**Board of Governors of the Federal Reserve System**

# Annual Report of Holding Companies—FR Y-6

## Report at the close of business as of the end of fiscal year

This Report is required by law: Section 5(c)(1)(A) of the Bank Holding Company Act (12 U.S.C. § 1844(c)(1)(A)); sections 8(a) and 13(a) of the International Banking Act (12 U.S.C. §§ 3106(a) and 3108(a)); sections 11(a)(1), 25, and 25A of the Federal Reserve Act (12 U.S.C. §§ 248(a)(1), 602, and 611a); and sections 113, 165, 312, 618, and 809 of the Dodd-Frank Act (12 U.S.C. §§ 5361, 5365, 5412, 1850a(c)(1), and 5468(b)(1)). Return to the appropriate Federal Reserve Bank the original and the number of copies specified.

This report form is to be filed by all top-tier bank holding companies, top-tier savings and loan holding companies, and U.S. intermediate holding companies organized under U.S. law, and by any foreign banking organization that does not meet the requirements of and is not treated as a qualifying foreign banking organization under Section 211.23 of Regulation K (12 C.F.R. § 211.23). (See page one of the general instructions for more detail of who must file.) The Federal Reserve may not conduct or sponsor, and an organization (or a person) is not required to respond to, an information collection unless it displays a currently valid OMB control number.

NOTE: The *Annual Report of Holding Companies* must be signed by one director of the top-tier holding company. This individual should also be a senior official of the top-tier holding company. In the event that the top-tier holding company does not have an individual who is a senior official and is also a director, the chairman of the board must sign the report. If the holding company is an ESOP/ESOT formed as a corporation or is an LLC, see the General Instructions for the authorized individual who must sign the report.

I, C. Ronald Christmas
Name of the Holding Company Director and Official

Vice Chairman and CEO
Title of the Holding Company Director and Official

attest that the *Annual Report of Holding Companies* (including the supporting attachments) for this report date has been prepared in conformance with the instructions issued by the Federal Reserve System and are true and correct to the best of my knowledge and belief.

*With respect to information regarding individuals contained in this report, the Reporter certifies that it has the authority to provide this information to the Federal Reserve. The Reporter also certifies that it has the authority, on behalf of each individual, to consent or object to public release of information regarding that individual. The Federal Reserve may assume, in the absence of a request for confidential treatment submitted in accordance with the Board's "Rules Regarding Availability of Information," 12 C.F.R. Part 261, that the Reporter* ***and*** *individual consent to public release of all details in the report concerning that individual.*

C. Ronald Christmas
Signature of Holding Company Director and Official

3/27/2018
Date of Signature

*For holding companies* ***not*** *registered with the SEC–*
Indicate status of Annual Report to Shareholders:
- ☐ is included with the FR Y-6 report
- ☒ will be sent under separate cover
- ☐ is not prepared

**For Federal Reserve Bank Use Only**
RSSD ID 3299140
C.I.

**Date of Report** (top-tier holding company's fiscal year-end):
December 31, 2017
Month / Day / Year

n/a
Reporter's Legal Entity Identifier (LEI) (20-Character LEI Code)

Reporter's Name, Street, and Mailing Address

Palmetto Heritage Bancshares, Inc.
Legal Title of Holding Company

PO Box 3788
(Mailing Address of the Holding Company) Street / P.O. Box

| City | State | Zip Code |
|---|---|---|
| Pawleys Island | SC | 29585 |

10919 Ocean Highway Pawleys Island, SC 29585
Physical Location (if different from mailing address)

Person to whom questions about this report should be directed:

| Name | Title |
|---|---|
| Dustin G. Formo | Chief Operations Officer |

843-237-7776
Area Code / Phone Number / Extension

843-237-7710
Area Code / FAX Number

dformo@palmettoheritagebank.com
E-mail Address

Address (URL) for the Holding Company's web page

Is confidential treatment requested for any portion of this report submission? .......... 0=No 1=Yes: 0

In accordance with the General Instructions for this report (check only one),
1. a letter justifying this request is being provided along with the report .......... ☐
2. a letter justifying this request has been provided separately ... ☐

NOTE: Information for which confidential treatment is being requested must be provided separately and labeled as "confidential."

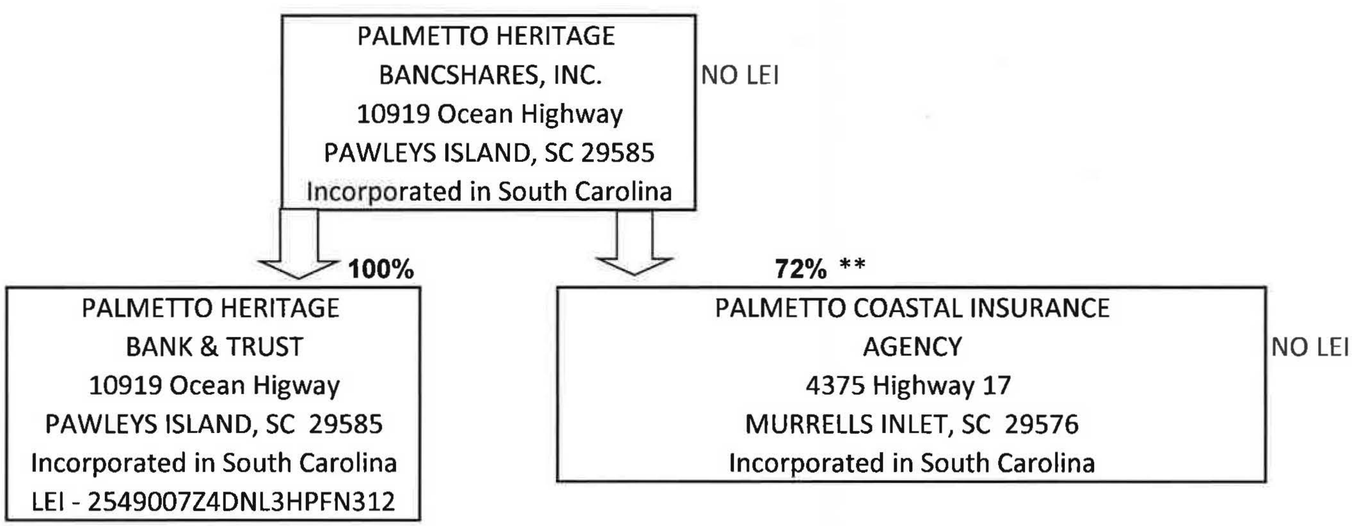
Public reporting burden for this information collection is estimated to vary from 1.3 to 101 hours per response, with an average of 5.50 hours per response, including time to gather and maintain data in the required form and to review instructions and complete the information collection. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden to: Secretary, Board of Governors of the Federal Reserve System, 20th and C Streets, NW, Washington, DC 20551, and to the Office of Management and Budget, Paperwork Reduction Project (7100-0297), Washington, DC 20503.

# FORM FR Y-6
# PALMETTO HERITAGE BANCSHARES, INC.
# PAWLEYS ISLAND, SC
# Fiscal Year Ending December 31, 2017
# Report Item 2a Organizational Chart

Report Item 2a

1. The bank holding company will prepare an annual report for its shareholders to be mailed by March 31, 2018.
   A 2017 Annual Report will be submitted upon receipt from printer in March 2018.

2. Organizational Chart




** 28% OWNED BY PRESIDENT OF PALMETTO COASTAL INSURANCE AGENCY INC., CHARLES ROBERT LOWE

**Results: A list of branches for your holding company: PALMETTO HERITAGE BANCSHARES, INC. (3299140) of PAWLEYS ISLAND, SC.**
The data are as of 12/31/2017. Data reflects information that was received and processed through 01/04/2018.

**Reconciliation and Verification Steps**
1. In the **Data Action** column of each branch row, enter one or more of the actions specified below
2. If required, enter the date in the **Effective Date** column

**Actions**
**OK:** If the branch information is correct, enter 'OK' in the **Data Action** column.
**Change:** If the branch information is incorrect or incomplete, revise the data, enter 'Change' in the **Data Action** column and the date when this information first became valid in the **Effective Date** column.
**Close:** If a branch listed was sold or closed, enter 'Close' in the **Data Action** column and the sale or closure date in the **Effective Date** column.
**Delete:** If a branch listed was never owned by this depository institution, enter 'Delete' in the **Data Action** column.
**Add:** If a reportable branch is missing, insert a row, add the branch data, and enter 'Add' in the **Data Action** column and the opening or acquisition date in the **Effective Date** column.

If printing this list, you may need to adjust your page setup in MS Excel. Try using landscape orientation, page scaling, and/or legal sized paper.

**Submission Procedure**
When you are finished, send a saved copy to your FRB contact. See the detailed instructions on this site for more information.
If you are e-mailing this to your FRB contact, put your institution name, city and state in the subject line of the e-mail.

Note:
To satisfy the **FR Y-10 reporting requirements**, you must also submit FR Y-10 Domestic Branch Schedules for each branch with a **Data Action** of Change, Close, Delete, or Add.
The FR Y-10 report may be submitted in a hardcopy format or via the FR Y-10 Online application - https://y10online.federalreserve.gov.

* FDIC UNINUM, Office Number, and ID_RSSD columns are for reference only. Verification of these values is not required.

| Data Action | Effective Date | Branch Service Type | Branch ID_RSSD* | Popular Name | Street Address | City | State | Zip Code | County | Country | FDIC UNINUM* | Office Number* | Head Office | Head Office ID_RSSD* | Comments |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Ok | | Full Service (Head Office) | 3299168 | PALMETTO HERITAGE BANK & TRUST | 10919 OCEAN HIGHWAY | PAWLEYS ISLAND | SC | 29585 | GEORGETOWN | UNITED STATES | Not Required | Not Required | PALMETTO HERITAGE BANK & TRUST | 3299168 | |
| Ok | | Full Service | 3797271 | MOUNT PLEASANT BRANCH | 3102 HIGHWAY 17 N | MOUNT PLEASANT | SC | 29466 | CHARLESTON | UNITED STATES | Not Required | Not Required | PALMETTO HERITAGE BANK & TRUST | 3299168 | |
| Ok | | Full Service | 4118985 | MURRELLS INLET BRANCH | 4375 HIGHWAY 17 | MURRELLS INLET | SC | 29576 | GEORGETOWN | UNITED STATES | Not Required | Not Required | PALMETTO HERITAGE BANK & TRUST | 3299168 | |

**FORM FR Y-6**
**PALMETTO HERITAGE BANCSHARES, INC.**
**PAWLEYS ISLAND, SC**
**Fiscal Year Ending December 31, 2017**

**Report Item 2b Domestic Branch Listing**

Report Item 2b

Name: Mt Pleasant Branch
Opened: June 16, 2008
Street Address: 3102 Highway 17 North
City: Mt Pleasant
County: Charleston
State: South Carolina
Country: USA
Zip Code: 29466
Service Type: Full Service

Name: Murrells Inlet Branch
Opened: March 15, 2010
Street Address: 4375 Highway 17
City: Murrells Inlet
County: Georgetown
State: South Carolina
Country: USA
Zip Code: 29576
Service Type: Full Service

**FORM FR Y-6**
**PALMETTO HERITAGE BANCSHARES, INC**
**FISCAL YEAR ENDING DECEMBER 31, 2017**

## Report Item 3: Shareholders
## (1)(a)(b)(c) and (2)(a)(b)(c)

**Current Shareholders with ownership, control or holdings of 5% or more with power to vote as of fiscal year ending 12-31-2017**

| (1)(a) Name & Address (City, State, Country) | (1)(b) Country of Citizenship or Incorporation | (1(c) Number and Percentage of Each Class of Voting Securities | |
|---|---|---|---|
| Palmetto Heritage Bar Trustee U/W for Elizabeth Lowe (deceased) Pawleys Island, SC | USA | 11,718 Common Stock | 5.34% |
| Robert G. Lowe Ft. Myers, FL | USA | 21,845 Common Stock | 9.95% |
| Palmetto Heritage Bank, Trustee Robert G. Lowe IRA | | 10,706 | 4.87% |
| E. Kendall Roy Hilton Head, SC | USA | 16,774 Common Stock | 7.64% |
| Linda B. Roy Hilton Head, SC | USA | 19,308 Common Stock | 8.79% |
| Thomas J. Wolf Garden City, SC | USA | 16,292 Common Stock | 7.42% |
| C. Ronald Christmas Georgetown, SC | USA | 17,371 Common Stock | 7.91% |

* Chairman Robert G. Lowe has shares he holds in his IRA account in the Trust Department of the Bank. This along with his deceased wife's trust (Elizabeth Lowe) are shares held on his behalf and that he votes.

**Shareholders not listed in 3(1)(a) through 3(1)(c) that had ownership, control or holdings of 5% or more with power to vote during the fiscal year ending 12/31/2017**

| (2)(a) Name & Address (City, State, Country) | (2)(b) Country of Citizenship or Incorporation | (2)(c) Number and Percentage of Each Class of Voting Securities |
|---|---|---|
| **NONE** | | |

FORM FR Y-6
PALMETTO HERITAGE BANCSHARES INC.
FISCAL YEAR ENDING DECEMBER 31, 2017

Report Item 4: Insiders
(1), (2), (3)(a)(b)(c), and (4)(a)(b)(c)

| (1) Names & Address (City, State, Country) | (2) Principal Occupation if other than with Bank Holding company | (3)(a) Title & Position with Bank Holding Company | (3)(b) Title & Position with Subsidiaries | (3)(c) Title & Position with other Businesses | (4)(a) Percentage of Voting Shares in Bank Holding Company | (4)(b) Percentage of Voting Shares in Subsidiaries | (4)(c) List names of other companies If 25% or more of voting securities are held |
|---|---|---|---|---|---|---|---|
| C. Ronald Christmas<br>Georgetown, SC<br>USA | N/A | Director<br>Vice Chairman &<br>CEO | Director<br>Vice Chairman & CEO<br>Palmetto Heritage Bank & Trust | N/A | 7.91% | N/A | N/A |
| Charles R. Lowe<br>Murrells Inlet, SC<br>USA | N/A | N/A | President<br>Palmetto Coastal Insurance<br>Agency Inc | N/A | 1.18% | 28%<br>Palmetto Coastal<br>Insurance Agency | N/A |
| Trust U/W Elizabeth A. Lowe<br>Pawleys Island, SC<br>USA | Shares in<br>Trust | * Shareholder | N/A | N/A | 5.34% | N/A | N/A |
| Robert G. Lowe<br>Ft Myers, FL<br>USA | Retired | Director | N/A | N/A | ** 20.16% | N/A | N/A |
| Sue Draper Lowe<br>Ft Myers, FL<br>USA | Retired | Director | N/A | N/A | .1138% | N/A | N/A |
| Debra P Lowman<br>Bluffton, SC<br>USA | Real Estate<br>Marketing | Director | N/A | Marketing Rep | .6586% | N/A | N/A |
| E. Kendall Roy<br>Hilton Head, SC<br>USA | Retired | Director<br>Chairman of the<br>Board | N/A | E. Kendall Roy, LLC<br>Hilton Head, SC<br>Owner | 7.64% | N/A | E. Kendall Roy, LLC<br>100% |
| Linda B. Roy<br>Hilton Head, SC<br>USA | Retired | *** Shareholder | N/A | N/A | 8.79% | N/A | N/A |
| Russell Vedder<br>Pawleys Island, SC<br>USA | N/A | Shareholder | President and Director<br>Palmetto Heritage Bank & Trust | Director<br>Palmetto Coastal Insurance | 0.17% | N/A | N/A |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Thomas J. Wolf<br>Garden City, SC<br>USA | Franchise<br>Owner | **** Shareholder | N/A | Owner<br>McDonalds Franchise<br>Ashland, KY &<br>Huntington, WV | 7.42% | N/A | Fifth Ave Broadcasting<br>TJ Wolf Inc<br>Abilene Corp<br>Odessa Corp<br>Carolina Corp<br>E-Jay Enterprises<br>Savannah Corp<br>Memphis Corp<br>Natchez Corp | 100%<br>100%<br>100%<br>100%<br>100%<br>100%<br>100%<br>100%<br>100% |

* Voted by Robert G. Lowe, spouse to Elizabeth Lowe, deceased
** Includes Voting Rights in Trust
*** Voted with Husband, E Kendall Roy
**** As an initial shareholder Mr. Wolf will Vote with Mr. Lowe,
Dr. Roy and Mr. Christmas on items of importance with Bancshares

# PALMETTO HERITAGE
• BANK & TRUST •

March 22, 2018

To Our Shareholders:

We are pleased to present our 2017 annual consolidated financial statements. Through organic balance sheet growth, improving interest margins, and measured efficiency, Palmetto Heritage Bancshares, Inc. and its subsidiaries, Palmetto Heritage Bank & Trust and Palmetto Coastal Insurance Agency continued to improve profitability and franchise value in 2017. The Company reported record net income in 2017 of $1,479,000, which represents an improvement of 29% over prior year (2016) earnings of $1,148,000. This increase resulted in an annualized return on average equity of 9.07% and consolidated earnings per share of $6.73.

As detailed in the following financial statements, our total assets grew at a controlled pace during 2017 with annual asset growth of 5.73% and increases in both loans and deposits of 8.11% and 4.21%, respectively. The Company continues to maintain a strong capital position through retained earnings resulting in a year end Bank leverage ratio of 10.06%. With continued growth, focused profitability, and advantageous tax policy, we are projecting another year of double digit income growth in 2018.

The Company paid dividends in 2017 to all shareholders of $3.25 per share representing 48% of the Company's 2017 earnings.

Our management and staff want to thank you, our shareholders, for the support, confidence and trust you have placed in our financial success. We believe in the future of the Waccamaw Neck and Mount Pleasant communities we serve. We are committed to building a strong community bank, providing unparalleled service to our clients and delivering long term value to our shareholders.

We appreciate your support and we encourage you to continue to use Palmetto Heritage Bank and Palmetto Coastal Insurance for all of your financial needs.

If you have any questions concerning the annual report or our plans for the future, please do not hesitate to call us or stop by the Bank to speak with a member of our management team.

Very truly yours, your Management Team,

C. Ronald Christmas

C. Ronald Christmas
Vice Chairman and
Chief Executive Officer
Palmetto Heritage Bank & Trust
President and CEO
Palmetto Heritage Bancshares, Inc.

Russell A. Vedder
President
Palmetto Heritage & Trust

C R Lowe

Charles R. Lowe
President
Palmetto Coastal
Insurance Agency

10919 OCEAN HIGHWAY • P.O. BOX 3788 • PAWLEYS ISLAND, SC 29585-3788
843.237.7776 • FAX 843-237-7710

# Palmetto Heritage Bancshares, Inc.
# and Subsidiaries

***Report on Consolidated Financial Statements***

***For the years ended December 31, 2017 and 2016***

*Contents*

elliott davis

## Independent Auditor's Report

The Board of Directors
Palmetto Heritage Bancshares, Inc. and Subsidiaries
Pawleys Island, South Carolina

### Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Palmetto Heritage Bancshares, Inc. and its Subsidiaries which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated 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 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 Palmetto Heritage Bancshares, Inc. and its Subsidiaries as of December 31, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Elliott Davis, LLC

Columbia, South Carolina
March 22, 2018

## Palmetto Heritage Bancshares, Inc. and Subsidiaries

***Consolidated Balance Sheets***
***As of December 31, 2017 and 2016***

| | 2017 | 2016 |
|---|---|---|
| **Assets** | | |
| Cash and cash equivalents: | | |
| Cash and due from banks | $ 854,407 | $ 617,278 |
| Interest bearing deposits | 6,503,747 | 7,249,258 |
| Federal funds sold | 1,950,000 | 1,950,000 |
| Total cash and cash equivalents | 9,308,154 | 9,816,536 |
| Time deposits in banks | 240,000 | 240,000 |
| Investment securities: | | |
| Securities available-for-sale | 6,896,298 | 7,669,059 |
| Nonmarketable equity securities | 1,158,700 | 1,000,800 |
| Total investment securities | 8,054,998 | 8,669,859 |
| Loans receivable | 130,568,789 | 120,771,413 |
| Less allowance for loan losses | (1,168,124) | (1,143,124) |
| Net loans | 129,400,665 | 119,628,289 |
| Premises, furniture and equipment, net | 8,948,928 | 9,271,235 |
| Accrued interest receivable | 555,089 | 500,023 |
| Other real estate owned | 3,257,143 | 3,269,848 |
| Cash surrender value of life insurance | 2,141,416 | 2,071,870 |
| Other assets | 1,063,332 | 673,660 |
| Total assets | $ 162,969,725 | $ 154,141,320 |
| **Liabilities** | | |
| Deposits: | | |
| Noninterest-bearing transaction accounts | $ 7,197,314 | $ 6,515,758 |
| Interest-bearing transaction accounts | 6,768,229 | 5,980,590 |
| Savings and money market accounts | 25,951,380 | 24,881,877 |
| Time deposits $250,000 and over | 21,790,050 | 21,526,822 |
| Other time deposits | 60,545,239 | 58,413,404 |
| Total deposits | 122,252,212 | 117,318,451 |
| Advances from Federal Home Loan Bank | 23,500,000 | 20,500,000 |
| Accrued interest payable | 144,091 | 114,180 |
| Other liabilities | 365,694 | 288,208 |
| Total liabilities | 146,261,997 | 138,220,839 |
| ***Commitments and contingencies - Notes 12 and 18*** | | |
| **Shareholders' Equity** | | |
| Common stock, $.01 par value, 600,000 shares authorized, 219,635 shares issued and outstanding at December 31, 2017 and 2016, respectively | 2,197 | 2,197 |
| Capital surplus | 16,347,977 | 16,322,048 |
| Retained earnings (deficit) | 372,745 | (391,954) |
| Accumulated other comprehensive loss | (15,191) | (11,810) |
| Total shareholders' equity | 16,707,728 | 15,920,481 |
| Total liabilities and shareholders' equity | $ 162,969,725 | $ 154,141,320 |

***See Notes to Consolidated Financial Statements***

## Palmetto Heritage Bancshares, Inc. and Subsidiaries

***Consolidated Statements of Income***
***For the years ended December 31, 2017 and 2016***

| | 2017 | 2016 |
|---|---|---|
| **Interest income:** | | |
| Loans, including fees | $ 7,142,809 | $ 6,343,359 |
| Securities available-for-sale | 79,974 | 58,773 |
| Federal funds sold and other | 150,126 | 102,562 |
| Total interest income | 7,372,909 | 6,504,694 |
| **Interest expense:** | | |
| Deposits | 1,013,663 | 844,897 |
| Other borrowings | 407,804 | 305,141 |
| Total interest expense | 1,421,467 | 1,150,038 |
| **Net interest income** | 5,951,442 | 5,354,656 |
| Provision for loan losses | 25,000 | 10,000 |
| **Net interest income after provision for loan losses** | 5,926,442 | 5,344,656 |
| **Noninterest income:** | | |
| Service charges on deposit accounts | 69,477 | 90,039 |
| Income from cash surrender value of life insurance | 69,546 | 71,870 |
| Income from fiduciary activities | 324,000 | 324,000 |
| Residential mortgage origination fees | 111,125 | 113,952 |
| Insurance commissions | 197,349 | 170,173 |
| Other service fees and commissions | 17,971 | 13,857 |
| Other | 7,174 | 4,342 |
| Total noninterest income | 796,642 | 788,233 |
| **Noninterest expense:** | | |
| Salaries and employee benefits | 2,186,152 | 2,191,123 |
| Net occupancy | 203,821 | 207,532 |
| Data processing | 177,252 | 175,324 |
| Furniture and equipment | 342,149 | 338,606 |
| Depreciation and amortization | 379,818 | 368,780 |
| Advertising and marketing | 40,359 | 43,992 |
| FDIC assessments | 112,676 | 111,600 |
| Net cost of operation of other real estate owned | 43,587 | 9,759 |
| Other operating | 943,943 | 885,321 |
| Total noninterest expense | 4,429,757 | 4,332,037 |
| **Income before income taxes** | 2,293,327 | 1,800,852 |
| Income tax expense | 814,148 | 652,534 |
| **Net income** | $ 1,479,179 | $ 1,148,318 |
| **Earnings per share** | | |
| Basic earnings per share | $ 6.73 | $ 5.23 |
| Diluted earnings per share | $ 6.72 | $ 5.22 |
| Weighted average shares outstanding (basic) | 219,635 | 219,635 |
| Weighted average shares outstanding (diluted) | 220,179 | 219,782 |

***See Notes to Consolidated Financial Statements***

## Palmetto Heritage Bancshares, Inc. and Subsidiaries

***Consolidated Statements of Comprehensive Income***

***For the years ended December 31, 2017 and 2016***

| | 2017 | 2016 |
|---|---|---|
| **Net income** | $ 1,479,179 | $ 1,148,318 |
| **Other comprehensive loss** | | |
| Unrealized holding losses arising during the period | (2,241) | (15,792) |
| Tax effect | 682 | 5,368 |
| **Other comprehensive loss, net of tax** | (1,559) | (10,424) |
| **Comprehensive income** | $ 1,477,620 | $ 1,137,894 |

***See Notes to Consolidated Financial Statements***

## Palmetto Heritage Bancshares, Inc. and Subsidiaries

***Consolidated Statements of Changes in Shareholders' Equity***

***For the years ended December 31, 2017 and 2016***

| | Common Stock | | Capital | Retained Earnings | Accumulated Other Comprehensive | |
|---|---|---|---|---|---|---|
| | **Shares** | **Amount** | **Surplus** | **(Deficit)** | **Loss** | **Total** |
| **Balance, December 31, 2015** | 219,635 | $ 2,197 | $ 16,302,509 | $ (1,177,874) | $ (1,386) | $ 15,125,446 |
| Net income | - | - | - | 1,148,318 | - | 1,148,318 |
| Other comprehensive loss, net of tax benefit of $5,368 | - | - | - | - | (10,424) | (10,424) |
| Stock compensation expense | - | - | 19,539 | - | - | 19,539 |
| Dividends paid ($1.65 per share) | - | - | - | (362,398) | - | (362,398) |
| **Balance, December 31, 2016** | 219,635 | 2,197 | 16,322,048 | (391,954) | (11,810) | 15,920,481 |
| Net income | - | - | - | 1,479,179 | - | 1,479,179 |
| Other comprehensive loss, net of tax benefit of $682 | - | - | - | - | (1,559) | (1,559) |
| Reclassification of other comprehensive loss due to tax rate change | - | - | - | 1,822 | (1,822) | - |
| Stock compensation expense | - | - | 25,929 | - | - | 25,929 |
| Dividends paid ($3.25 per share) | - | - | - | (716,302) | - | (716,302) |
| **Balance, December 31, 2017** | 219,635 | $ 2,197 | $ 16,347,977 | $ 372,745 | $ (15,191) | $ 16,707,728 |

***See Notes to Consolidated Financial Statements***

## Palmetto Heritage Bancshares, Inc. and Subsidiaries

***Consolidated Statements of Cash Flows***

***For the years ended December 31, 2017 and 2016***

| | 2017 | 2016 |
|---|---|---|
| **Operating activities:** | | |
| Net income | $ 1,479,179 | $ 1,148,318 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for loan losses | 25,000 | 10,000 |
| Depreciation and amortization expense | 379,818 | 368,780 |
| Discount accretion and premium amortization, net | 34,987 | 69,270 |
| Increase in cash surrender value of life insurance | (69,546) | (71,870) |
| Stock compensation expense | 25,929 | 19,539 |
| Writedowns on other real estate owned | 12,705 | 163,683 |
| Gain on sale of premises, furniture and equipment | (4,400) | - |
| Gain on sale of other real estate owned | - | (21,483) |
| Increase in accrued interest receivable | (55,066) | (45,601) |
| Increase in accrued interest payable | 29,911 | 22,900 |
| (Increase) decrease in other assets | (388,990) | 265,272 |
| Increase in other liabilities | 77,486 | 27,991 |
| Net cash provided by operating activities | 1,547,013 | 1,956,799 |
| **Investing activities:** | | |
| Net increase in nonmarketable equity securities | (157,900) | (81,900) |
| Purchase of securities available-for-sale | (997,656) | (7,415,714) |
| Proceeds from maturities of time deposits in banks | - | 480,049 |
| Proceeds from maturities and paydowns of securities available-for-sale | 1,733,189 | 6,124,486 |
| Proceeds from sale of other real estate owned | - | 248,262 |
| Net increase in loans receivable | (9,797,376) | (11,261,864) |
| Purchase of premises, furniture and equipment | (57,511) | (111,641) |
| Proceeds from sale of premises, furniture and equipment | 4,400 | - |
| Net cash used by investing activities | (9,272,854) | (12,018,322) |
| **Financing activities** | | |
| Dividends paid | (716,302) | (362,398) |
| Increase in noninterest-bearing deposits | 681,556 | 1,563,192 |
| Increase in interest bearing deposits | 4,252,205 | 4,391,076 |
| Net increase in Federal Home Loan Bank borrowings | 3,000,000 | 3,500,000 |
| Net cash provided by financing activities | 7,217,459 | 9,091,870 |
| Net decrease in cash and cash equivalents | (508,382) | (969,653) |
| **Cash and cash equivalents, beginning of year** | 9,816,536 | 10,786,189 |
| **Cash and cash equivalents, end of year** | $ 9,308,154 | $ 9,816,536 |
| **Cash paid during the year for:** | | |
| Interest | $ 1,391,556 | $ 1,127,138 |
| Income taxes | $ 873,756 | $ 489,953 |
| **Noncash investing and financing activities** | | |
| Change in unrealized loss on securities available-for-sale | $ (2,241) | $ (15,792) |
| Transfer of loans to other real estate owned | $ - | $ 241,763 |

***See Notes to Consolidated Financial Statements***

## Note 1. Summary of Significant Accounting Policies

*Organization:*

Palmetto Heritage Bancshares, Inc. and Subsidiaries (the "Company") was incorporated to serve as a bank holding company for Palmetto Heritage Bank (the "Bank") and Palmetto Coastal Insurance Agency (the "Insurance Agency"). Palmetto Heritage Bank commenced business on January 3, 2005. The principal business activity of the Bank is to provide banking services to domestic markets, principally in Georgetown and Charleston Counties in South Carolina. The Bank is a state-chartered commercial bank, and its deposits are insured by the Federal Deposit Insurance Corporation. The consolidated financial statements include the accounts of the parent company, its wholly-owned bank subsidiary, and its majority owned Insurance Agency after elimination of all significant intercompany balances and transactions.

In 2006, the Company formed the Insurance Agency, a subsidiary of the Company. As of December 31, 2017 and 2016, the Company owns 72% and the president of the Insurance Agency owns 28%. Amounts representing non-controlling interests are immaterial to the consolidated financial statements and have not been presented separately in the Company's consolidated balance sheets and statements of operations.

*Management's Estimates:*

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the dates of the consolidated balance sheets and the statements of operations for the periods covered. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, including valuation allowances for impaired loans, and the valuation of real estate acquired in connection with foreclosures or in satisfaction of loans. In connection with the determination of the allowances for loan losses and foreclosed real estate, management obtains independent appraisals for significant properties. Management must also make estimates in determining the estimated useful lives and methods for depreciating premises and equipment.

While management uses available information to recognize losses on loans and foreclosed real estate, future additions 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 Company's allowances for loan losses and foreclosed real estate. Such agencies may require the Company to recognize additions to the allowances 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 allowances for loan losses and foreclosed real estate may change materially in the near term.

**Note 1. Summary of Significant Accounting Policies, Continued**

*Concentrations of Credit Risk:*

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist principally of loans receivable, investment securities, federal funds sold and amounts due from banks.

In addition to monitoring potential concentrations of loans to particular borrowers or groups of borrowers, industries and geographic regions, management monitors exposure to credit risk from concentrations of lending products and practices such as loans that subject borrowers to substantial payment increases (e.g. principal deferral periods, loans with initial interest-only periods, etc.), and loans with high loan-to-value ratios. Additionally, there are industry practices that could subject the Company to increased credit risk should economic conditions change over the course of a loan's life. For example, the Company makes variable rate loans and fixed rate principal-amortizing loans with maturities prior to the loan being fully paid (i.e. balloon payment loans). These loans are underwritten and monitored to manage the associated risks. Therefore, management believes that these particular practices do not subject the Company to unusual credit risk.

The Company's investment portfolio consists principally of obligations of the United States, or its sponsored enterprises. In the opinion of management, there is no concentration of credit risk in its investment portfolio. The Company places its deposits and correspondent accounts with and sells its federal funds to high quality institutions. Management believes credit risk associated with correspondent accounts is not significant.

*Securities Available-for-Sale:*

Securities available-for-sale are carried at amortized cost and adjusted to their estimated market value by recognizing the aggregate unrealized gains or losses in a valuation account. Aggregate market valuation adjustments are excluded from earnings and reported in other comprehensive income, net of deferred income taxes. Management does not actively trade securities available-for-sale but intends to hold these securities for an indefinite period of time and may sell them prior to maturity to achieve certain objectives. Reductions in market value considered by management to be other than temporary are reported as a realized loss and a reduction in the cost basis of the security. The adjusted cost basis of securities available-for-sale is determined by specific identification and is used in computing the gain or loss upon sale. Interest income is recognized when earned.

*Nonmarketable Equity Securities:*

Nonmarketable equity securities include the cost of the Company's investment in the stock of the Federal Home Loan Bank. This stock has no quoted market value and no ready market exists. Investment in Federal Home Loan Bank stock is a condition of borrowing from the Federal Home Loan Bank, and the stock is pledged to secure borrowings. At December 31, 2017 and 2016, the Company's investment in the Federal Home Loan Bank was $1,158,700 and $1,000,800, respectively. Dividends are recognized when earned and included as a separate component of interest income.

*Time Deposits in Banks:*

Time deposits in banks include certificates of deposits held at other financial institutions. At both December 31, 2017 and 2016, the Bank had one certificate of deposit with a balance of $240,000 and a rate of 1.04%. The certificate of deposit is scheduled to mature on January 25, 2018.

**Note 1. Summary of Significant Accounting Policies, Continued**

*Loans Receivable:*

Loans are stated at their unpaid principal balance less any charge-offs. Interest income is accrued on the unpaid principal balance using the simple interest method and is recorded in the period earned.

When serious doubt exists as to the collectability of a loan or when a loan becomes contractually 90 days past due as to principal or interest, the accrual of interest income is generally discontinued unless the estimated net realizable value of collateral exceeds the principal balance and accrued interest. When interest accruals are discontinued, income in the current year is reversed and interest accrued in prior years is charged to the allowance for loan losses.

While a loan is on nonaccrual status, the Company's policy is that all cash receipts are applied to principal. Once the recorded principal balance has been reduced to zero, future cash receipts are applied to recoveries of any amounts previously charged off. Further cash receipts are recorded as interest income to the extent that any interest has been foregone. Loans are removed from nonaccrual status when they become current as to both principal and interest, when concern no longer exists as to the collectability of principal and interest, and after a sufficient history of satisfactory payment performance has been established.

Impairment of a loan is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or fair value of the collateral less estimated selling costs if the loan is collateral dependent. When management determines that a loan is impaired, the difference between the Company's investment in the related loan and the present value of the expected future cash flows or the fair value of the collateral less estimated selling costs, is charged to the allowance for loan losses or recorded as a specific reserve to the allowance for loan loss. The accrual of interest is discontinued on an impaired loan when management determines that the borrower may be unable to meet payments as they become due. Subsequent interest earned is recognized only to the point that cash payments are received. All payments are applied to principal if the entire amount of principal is not expected to be collected.

The Bank identifies impaired loans through its normal internal loan review process. Loans on the Bank's problem loan watch list are considered potentially impaired loans. These loans are evaluated in determining whether the borrower will be able to perform in accordance with the loan agreement. Loans are not considered impaired if a minimal payment delay occurs and all amounts due, including accrued interest at the contractual interest rate for the period of delay, are expected to be collected.

*Allowance for Loan Losses:*

The allowance for loan losses is based on management's ongoing evaluation of the loan portfolio and reflects an amount that, in management's opinion, is adequate to absorb losses in the existing portfolio. In evaluating the portfolio, management takes into consideration numerous factors, including current economic conditions, prior loan loss experience, the composition of the loan portfolio, and management's estimate of anticipated credit losses. An unallocated component is maintained to cover uncertainties that could affect management's estimate of the probability of 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. Loans are charged-off against the allowance at such time as they are determined to be losses. Subsequent recoveries and provisions for loan losses are credited to the allowance. Management considers the year-end allowance appropriate and adequate to cover possible losses in the loan portfolio; however, management's judgment is based upon a number of assumptions about future events, which are believed to be reasonable, but which may or may not prove valid. Thus, there can be no assurance that charge-offs in future periods will not exceed the allowance for loan losses or that additional increases in the allowance for loan losses will not be required. Allowances for loan losses are subject to review by various regulatory authorities and may be subject to adjustment upon their examination.

**Note 1. Summary of Significant Accounting Policies, Continued**

*Allowance for Loan Losses (continued):*

Loans are placed in a non-accrual status when, in the opinion of management, the collection of additional interest is questionable. Thereafter, no interest is taken into income unless received in cash or until such time as the borrower demonstrates the ability to pay principal and interest.

*Premises, Furniture and Equipment:*

Premises, furniture and equipment are stated at cost, less accumulated depreciation. The provision for depreciation is computed by the straight-line method, based on the estimated useful lives for buildings of 40 years, furniture and equipment of 5 to 10 years and software of 3 years. The cost of assets sold or otherwise disposed of and the related allowance for depreciation are eliminated from the accounts and the resulting gains or losses are reflected in the income statement when incurred. Maintenance and repairs are charged to current expense. The costs of major renewals and improvements are capitalized.

*Other Real Estate Owned:*

Other real estate owned includes real estate acquired through foreclosure. Other real estate owned is initially recorded at fair value at the date of foreclosure less estimated costs of disposal, which establishes a new cost. After foreclosure, valuations are periodically performed by management and foreclosed assets are carried at the lower of cost or fair value less estimated costs of disposal. Any write-down to fair value at the time of transfer to foreclosed assets is charged to the allowance for loan losses. Property is evaluated regularly to ensure the recorded amount is supported by its current fair value and valuation allowances to reduce the carrying amount to fair value less estimated costs to dispose are recorded as necessary. Revenue and expense from the operations of foreclosed assets and changes in the valuation allowances are included in net cost of operation of other real estate owned.

*Income and Expense Recognition:*

The accrual method of accounting is used for all significant categories of income and expense. Immaterial amounts of miscellaneous fees are reported when received.

*Income Taxes:*

The Company accounts for income taxes in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") topic 740, "Income Taxes." Under ASC 740, deferred tax assets or liabilities are computed based upon the difference between financial statement and income tax bases of assets and liabilities using the enacted marginal tax rate. The Company has provided a valuation allowance on its net deferred tax assets where it is more likely than not such assets will not be realized.

The Company recognizes the tax benefit from an uncertain tax position only if it is more likely than not the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such positions are then measured based on the largest benefit that has a greater than 50% likelihood of being realized upon settlement. See Note 10, "Income Taxes" for additional information. The Company records any penalties and interest attributed to uncertain tax positions as a component of income tax expense.

**Note 1. Summary of Significant Accounting Policies, Continued**

*Income Taxes (continued):*

The Company has adopted Accounting Standards Update ("ASU") 2018-02, "Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income" which is considered a change in accounting principle. Because the required adjustment of deferred taxes is required to be included in income from continuing operations, the tax effects of items within accumulated other comprehensive income (commonly referred to as "stranded" tax effects) would not reflect the appropriate tax rate. Adoption of this ASU eliminates the "stranded" tax effects associated with the change in the federal corporate income tax rate in the Tax Cuts and Jobs Act of 2017. The Company has reclassified "stranded" tax effects totaling $1,822 from accumulated other comprehensive loss to retained earnings and these reclassified amounts are reflected in the accompanying consolidated balance sheets and consolidated statements of changes in shareholders' equity.

*Advertising Expense:*

Advertising and public relations costs are generally expensed as incurred. External costs incurred in producing media advertising are expensed the first time the advertising takes place. External costs relating to direct mailing costs are expended in the period in which the direct mailings are sent. Advertising costs of $40,359 and $43,992, were included in the Company's consolidated statements of income in advertising and marketing expenses for 2017 and 2016, respectively.

*Income Per Share:*

Basic income per share represents income available to shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted income per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued. The only potential common share equivalents are those related to stock options.

*Stock-Based Compensation:*

The Company accounts for stock options in accordance with generally accepted accounting principles. Compensation expense is recognized as salaries and employee benefits in the statements of operations. There were 4,000 stock options granted in 2017.

In calculating the compensation expense for stock options issued in 2017, the fair value of options is estimated as of the date issued using the Black-Scholes option pricing model with the following weighted-average assumptions: dividend yield of 4.58%; expected volatility of 27.83% based on peer group data since the Company does not have sufficient historical information; risk-free interest rate of 1.50% based on the issue date, expected life of 5 years based on factors such as the vesting period and the options' contractual term which is 10 years; and expected forfeitures of 13.24% based on the Company's historical information.

*Statement of Cash Flows:*

For purposes of reporting cash flows in the consolidated financial statements, the Company considers certain highly liquid debt instruments purchased with a original maturity of three months or less to be cash equivalents. Cash equivalents include amounts due from banks, federal funds sold, and interest bearing deposits. Generally, federal funds are sold for one-day periods.

**Note 1. Summary of Significant Accounting Policies, Continued**

*Off-Balance-Sheet Financial Instruments:*

In the ordinary course of business, the Company enters into off-balance-sheet financial instruments consisting of commitments to extend credit and letters of credit. These financial instruments are recorded in the consolidated financial statements when they become payable by the customer.

*Recently Issued Accounting Pronouncements:*

The following is a summary of recent authoritative pronouncements:

In May 2014, the Financial Accounting Standards Board (FASB) issued guidance to change the recognition of revenue from contracts with customers. The core principle of the new guidance is that an entity should recognize revenue to reflect the transfer of goods and services to customers in an amount equal to the consideration the entity receives or expects to receive. The guidance will be effective for the Company for annual periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019. The Company will apply the guidance using a modified retrospective approach. The Company's revenue is comprised of net interest income and noninterest income. The scope of the guidance explicitly excludes net interest income as well as many other revenues for financial assets and liabilities including loans, leases, securities, and derivatives. Accordingly, the majority of the Company's revenues will not be affected. The Company is currently assessing revenue contracts related to revenue streams that are within the scope of the standard. The Company's accounting policies will not change materially since the principles of revenue recognition from the Accounting Standards Update (ASU) are largely consistent with existing guidance and current practices applied by the Company's businesses. The Company has not identified material changes to the timing or amount of revenue recognition. Based on the updated guidance, the Company does anticipate changes in disclosures associated with revenues. The Company will provide qualitative disclosures of performance obligations related to revenue recognition and will continue to evaluate disaggregation for significant categories of revenue in the scope of the guidance.

In January 2016, the FASB amended the Financial Instruments topic of the Accounting Standards Codification (ASC) to address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The amendments will be effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. The Company will apply the guidance by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The amendments related to equity securities without readily determinable fair values will be applied prospectively to equity investments that exist as of the date of adoption of the amendments. The Company does not expect these amendments to have a material effect on its financial statements.

**Note 1. Summary of Significant Accounting Policies, Continued**

*Recently Issued Accounting Pronouncements (continued):*

In February 2016, the FASB amended the Leases topic of the ASC to revise certain aspects of recognition, measurement, presentation, and disclosure of leasing transactions. The amendments will be effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. Early adoption is permitted. The Company expects to adopt the guidance using the modified retrospective method and practical expedients for transition. The practical expedients allow the Company to largely account for existing leases consistent with current guidance except for the incremental balance sheet recognition for lessees. The Company has started an initial evaluation of leasing contracts and activities. The Company has also started developing the methodology to estimate the right-of use assets and lease liabilities, which is based on the present value of lease payments; however, as of December 31, 2017, the Company does not expect these future minimum lease payments to have a material effect on its financial statements. The Company does not expect a material change to the timing of expense recognition, but is early in the implementation process and will continue to evaluate the impact. The Company is evaluating existing disclosures and may need to provide additional information as a result of adoption of the ASU.

In March 2016, the FASB amended the Revenue from Contracts with Customers topic of the ASC to clarify the implementation guidance on principal versus agent considerations and address how an entity should assess whether it is the principal or the agent in contracts that include three or more parties. The amendments will be effective for the Company for annual periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019. The Company does not expect these amendments to have a material effect on its financial statements.

In March 2016, the FASB issued guidance to simplify several aspects of the accounting for share-based payment award transactions including the income tax consequences, the classification of awards as either equity or liabilities, and the classification on the statement of cash flows. Additionally, the guidance simplifies two areas specific to entities other than public business entities allowing them apply a practical expedient to estimate the expected term for all awards with performance or service conditions that have certain characteristics and also allowing them to make a one-time election to switch from measuring all liability-classified awards at fair value to measuring them at intrinsic value. The amendments will be effective for the Company for annual periods beginning after December 15, 2017, and interim periods within annual reporting periods beginning after December 15, 2018. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

In April 2016, the FASB amended the Revenue from Contracts with Customers topic of the ASC to clarify guidance related to identifying performance obligations and accounting for licenses of intellectual property. The amendments will be effective for the Company for annual periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019. The Company does not expect these amendments to have a material effect on its financial statements.

In May 2016, the FASB amended the Revenue from Contracts with Customers topic of the ASC to clarify guidance related to collectability, noncash consideration, presentation of sales tax, and transition. The amendments will be effective for the Company for annual periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019. The Company does not expect these amendments to have a material effect on its financial statements.

**Note 1. Summary of Significant Accounting Policies, Continued**

*Recently Issued Accounting Pronouncements (continued):*

In June 2016, the FASB issued guidance to change the accounting for credit losses and modify the impairment model for certain debt securities. The amendments will be effective for the Company for annual periods beginning after December 15, 2020, and interim periods within annual reporting periods beginning after December 15, 2021. Early adoption is permitted for all organizations for periods beginning after December 15, 2018. The Company will apply the amendments to the ASU through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption. While early adoption is permitted beginning in first quarter 2019, the Company does not expect to elect that option. The Company is evaluating the impact of the ASU on the consolidated financial statements with regards to the impact on the recorded allowance for loan losses given the change to estimated losses over the contractual life of the loans adjusted for expected prepayments. In addition to the allowance for loan losses, the Company will also record an allowance for credit losses on debt securities instead of applying the impairment model currently utilized. The amount of the adjustments will be impacted by each portfolio's composition and credit quality at the adoption date as well as economic conditions and forecasts at that time.

In August 2016, the FASB amended the Statement of Cash Flows topic of the ASC to clarify how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The amendments will be effective for the Company for fiscal years beginning after December 15, 2017, and interim periods within fiscal years beginning after December 15, 2018. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

In October 2016, the FASB amended the Income Taxes topic of the ASC to modify the accounting for intra-entity transfers of assets other than inventory. The amendments will be effective for the Company for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

In November 2016, the FASB amended the Statement of Cash Flows topic of the ASC to clarify how restricted cash is presented and classified in the statement of cash flows. The amendments will be effective for the Company for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

In December 2016, the FASB issued technical corrections and improvements to the Revenue from Contracts with Customers Topic. These corrections make a limited number of revisions to several pieces of the revenue recognition standard issued in 2014. The effective date and transition requirements for the technical corrections will be effective for the Company for annual periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019. The Company will apply the guidance using a modified retrospective approach. The Company does not expect these amendments to have a material effect on its financial statements.

**Note 1. Summary of Significant Accounting Policies, Continued**

*Recently Issued Accounting Pronouncements (continued):*

In February 2017, the FASB amended the Other Income Topic of the ASC to clarify the scope of the guidance on nonfinancial asset derecognition as well as the accounting for partial sales of nonfinancial assets. The amendments conform the derecognition guidance on nonfinancial assets with the model for transactions in the new revenue standard. The amendments will be effective for the Company for annual periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019. The Company does not expect these amendments to have a material effect on its financial statements.

In March 2017, the FASB amended the requirements in the Receivables-Nonrefundable Fees and Other Costs Topic of the ASC related to the amortization period for certain purchased callable debt securities held at a premium. The amendments shorten the amortization period for the premium to the earliest call date. The amendments will be effective for the Company for annual periods beginning after December 15, 2019, and interim periods within annual reporting periods beginning after December 15, 2020. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

In February 2018, the FASB issued ASU 2018-02, *Income Statement (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*, which requires Companies to reclassify the stranded effects in other comprehensive income (loss) to retained earnings as a result of the change in the tax rates under the Tax Cuts and Jobs Act. The Company has opted to early adopt this pronouncement by retrospective application to each period (or periods) in which the effect of the change in the tax rate under the Tax Cuts and Jobs Act is recognized. The impact of the reclassification from other comprehensive loss to retained earnings is $1,822.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company's financial position, results of operations or cash flows.

*Risks and Uncertainties:*

In the normal course of its business, the Company encounters two significant types of risks: economic and regulatory. There are three main components of economic risk: interest rate risk, credit risk and market risk. The Company is subject to interest rate risk to the degree that its interest-bearing liabilities mature or reprice at different speeds, or on different basis, than its interest-earning assets. Credit risk is the risk of default on the Company's loan portfolio that results from a borrower's inability or unwillingness to make contractually required payments. Market risk reflects changes in the value of collateral underlying loans receivable and the valuation of real estate held by the Company.

The Company is subject to the regulations of various governmental agencies. These regulations can and do change significantly from period to period. The Company also undergoes periodic examinations by the regulatory agencies, which may subject it to further changes with respect to asset valuations, amounts of required loss allowances and operating restrictions from the regulators' judgments based on information available to them at the time of their examination.

**Note 1. Summary of Significant Accounting Policies, Continued**

*Reclassifications:*

Certain captions and amounts in the 2016 consolidated financial statements were reclassified to conform with the 2017 presentation. All such reclassifications had no impact on previously reported net income, comprehensive income or shareholders' equity.

**Note 2. Cash and Due From Banks**

The Company is required by regulation to maintain an average cash reserve balance based on a percentage of deposits. At December 31, 2017 and 2016, the required cash reserve was satisfied by vault cash.

**Note 3. Securities Available-for-Sale**

The amortized cost and estimated fair values of securities available-for-sale were:

| | December 31, 2017 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
| Mortgage-backed securities | $ 921,069 | $ 31 | $ 4,974 | $ 916,126 |
| Government-sponsored enterprises | 2,500,000 | - | 3,657 | 2,496,343 |
| U.S. Treasury notes and bonds | 3,495,364 | - | 11,535 | 3,483,829 |
| Total investment securities available-for-sale | $ 6,916,433 | $ 31 | $ 20,166 | $ 6,896,298 |

| | December 31, 2016 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
| Mortgage-backed securities | $ 1,544,214 | $ 148 | $ 6,031 | $ 1,538,331 |
| Government-sponsored enterprises | 2,650,000 | 40 | 8,687 | 2,641,353 |
| U.S. Treasury notes and bonds | 3,492,739 | 817 | 4,181 | 3,489,375 |
| Total investment securities available-for-sale | $ 7,686,953 | $ 1,005 | $ 18,899 | $ 7,669,059 |

**Note 3. Securities Available-for-Sale, Continued**

The following table shows gross unrealized losses and fair value, aggregated by investment category, and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2017 and 2016.

| | December 31, 2017 | | | | | |
|---|---|---|---|---|---|---|
| | Less than twelve months | | Twelve months or more | | Total | |
| | Fair value | Unrealized losses | Fair value | Unrealized losses | Fair value | Unrealized losses |
| Mortgage-backed securities | $ 513,695 | $ 1,899 | $ 334,712 | $ 3,075 | $ 848,407 | $ 4,974 |
| Government-sponsored enterprises | - | - | 2,496,343 | 3,657 | 2,496,343 | 3,657 |
| U.S. Treasury notes and bonds | 1,986,250 | 9,328 | 1,497,579 | 2,207 | 3,483,829 | 11,535 |
| Total investment securities available-for-sale | $ 2,499,945 | $ 11,227 | $ 4,328,634 | $ 8,939 | $ 6,828,579 | $ 20,166 |

| | December 31, 2016 | | | | | |
|---|---|---|---|---|---|---|
| | Less than twelve months | | Twelve months or more | | Total | |
| | Fair value | Unrealized losses | Fair value | Unrealized losses | Fair value | Unrealized losses |
| Mortgage-backed securities | $ 812,034 | $ 2,227 | $ 458,144 | $ 3,804 | $ 1,270,178 | $ 6,031 |
| Government-sponsored enterprises | 2,491,313 | 8,687 | - | - | 2,491,313 | 8,687 |
| U.S. Treasury notes and bonds | 2,489,688 | 4,181 | - | - | 2,489,688 | 4,181 |
| Total investment securities available-for-sale | $ 5,793,035 | $ 15,095 | $ 458,144 | $ 3,804 | $ 6,251,179 | $ 18,899 |

Securities classified as available-for-sale are recorded at fair market value. At December 31, 2017 and 2016, the Company had nine and three individual securities, respectively, in an unrealized loss position. The Company had six securities in a continuous loss position for twelve months or more at December 31, 2017 as compared to one at December 31, 2016. The Company does not intend to sell these securities and it is more likely than not that the Company will not be required to sell the securities before recovery of its amortized cost. The Company believes, based on industry analyst reports and credit ratings, that the deterioration in value is attributable to changes in market interest rates and is not in the credit quality of the issuer and therefore, these losses are not considered other-than-temporary.

**Note 3. Securities Available-for-Sale, Continued**

The amortized cost and fair values of investment securities at December 31, 2017, by contractual maturity, are shown in the following chart. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | Amortized Cost | Estimated Fair Value |
|---|---|---|
| Due in one year or less | $ 4,997,527 | $ 4,986,891 |
| Due after one year but within five years | 1,310,501 | 1,305,188 |
| Due after five years but within ten years | 608,405 | 604,219 |
| Total | $ 6,916,433 | $ 6,896,298 |

At December 31, 2017 and 2016, securities with an amortized cost of $3,498,705 and $4,619,411 and an estimated fair value of $3,492,001 and $4,609,483, respectively, were pledged to secure public deposits.

There were no sales of securities available-for-sale for the years ended December 31, 2017 and 2016.

**Note 4. Loans Receivable**

Following is a summary of loans by major classification at December 31:

| | 2017 | 2016 |
|---|---|---|
| Construction and land development | $ 24,416,996 | $ 22,781,158 |
| Farmland | 1,057,074 | 1,079,948 |
| Residential real estate | 64,082,793 | 57,758,668 |
| Commercial real estate | 27,724,034 | 26,395,075 |
| Commercial other | 9,640,622 | 8,684,069 |
| Consumer | 3,647,270 | 4,072,495 |
| | $ 130,568,789 | $ 120,771,413 |

The Company had pledged $30,974,132 and $24,474,775 of loans as collateral for advances from the Federal Home Loan Bank as of December 31, 2017 and 2016, respectively (see Note 8).

## Note 4. Loans Receivable, Continued

The following is a summary of information pertaining to our allowance for loan losses at December 31, 2017.

| | Construction and Land Development | Farmland | Residential Real Estate | Commercial Real Estate | Commercial Other | Consumer | Total |
|---|---|---|---|---|---|---|---|
| **Allowance for loan losses:** | | | | | | | |
| Beginning balance | $ 269,812 | $ 7,292 | $ 624,628 | $ 167,881 | $ 43,231 | $ 30,280 | $ 1,143,124 |
| Charge-offs | - | - | - | - | - | - | - |
| Recoveries | - | - | - | - | - | - | - |
| Provisions | 68,222 | 3,296 | (174,902) | 95,389 | 31,971 | 1,024 | 25,000 |
| Ending balance | $ 338,034 | $ 10,588 | $ 449,726 | $ 263,270 | $ 75,202 | $ 31,304 | $ 1,168,124 |
| Ending balances: | | | | | | | |
| Individually evaluated for impairment | $ - | $ - | $ 12,565 | $ - | $ - | $ - | $ 12,565 |
| Collectively evaluated for impairment | $ 338,034 | $ 10,588 | $ 437,161 | $ 263,270 | $ 75,202 | $ 31,304 | $ 1,155,559 |
| **Loans receivable:** | | | | | | | |
| Ending balance - total | $ 24,416,996 | $ 1,057,074 | $ 64,082,793 | $ 27,724,034 | $ 9,640,622 | $ 3,647,270 | $ 130,568,789 |
| Ending balances: | | | | | | | |
| Individually evaluated for impairment | $ 102,223 | $ - | $ 377,501 | $ - | $ - | $ - | $ 479,724 |
| Collectively evaluated for impairment | $ 24,314,773 | $ 1,057,074 | $ 63,705,292 | $ 27,724,034 | $ 9,640,622 | $ 3,647,270 | $ 130,089,065 |

The following is a summary of information pertaining to our allowance for loan losses at December 31, 2016.

| | Construction and Land Development | Farmland | Residential Real Estate | Commercial Real Estate | Commercial Other | Consumer | Total |
|---|---|---|---|---|---|---|---|
| **Allowance for loan losses:** | | | | | | | |
| Beginning balance | $ 210,742 | $ 5,537 | $ 547,255 | $ 220,500 | $ 27,323 | $ 22,874 | $ 1,034,231 |
| Charge-offs | (15,000) | - | - | - | - | - | (15,000) |
| Recoveries | 9,317 | - | 103,717 | - | 859 | - | 113,893 |
| Provisions | 64,753 | 1,755 | (26,344) | (52,619) | 15,049 | 7,406 | 10,000 |
| Ending balance | $ 269,812 | $ 7,292 | $ 624,628 | $ 167,881 | $ 43,231 | $ 30,280 | $ 1,143,124 |
| Ending balances: | | | | | | | |
| Individually evaluated for impairment | $ 14,393 | $ - | $ 19,817 | $ - | $ - | $ - | $ 34,210 |
| Collectively evaluated for impairment | $ 255,419 | $ 7,292 | $ 604,811 | $ 167,881 | $ 43,231 | $ 30,280 | $ 1,108,914 |
| **Loans receivable:** | | | | | | | |
| Ending balance - total | $ 22,781,158 | $ 1,079,948 | $ 57,758,668 | $ 26,395,075 | $ 8,684,069 | $ 4,072,495 | $ 120,771,413 |
| Ending balances: | | | | | | | |
| Individually evaluated for impairment | $ 214,330 | $ - | $ 418,041 | $ - | $ - | $ - | $ 632,371 |
| Collectively evaluated for impairment | $ 22,566,828 | $ 1,079,948 | $ 57,340,627 | $ 26,395,075 | $ 8,684,069 | $ 4,072,495 | $ 120,139,042 |

**Note 4. Loans Receivable, Continued**

The following is an analysis of our impaired loan portfolio detailing the related allowance recorded at December 31, 2017:

| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Income Recognized |
|---|---|---|---|---|---|
| With no related allowance needed: | | | | | |
| Construction and land development | $ 102,223 | $ 102,223 | $ - | $ 158,277 | $ 8,016 |
| Farmland | - | - | - | - | - |
| Residential real estate | 11,015 | 11,015 | - | 28,083 | 1,351 |
| Commercial real estate | - | - | - | - | - |
| Commercial Other | - | - | - | - | - |
| Consumer | - | - | - | - | - |
| With an allowance recorded: | | | | | |
| Construction and land development | $ - | $ - | $ - | $ - | $ - |
| Farmland | - | - | - | - | - |
| Residential real estate | 366,486 | 366,486 | 12,565 | 369,687 | 16,798 |
| Commercial real estate | - | - | - | - | - |
| Commercial Other | - | - | - | - | - |
| Consumer | - | - | - | - | - |
| Total: | | | | | |
| Construction and land development | $ 102,223 | $ 102,223 | $ - | $ 158,277 | $ 8,016 |
| Farmland | - | - | - | - | - |
| Residential real estate | 377,501 | 377,501 | 12,565 | 397,770 | 18,149 |
| Commercial real estate | - | - | - | - | - |
| Commercial Other | - | - | - | - | - |
| Consumer | - | - | - | - | - |
| | $ 479,724 | $ 479,724 | $ 12,565 | $ 556,047 | $ 26,165 |

The following is an analysis of our impaired loan portfolio detailing the related allowance recorded at December 31, 2016:

| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Income Recognized |
|---|---|---|---|---|---|
| With no related allowance needed: | | | | | |
| Construction and land development | $ - | $ - | $ - | $ - | $ - |
| Farmland | - | - | - | - | - |
| Residential real estate | - | - | - | - | - |
| Commercial real estate | - | - | - | - | - |
| Commercial Other | - | - | - | - | - |
| Consumer | - | - | - | - | - |
| With an allowance recorded: | | | | | |
| Construction and land development | $ 214,330 | $ 214,330 | $ 14,393 | $ 218,174 | $ 8,743 |
| Farmland | - | - | - | - | - |
| Residential real estate | 418,041 | 418,041 | 19,817 | 430,474 | 19,339 |
| Commercial real estate | - | - | - | - | - |
| Commercial Other | - | - | - | - | - |
| Consumer | - | - | - | - | - |
| Total: | | | | | |
| Construction and land development | $ 214,330 | $ 214,330 | $ 14,393 | $ 218,174 | $ 8,743 |
| Farmland | - | - | - | - | - |
| Residential real estate | 418,041 | 418,041 | 19,817 | 430,474 | 19,339 |
| Commercial real estate | - | - | - | - | - |
| Commercial Other | - | - | - | - | - |
| Consumer | - | - | - | - | - |
| | $ 632,371 | $ 632,371 | $ 34,210 | $ 648,648 | $ 28,082 |

**Note 4. Loans Receivable, Continued**

The following is an aging analysis of our loan portfolio at December 31, 2017:

| | 30 - 59 Days Past Due | 60 - 89 Days Past Due | Greater Than 90 Days | Total Past Due | Current | Total Loans Receivable | Recorded Investment >90 Days and Accruing |
|---|---|---|---|---|---|---|---|
| Construction and land development | $ - | $ - | $ - | $ - | $ 24,416,996 | $ 24,416,996 | $ - |
| Farmland | - | - | - | - | 1,057,074 | 1,057,074 | - |
| Residential real estate | - | - | - | - | 64,082,793 | 64,082,793 | - |
| Commercial real estate | - | - | - | - | 27,724,034 | 27,724,034 | - |
| Commercial other | - | - | - | - | 9,640,622 | 9,640,622 | - |
| Consumer | - | - | - | - | 3,647,270 | 3,647,270 | - |
| | $ - | $ - | $ - | $ - | $ 130,568,789 | $ 130,568,789 | $ - |

The following is an aging analysis of our loan portfolio at December 31, 2016:

| | 30 - 59 Days Past Due | 60 - 89 Days Past Due | Greater Than 90 Days | Total Past Due | Current | Total Loans Receivable | Recorded Investment >90 Days and Accruing |
|---|---|---|---|---|---|---|---|
| Construction and land development | $ - | $ - | $ 29,728 | $ 29,728 | $ 22,751,430 | $ 22,781,158 | $ 29,728 |
| Farmland | - | - | - | - | 1,079,948 | 1,079,948 | - |
| Residential real estate | 385,026 | | 124,691 | 509,717 | 57,248,951 | 57,758,668 | 124,691 |
| Commercial real estate | - | - | - | - | 26,395,075 | 26,395,075 | - |
| Commercial other | - | - | - | - | 8,684,069 | 8,684,069 | - |
| Consumer | - | - | - | - | 4,072,495 | 4,072,495 | - |
| | $ 385,026 | $ - | $ 154,419 | $ 539,445 | $ 120,231,968 | $ 120,771,413 | $ 154,419 |

There were no loans on nonaccrual status at December 31, 2017 or 2016.

**Credit Quality Indicators**

Loans are categorized into risk categories based on relevant information about the ability of borrowers to service their debt, such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The following definitions are utilized for risk ratings, which are consistent with the definitions used in supervisory guidance:

***Special Mention*** - Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

***Substandard*** - Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

***Doubtful*** - Loans classified as doubtful have all the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans.

**Note 4. Loans Receivable, Continued**

The following is an analysis of our loan portfolio by credit quality indicators at December 31, 2017:

| | Construction and Land Development | Farmland | Residential Real Estate | Commercial Real Estate | Commercial Other | Consumer | Total |
|---|---|---|---|---|---|---|---|
| Pass | $ 24,314,773 | $ 1,057,074 | $ 63,580,061 | $ 27,724,034 | $ 9,598,221 | $ 3,647,270 | $ 129,921,433 |
| Special mention | - | - | 179,971 | - | 42,401 | - | 222,372 |
| Substandard | 102,223 | - | 322,761 | - | - | - | 424,984 |
| Doubtful | - | - | - | - | - | - | - |
| | $ 24,416,996 | $ 1,057,074 | $ 64,082,793 | $ 27,724,034 | $ 9,640,622 | $ 3,647,270 | $ 130,568,789 |

The following is an analysis of our loan portfolio by credit quality indicators at December 31, 2016:

| | Construction and Land Development | Farmland | Residential Real Estate | Commercial Real Estate | Commercial Other | Consumer | Total |
|---|---|---|---|---|---|---|---|
| Pass | $ 22,566,828 | $ 1,079,948 | $ 57,193,261 | $ 26,395,075 | $ 8,627,191 | $ 4,072,495 | $ 119,934,798 |
| Special mention | - | - | 231,802 | - | 56,878 | - | 288,680 |
| Substandard | 214,330 | - | 333,605 | - | - | - | 547,935 |
| Doubtful | - | - | - | - | - | - | - |
| | $ 22,781,158 | $ 1,079,948 | $ 57,758,668 | $ 26,395,075 | $ 8,684,069 | $ 4,072,495 | $ 120,771,413 |

**Troubled Debt Restructurings ("TDRs")**

The following table summarizes the carrying balance of troubled debt restructurings ("TDRs") as of December 31, 2017 and 2016:

| | 2017 | 2016 |
|---|---|---|
| Construction and land development | $ 102,223 | $ 214,330 |
| Residential real estate | 377,501 | 418,041 |
| Total TDRs | $ 479,724 | $ 632,371 |

During the years ended December 31, 2017 and 2016, there were no modified loans that were considered to be TDRs. No loans previously identified as TDRs went into default (as defined by nonaccrual status classification) during the years ended December 31, 2017 and 2016.

**Note 5. Premises, Furniture and Equipment**

Premises, furniture and equipment is summarized as follows as of December 31:

| | 2017 | 2016 |
|---|---|---|
| Land | $ 3,535,844 | $ 3,535,844 |
| Building and improvements | 6,542,212 | 6,517,918 |
| Furniture and equipment | 2,512,274 | 2,509,188 |
| Automobile | 26,245 | 26,500 |
| Software | 326,986 | 321,986 |
| Construction in progress | 23,508 | 23,508 |
| Total | 12,967,069 | 12,934,944 |
| Less accumulated depreciation | (4,018,141) | (3,663,709) |
| Premises, furniture and equipment, net | $ 8,948,928 | $ 9,271,235 |

Depreciation expense for the years ended December 31, 2017 and 2016 was $379,818 and $368,780, respectively.

## Note 6. Other Real Estate Owned

The following summarizes the activity in the other real estate owned for the years ended December 31:

| | 2017 | 2016 |
|---|---|---|
| Balance, beginning of year | $ 3,269,848 | $ 3,418,547 |
| Additions | - | 241,763 |
| Sales | - | (248,262) |
| Writedowns | (12,705) | (163,683) |
| Gain on sales | - | 21,483 |
| Balance, end of year | $ 3,257,143 | $ 3,269,848 |

## Note 7. Deposits

At December 31, 2017, the scheduled maturities of time deposit are as follows:

| | |
|---|---|
| 2018 | $ 50,895,319 |
| 2019 | 17,589,381 |
| 2020 | 4,394,942 |
| 2021 | 7,007,950 |
| 2022 and thereafter | 2,447,697 |
| | $ 82,335,289 |

Time deposits that meet or exceed the FDIC insurance limit of $250,000 as of December 31, 2017 and 2016 were $21,790,050 and $21,526,822, respectively.

## Note 8. Advances from Federal Home Loan Bank

Advances from the Federal Home Loan Bank ("FHLB") consisted of the following at December 31:

| Description | Current Interest Rate | 2017 Balance | 2016 Balance |
|---|---|---|---|
| Fixed rate advances maturing | | | |
| January 23, 2017 | 1.04% | $ - | $ 1,000,000 |
| February 10, 2017 | 0.90% | - | 1,000,000 |
| March 31, 2017 | 1.16% | - | 1,000,000 |
| June 19, 2017 | 1.15% | - | 1,000,000 |
| July 17, 2017 | 1.30% | - | 2,000,000 |
| October 30, 2017 | 1.31% | - | 1,000,000 |
| December 11, 2017 | 1.37% | - | 1,000,000 |
| January 8, 2018 | 1.09% | 500,000 | 500,000 |
| February 12, 2018 | 1.39% | 1,000,000 | 1,000,000 |
| February 16, 2018 | 1.08% | 1,000,000 | - |
| May 2, 2018 | 0.98% | 1,000,000 | 1,000,000 |
| May 22, 2018 | 4.59% | 2,000,000 | 2,000,000 |
| January 9, 2020 | 1.79% | 1,000,000 | 1,000,000 |
| April 10, 2020 | 1.69% | 500,000 | 500,000 |
| April 20, 2020 | 1.34% | 500,000 | 500,000 |
| August 18, 2020 | 1.30% | 1,000,000 | 1,000,000 |

### Note 8. Advances from Federal Home Loan Bank, Continued

| Description | Current Interest Rate | 2017 Balance | 2016 Balance |
|---|---|---|---|
| Fixed rate advances maturing | | | |
| February 11, 2021 | 1.34% | 1,000,000 | 1,000,000 |
| March 31, 2021 | 2.04% | 1,000,000 | - |
| April 19, 2021 | 1.50% | 500,000 | 500,000 |
| June 28, 2021 | 1.32% | 1,500,000 | 1,500,000 |
| August 18, 2021 | 1.45% | 1,000,000 | 1,000,000 |
| November 8, 2021 | 1.60% | 1,000,000 | 1,000,000 |
| February 16, 2022 | 2.27% | 1,000,000 | - |
| April 19, 2022 | 2.04% | 1,000,000 | - |
| May 31, 2022 | 2.05% | 1,000,000 | - |
| June 9, 2022 | 2.06% | 1,500,000 | - |
| July 18, 2022 | 2.10% | 2,500,000 | - |
| October 31, 2022 | 2.25% | 1,000,000 | - |
| December 12, 2022 | 2.43% | 1,000,000 | - |
| | | $ 23,500,000 | $ 20,500,000 |

Scheduled maturities of the advances at December 31, 2017 are as follows:

| | |
|---|---|
| 2018 | $ 5,500,000 |
| 2019 | - |
| 2020 | 3,000,000 |
| 2021 | 6,000,000 |
| 2022 and thereafter | 9,000,000 |
| | $ 23,500,000 |

At December 31, 2017, the Company has pledged certain loans totaling $30,974,132, as collateral to secure its borrowings from the Federal Home Loan Bank. In addition, the Company's Federal Home Loan Bank stock is pledged to secure the borrowings. Certain advances are subject to prepayment penalties.

### Note 9. Stock Compensation Plan

Under the terms of the employment agreements with the Company's executive officers, stock options were granted to each as part of their compensation and benefits package. The Company also established the Stock Option Agreement and Plan which provides for the granting of options to employees.

A summary of the status of the Company's stock options as of December 31, and changes during the year are presented below:

| | 2017 | | 2016 | |
|---|---|---|---|---|
| | Shares | Weighted Average Exercise Price | Shares | Weighted Average Exercise Price |
| Outstanding at January 1, | 5,699 | $ 83.97 | 4,099 | $ 89.42 |
| Granted | 4,000 | 71.00 | 1,600 | 70.00 |
| Exercised | - | - | - | - |
| Forfeited/Expired | 1,284 | 91.08 | - | - |
| Outstanding at December 31, | 8,415 | $ 76.72 | 5,699 | $ 83.97 |

**Note 9. Stock Compensation Plan, Continued**

The following table summarizes information about stock options outstanding under the Company's Plan at December 31, 2017:

| | Outstanding | Exercisable |
|---|---|---|
| Number of options | 8,415 | 3,266 |
| Weighted average remaining life | 7.50 years | 5.42 years |
| Weighted average exercise price | $ 76.72 | $ 86.25 |
| Aggregate intrinsic value | $ 46,180 | $ 15,068 |
| High exercise price | $ 120.00 | $ 120.00 |
| Low exercise price | $ 69.56 | $ 69.56 |

**Note 10. Income Taxes**

The Tax Cuts and Jobs Act (TCJA) was signed into law by the President on December 21, 2017. The TCJA includes the reduction in the corporate tax rate from a top rate of 35% to a flat rate of 21%, changes in business deductions, and many international provisions.

Income tax expense is summarized as follows for the years ended December 31:

| | 2017 | 2016 |
|---|---|---|
| Current expense: | | |
| Federal | $ 843,747 | $ 470,356 |
| State | 33,831 | 27,375 |
| | 877,578 | 497,731 |
| Deferred expense (benefit) | (63,430) | 154,803 |
| Income tax expense | $ 814,148 | $ 652,534 |

The gross amounts of deferred tax assets and deferred tax liabilities are as follows as of December 31:

| | 2017 | 2016 |
|---|---|---|
| Deferred tax assets: | | |
| Allowance for loan losses | $ 85,443 | $ 129,837 |
| Net operating loss carryforward | 174,749 | 238,375 |
| Organization and start-up costs | 10 | 22 |
| Other real estate owned | 41,487 | 62,849 |
| Unrealized loss on securities available-for-sale | 4,944 | 6,084 |
| Other | 365 | 22,605 |
| Gross deferred tax assets | 306,998 | 459,772 |
| Valuation allowance | 174,751 | 238,377 |
| Total deferred tax assets | 132,247 | 221,395 |
| Deferred tax liabilities: | | |
| Accumulated depreciation | 151,222 | 302,437 |
| Prepaid expenses | 9,158 | 17,439 |
| Total deferred tax liabilities | 160,380 | 319,876 |
| Net deferred tax liability | $ (28,133) | $ (98,481) |

**Note 10. Income Taxes, Continued**

Deferred tax assets represent the future tax benefit of deductible differences and, if it is more likely than not that a tax asset will not be realized, a valuation allowance is required to reduce the recorded deferred tax assets to net realizable value. As of December 31, 2017, management has recorded a valuation allowance of $174,751. Net deferred tax asset (liability) is included in other assets on the Company's consolidated balance sheets.

A reconciliation between the income tax expense and the amount computed by applying the Federal statutory rate of 34% to income loss before income taxes follows for the years ended December 31:

| | 2017 | 2016 |
|---|---|---|
| Tax expense at statutory rate | $ 779,731 | $ 612,290 |
| State income tax, net of federal income tax benefit | 44,658 | 34,446 |
| Tax impact of rate change | (18,940) | - |
| Other | 8,699 | 5,798 |
| Income tax expense | $ 814,148 | $ 652,534 |

Tax returns for 2014 and subsequent years are subject to examination by taxing authorities.

The Company has analyzed the tax positions taken or expected to be taken on its tax returns and concluded it has no liability related to uncertain tax positions in accordance with ASC Topic 740.

**Note 11. Related Party Transactions**

Certain parties (principally certain directors and executive officers of the Company, their immediate families and business interests) were loan customers of and had other transactions in the normal course of business with the Company. Related party loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated persons and do not involve more than the normal risk of collectability. As of December 31, 2017 and 2016, the Company had related party loans totaling $6,374,962 and $4,472,606, respectively.

**Note 12. Commitments and Contingencies**

In the ordinary course of business, the Company may, from time to time, become a party to legal claims and disputes. At December 31, 2017, management is not aware of any pending or threatened litigation or unasserted claims or assessments that could result in losses, if any, that would be material to the consolidated financial statements.

### Note 13. Income Per Share

Basic income per share is computed by dividing net income by the weighted-average number of common shares outstanding. Diluted income per share is computed by dividing net income by the weighted-average number of common shares outstanding and dilutive common share equivalents using the treasury stock method. Dilutive common share equivalents include common shares issuable upon exercise of outstanding stock options.

| | 2017 | 2016 |
|---|---|---|
| **Basic income per share computation:** | | |
| Net income to common shareholders | $ 1,479,179 | $ 1,148,318 |
| Average common shares outstanding - basic | 219,635 | 219,635 |
| Basic income per common share | $ 6.73 | $ 5.23 |
| **Diluted income per share computation:** | | |
| Net income to common shareholders | $ 1,479,179 | $ 1,148,318 |
| Average common shares outstanding - basic | 219,635 | 219,635 |
| Incremental shares from assumed conversions: | | |
| Stock options | 544 | 147 |
| Average common shares outstanding - diluted | 220,179 | 219,782 |
| Diluted income per common share | $ 6.72 | $ 5.22 |

### Note 14. Regulatory Matters

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum ratios (set forth in the table below) of Tier 1, Common Equity Tier 1 (CET1), and total capital as a percentage of assets and off-balance-sheet exposures, adjusted for risk-weights ranging from 0% to 150%. Tier 1 capital of the Bank consists of common stockholders' equity, excluding the unrealized gain or loss on securities available-for-sale, minus certain intangible assets, while CET1 is comprised of Tier 1 capital, adjusted for certain regulatory deductions and limitations. Tier 2 capital consists of the allowance for loan losses subject to certain limitations. Total capital for purposes of computing the capital ratios consists of the sum of Tier 1 and Tier 2 capital.

The Bank is also required to maintain capital at a minimum level based on total average assets, which is known as the leverage ratio. Only the strongest institutions are allowed to maintain capital at the minimum requirement. All others are subject to maintaining ratios 1% to 2% above the minimum.

**Note 14. Regulatory Matters, Continued**

Effective March 31, 2015, quantitative measures established by applicable regulatory standards, including the newly implemented Basel III revised capital adequacy standards and relevant provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd Frank Act"), require the Bank to maintain (i) a minimum ratio of Tier 1 capital to average total assets, after certain adjustments, of 4.00%, (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of 6.00%, (iii) a minimum ratio of total-capital to risk-weighted assets of 8.00% and (iv) a minimum ratio of CET1 to risk-weighted assets of 4.50%. A "well-capitalized" institution must generally maintain capital ratios 2% higher than the minimum guidelines.

In order to avoid restrictions on capital distributions or discretionary bonus payments to executives, the Bank will also be required to maintain a "capital conservation buffer" in addition to its minimum risk-based capital requirements. This buffer will be required to consist solely of CET1, but the buffer will apply to all three risk-based measurements (CET1, Tier 1 and total capital). The capital conservation buffer will be phased in incrementally over time, beginning January 1, 2016 at 0.625% and becoming fully effective on January 1, 2019, and will ultimately consist of an additional amount of Tier 1 capital equal to 2.5% of risk-weighted assets. The capital conservation buffer in effect for the year ended December 31, 2017 was 1.25%.

As of December 31, 2017, management believes it is categorized as well-capitalized under the regulatory framework for prompt corrective action. There are no conditions or events that management believes have changed the Bank's category.

The following table summarizes the capital amounts and ratios of the Bank and the regulatory minimum requirements:

| *(Dollars in thousands)* | Actual | | For capital adequacy purposes Minimum | | To be well capitalized under prompt corrective action provisions Minimum | |
|---|---|---|---|---|---|---|
| | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| **December 31, 2017** | | | | | | |
| Total capital (to risk weighted assets) | $ 17,502 | 14.13% | $ 9,910 | 8.00% | $ 12,387 | 10.00% |
| Tier 1 capital (to risk weighted assets) | 16,334 | 13.19% | 7,432 | 6.00% | 9,910 | 8.00% |
| Tier 1 capital (to average assets) | 16,334 | 10.06% | 6,493 | 4.00% | 8,116 | 5.00% |
| Common Equity Tier 1 Capital (to risk-weighted assets) | 16,334 | 13.19% | 5,574 | 4.50% | 8,052 | 6.50% |
| **December 31, 2016** | | | | | | |
| Total capital (to risk weighted assets) | $ 16,659 | 14.24% | $ 9,362 | 8.00% | $ 11,702 | 10.00% |
| Tier 1 capital (to risk weighted assets) | 15,516 | 13.26% | 7,021 | 6.00% | 9,362 | 8.00% |
| Tier 1 capital (to average assets) | 15,516 | 10.06% | 6,168 | 4.00% | 7,710 | 5.00% |
| Common Equity Tier 1 Capital (to risk-weighted assets) | 15,516 | 13.26% | 5,266 | 4.50% | 7,607 | 6.50% |

**Note 15. Other Operating Expenses**

Other operating expenses are summarized as follows for the years ended December 31:

| | 2017 | 2016 |
|---|---|---|
| Stationery, printing and postage | $ 92,802 | $ 93,822 |
| Telephone | 50,765 | 46,407 |
| Director fees | 47,400 | 42,700 |
| Professional fees | 217,384 | 212,362 |
| Loan collection expenses | 5,574 | 21,861 |
| Insurance | 41,516 | 44,701 |
| Business development | 85,387 | 76,889 |
| Dues and publications | 48,693 | 48,462 |
| Meetings | 45,679 | 42,820 |
| Other | 308,743 | 255,297 |
| | $ 943,943 | $ 885,321 |

**Note 16. Unused Lines of Credit**

At December 31, 2017, the Bank had the ability to borrow an additional $7,474,132 from the FHLB secured by a blanket lien on pledged loan collateral. FHLB has approved borrowings up to 20% of the Bank's total assets less advances outstanding. The borrowings are available by pledging collateral and purchasing additional stock in the FHLB.

As of December 31, 2017, the Company had unused lines of credit to purchase federal funds from unrelated banks totaling $7,000,000. These lines of credit are available on a one to fourteen day basis for general reporting purposes. As of December 31, 2017, there were no amounts outstanding on these lines.

**Note 17. Restrictions on Dividends, Loans, or Advances**

The ability of the Company to pay cash dividends to shareholders is dependent upon receiving cash in the form of dividends from its banking subsidiary. However, certain restrictions exist regarding the ability of the subsidiary to transfer funds in the form of cash dividends to the Company. State chartered banks are authorized to pay cash dividends up to 100% of net income in any calendar year without obtaining the prior approval of the State Board of Financial Institutions or the Commissioner of Banking provided that the Bank received a composite rating of one or two at the last examination conducted by the State or Federal regulatory authority. Otherwise, the Bank must file an income and expense report and obtain the specific approval of the State Board.

During the year, the Bank transferred $715,165 to the Company to pay dividends. As of December 31, 2017, $788,463 of the Bank's retained earnings were available for dividends to the Company without prior regulatory approval.

Under Federal Reserve Board regulations, the amount of loans or advances from the banking subsidiary to the parent company are also restricted.

## Note 18. Financial Instruments With Off-Balance-Sheet Risk

The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments consist of commitments to extend credit and 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. A commitment involves, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The Company's exposure to credit loss in the event of nonperformance by the other party to the instrument is represented by the contractual notional amount of the instrument. Since certain commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company uses the same credit policies in making commitments to extend credit as it does for on-balance-sheet instruments. Letters of credit are conditional commitments issued to guarantee a customer's performance to a third party and have essentially the same credit risk as other lending facilities.

Collateral held for commitments to extend credit and letters of credit varies but may include accounts receivable, inventory, property, plant, equipment and income-producing commercial properties.

The following table summarizes the Bank's off-balance-sheet financial instruments at December 31, 2017 and 2016 whose contract amounts represent credit risk:

| | 2017 | 2016 |
|---|---|---|
| Commitments to extend credit | $ 21,615,253 | $ 14,768,284 |
| Letters of credit | 248,730 | 201,181 |

## Note 19. Fair Value of Financial Instruments

Accounting standards require disclosures about the fair value of assets and liabilities recognized in the balance sheet in periods subsequent to initial recognition, whether the measurements are made on a recurring basis (for example, available-for-sale investment securities) or on a nonrecurring basis (for example, impaired loans).

Fair value is defined as the exchange in price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. U.S. GAAP also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The Company utilizes fair value measurements to record fair value adjustments to certain assets and to determine fair value disclosures. Securities available-for-sale are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as loans held for sale, loans held for investment and certain other assets. These nonrecurring fair value adjustments typically involve application of lower of cost or market accounting or write-downs of individual assets.

**Note 19. Fair Value of Financial Instruments, Continued**

***Fair Value Hierarchy***
The Company groups assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine the fair value. These levels are:

Level 1 - Valuation is based upon quoted prices for identical instruments traded in active markets.

Level 2 - Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 - Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include the use of option pricing models, discounted cash flow models and similar techniques.

Following is a description of valuation methodologies used for assets and liabilities recorded at fair value:

***Investment Securities Available-for-Sale***
Investment securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange such as the New York Stock Exchange, Treasury securities that are traded by dealers or brokers in active over-the counter markets and money market funds. Level 2 securities include mortgage backed securities issued by government sponsored entities, municipal bonds and corporate debt securities. Securities classified as Level 3 include asset-backed securities in less liquid markets.

***Loans***
The Company does not record loans at fair value on a recurring basis, however, from time to time, a loan is considered impaired and an allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan are considered impaired. Once a loan is identified as individually impaired, management measures impairment. The fair value of impaired loans is estimated using one of several methods, including the collateral value, market value of similar debt, enterprise value, liquidation value or discounted cash flows. Those impaired loans not requiring a specific allowance represent loans for which the fair value of expected repayments or collateral exceed the recorded investment in such loans. At December 31, 2017 and 2016, substantially all of the impaired loans were evaluated based upon the fair value of the collateral. Impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the loan as nonrecurring Level 3.

**Note 19. Fair Value of Financial Instruments, Continued**

***Other Real Estate Owned***

Foreclosed assets are adjusted to fair value upon transfer of the loans to other real estate owned. Real estate acquired in settlement of loans is recorded initially at estimated fair value of the property less estimated selling costs at the date of foreclosure. The initial recorded value may be subsequently reduced by additional allowances, which are charges to earnings if the estimated fair value of the property less estimated selling costs declines below the initial recorded value. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company recorded the foreclosed asset as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the foreclosed asset as nonrecurring Level 3.

***Assets Recorded At Fair Value on a Recurring Basis***

The tables below present the balances of assets and liabilities measured at fair value on a recurring basis by level within the hierarchy.

| | December 31, 2017 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| Mortgage-backed securities | $ 916,126 | $ - | $ 916,126 | $ - |
| Government-sponsored enterprises | 2,496,343 | - | 2,496,343 | - |
| U.S. Treasury notes and bonds | 3,483,829 | - | 3,483,829 | - |
| Total | $ 6,896,298 | $ - | $ 6,896,298 | $ - |

| | December 31, 2016 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| Mortgage-backed securities | $ 1,538,331 | $ - | $ 1,538,331 | $ - |
| Government-sponsored enterprises | 2,641,353 | - | 2,641,353 | - |
| U.S. Treasury notes and bonds | 3,489,375 | - | 3,489,375 | - |
| Total | $ 7,669,059 | $ - | $ 7,669,059 | $ - |

There were no liabilities recorded at fair value on a recurring basis at December 31, 2017 and 2016.