ 8,458

As of March 31, 2019 and December 31, 2018, the Company had reserves for credit losses on undisbursed loans of $87,000 and $73,000, respectively, which were included in other liabilities.

The following tables summarize the changes in the allowance for loan losses by portfolio type:

	For the Three Months Ended March 31,							
	Manufactured Housing	Commercial Real Estate	Commercial	SBA	HELOC	Single Family Real Estate	Consumer	Total
2019	(in thousands)							

Beginning balance	$2,196	$ 5,028	$ 1,210	$79	$ 90	$ 88	$ —	$8,691
Charge-offs	—	—	(17)	—	—	—	—	(17)
Recoveries	6	—	19	5	1	—	—	31
Net (charge-offs) recoveries	6	—	2	5	1	—	—	14
Provision (credit)	(14)	30	7	(40)	(43)	3	—	(57)
Ending balance	$2,188	$ 5,058	$ 1,219	$44	$ 48	$ 91	$ —	$8,648
2018								
Beginning balance	$2,180	$ 4,844	$ 1,133	$73	$ 92	$ 98	$ —	$8,420
Charge-offs	(6)	—	—	—	—	—	—	(6)
Recoveries	99	15	5	62	7	—	—	188
Net (charge-offs) recoveries	93	15	5	62	7	—	—	182
Provision (credit)	(171)	117	(11)	(74)	(6)	1	—	(144)
Ending balance	$2,102	$ 4,976	$ 1,127	$61	$ 93	$ 99	$ —	$8,458

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The following tables present impairment method information related to loans and allowance for loan losses by loan portfolio segment:

	Manufactured Housing	Commercial Real Estate	Commercial	SBA	HELOC	Single Family Real Estate	Consumer	Total Loans
Loans Held for Investment as of March 31, 2019:	(in thousands)							
Recorded Investment:								
Impaired loans with an allowance recorded	$6,299	$ 241	$ 3,475	$—	$ —	$ 770	$ —	$10,785
Impaired loans with no allowance recorded	2,755	97	4,064	785	193	1,798	—	9,692
Total loans individually evaluated for impairment	9,054	338	7,539	785	193	2,568		