IDAHO INDEPENDENT BANK®

2017
ANNUAL REPORT
TO SHAREHOLDERS

(This Annual Report to Shareholders has not been reviewed by the Federal Deposit Insurance Corporation.)

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March 5, 2018

Dear Shareholder(s),

The U.S. economy turned higher and gained momentum throughout 2017. Employment was up, and businesses and consumers became more and more optimistic as the year progressed. Home prices now exceed the highs recorded prior to the financial crisis. Idaho is a great place to be in business, and I am happy to report that Idaho Independent Bank ("IIB" or the "Bank") has been participating in the growth and prosperity.

Last year, IIB exceeded expectations in a number of important categories. As of December 31, 2017, the Bank's assets totaled $692.9 million, an increase of $74.1 million, or 12.0%, when compared to December 31, 2016. Loans, including those held-for-sale, increased $41.3 million, or 12.7%, to $365.9 million; while deposits and repurchase agreements increased $69.4 million, or 12.9%, to $608.3 million over the same timeframe. At year end, the allowance for loan and lease losses was at $6.5 million, or 1.8% of total loans, excluding loans held-for-sale, and nonperforming assets remained below 0.2% of total assets.

Net income before-tax for 2017 was $7.5 million compared to $4.9 million for 2016, an increase of 53.0%. This before-tax comparison is the best measure of IIB's improved profitability, as tax expense for 2016 included a $1.0 million benefit related to a reversal of the Bank's deferred tax valuation allowance, while 2017 included a one-time, $1.7 million cost due to a revaluation of deferred taxes to reflect the impact of the Tax Cuts and Jobs Act ("TCJA") having been signed into law on December 22, 2017. Because of the revaluation, IIB posted an after-tax loss of $0.3 million for the fourth quarter of 2017, or a loss of $0.04 per diluted share, compared to after-tax income of $1.2 million, or $0.15 per diluted share, for the fourth quarter of 2016. After-tax income for all of 2017 settled at $3.1 million, or $0.39 per diluted share, compared to $4.1 million, or $0.51 per diluted share, for 2016. To illustrate the magnitude of the tax differential, IIB's tax expense went from $0.8 million in 2016 to $4.5 million in 2017, an increase of $3.7 million. Of course, lower taxes will boost IIB's net earnings starting in 2018, as the Bank will be benefitting from the top corporate tax rate going from 35% down to 21%.

At December 31, 2017, the Bank's Stockholders' Equity to Average Total Assets was 9.7%, and all capital ratios exceeded the regulatory thresholds required to be considered "Well-Capitalized." This is after the Bank purchased 129,713 shares of its common stock at a cost of $1.3 million during 2017. As of year-end, IIB could purchase up to $0.8 million worth of additional shares under its increased and extended buyback plan. IIB's strong capital provides the foundation and support for future growth.

The general outlook for 2018 is positive. Wages are heading higher, household wealth is increasing, and unemployment is low. The global economy is strengthening, so manufacturers should be investing in plant and equipment to meet increased demand. Not only will the TCJA lower tax rates, but the generous depreciation rules related to expensing capital goods will further encourage business spending. Some relief from costly regulations is already contributing to efficiencies and optimism.

In addition, it appears as if the Federal Reserve will continue to move short-term interest rates higher. This is expected to help the Bank's net interest margin, as rates on its earning assets should move up at a faster pace than its cost of funds. On a cautionary note, things do not always go as expected. There can be disruptions such as escalated tensions in the Middle East and/or North Korea, a major cyber attack, a trade war, or a problem related to cryptocurrencies. Any one of these events could prompt a change in our priorities. Regardless, IIB expects surprises and will adjust or change its course of action as necessary and appropriate.

With that said, IIB can only focus on what it can control. We strive to build and retain long-term, mutually beneficial banking relationships based on quality service and high ethical standards. This philosophy has served us well in both good times and bad. Now, led by our Chief Executive Officer, Kurt Gustavel, we will reinforce and build on this proven philosophy. IIB has a great team of employees, officers, and Board of Directors, and their commitment and ability to execute on the Bank's strategies will continue to be our formula for success.

Finally, thank you for your confidence and for investing in IIB. Please call me at 208-292-1902, if you have any questions. Also, you are invited to attend the Bank's Annual Meeting of Shareholders to be held at our Coeur d'Alene Branch, 1260 W. Riverstone Drive, Coeur d'Alene, Idaho, on Wednesday, April 18, 2018, at 2:00 p.m. Pacific Daylight Time.

Sincerely,

/s/ Jack W. Gustavel

Jack W. Gustavel
Executive Chairman of the Board

Disclosure Regarding Forward-Looking Statements

Statements contained herein concerning future performance, developments or events, expectations for earnings, growth and market forecasts, and similar statements that are not historical facts are intended to be "forward-looking statements" as that term is defined in the Private Securities Litigation Reform Act of 1995, and as such, are subject to a number of risks and uncertainties that may cause actual results to differ materially from expectations or our stated objectives. Factors that could cause actual results to differ materially, include, but are not limited to, declines in regional and general economic conditions; changes in interest rates, deposit flows, demand for loans, real estate values, competition, and/or loan delinquency rates; changes in accounting principles, practices, policies, or guidelines; changes in legislation or regulations; changes in the regulatory environment; changes in monetary policy of the Federal Reserve Bank; changes in fiscal policy of the Federal government and the State of Idaho; changes in other economic, competitive, governmental, regulatory, and technological factors affecting operations, pricing, products, and services; material unforeseen changes in the liquidity, results of operations, or financial condition of the Bank's customers . Accordingly, these factors should be considered in evaluating forward-looking statements, and there should not be undue reliance placed on such statements. The Bank undertakes no responsibility to update or revise any forward-looking statements.

IDAHO INDEPENDENT BANK®

Report of Independent Auditors and Consolidated Financial Statements

December 31, 2017 and 2016

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REPORT OF INDEPENDENT AUDITORS

The Board of Directors and Stockholders
Idaho Independent Bank and Subsidiary

Report on Financial Statements

We have audited the accompanying consolidated financial statements of Idaho Independent Bank and Subsidiary (Bank), which comprise the consolidated statements of financial condition as of December 31, 2017 and 2016, and the related consolidated statements of income, comprehensive income, changes in stockholders' 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 audits 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 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 Idaho Independent Bank and Subsidiary as of December 31, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Moss Adams LLP

Spokane, Washington
February 9, 2018

IDAHO INDEPENDENT BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(In thousands, except share data)

	December 31, 2017	December 31, 2016
ASSETS		
Cash and cash equivalents:		
Cash and due from banks	$ 14,259	$ 12,693
Interest-bearing deposits in banks	54,850	9,482
Total cash and cash equivalents	69,109	22,175
Certificates of deposit ("CDs") held for investment, at cost	156,715	160,111
Trading securities, at fair value	4,370	3,776
Securities available for sale, at fair value	63,352	72,577
Federal Home Loan Bank stock, at cost	903	828
Loans held for sale	4,585	4,723
Loans receivable, net of allowance for loan losses of $6,522 and $6,124, respectively	354,830	313,788
Premises and equipment, net	15,362	15,792
Bank owned life insurance	14,673	14,242
Deferred tax asset, net	4,182	6,614
Other real estate owned	1,036	1,029
Accrued interest receivable and other assets	3,738	3,139
TOTAL ASSETS	$ 692,855	$ 618,794
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Deposits:		
Noninterest-bearing	$ 229,141	$ 205,479
Interest-bearing	349,265	306,947
Securities sold under agreements to repurchase, net	29,906	26,464
Notes payable	4,000	4,000
Accrued interest payable and other liabilities	14,575	11,825
Total liabilities	626,887	554,715
STOCKHOLDERS' EQUITY		
Preferred stock, $0.10 par value; 10,000,000 shares authorized; none issued	-	-
Common stock, $5 par value; 20,000,000 shares authorized;		
Issued and outstanding, net of treasury stock:	45,006	44,965
December 31, 2017 - 7,512,367		
December 31, 2016 - 7,633,918		
Capital surplus	42,014	41,954
Accumulated deficit	(3,756)	(6,810)
Accumulated other comprehensive loss	(77)	(144)
Treasury stock, at cost:	(17,219)	(15,886)
December 31, 2017 - 1,488,833 shares		
December 31, 2016 - 1,359,120 shares		
Total stockholders' equity	65,968	64,079
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 692,855	$ 618,794

See accompanying notes.

IDAHO INDEPENDENT BANK & SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
(In thousands, except share data)

	Years Ended December 31, 2017	Years Ended December 31, 2016
Interest and dividend income:		
Loans receivable, including fees	$ 19,674	$ 16,622
Securities available for sale	1,182	898
Interest-bearing deposits in banks and CDs	2,292	1,660
FHLB dividends	16	14
Total interest and dividend income	23,164	19,194
Interest expense:		
Deposits	353	285
Securities sold under agreements to repurchase and other borrowed funds	244	258
Total interest expense	597	543
Net interest income	22,567	18,651
Provision for loan losses	-	-
Net interest income after provision for loan losses	22,567	18,651
Noninterest income:		
Service charges on deposits	841	820
ATM and card transaction fees	1,683	1,580
Fee income on loans sold	2,834	3,392
Gain on sale or call of investments	11	15
Other income	2,120	1,422
Total noninterest income	7,489	7,229
Noninterest expense:		
Salaries	12,550	11,231
Employee benefits	2,491	2,314
Occupancy	1,858	1,826
Information technology	2,445	2,249
Furniture and equipment	485	470
Supplies and postage	378	434
Advertising and business development	719	652
Insurance and assessments	444	454
Other real estate owned, net	21	12
Other operating expenses	1,143	1,323
Total noninterest expense	22,534	20,965
Income before provision for income tax expense	7,522	4,915
Provision for income tax expense	4,468	779
NET INCOME	$ 3,054	$ 4,136
Earnings per common share:		
Basic	$ 0.40	$ 0.52
Diluted	$ 0.39	$ 0.51
Weighted average number of shares outstanding:		
Basic	7,587,992	7,936,267
Diluted	7,803,563	8,048,726

See accompanying notes.

IDAHO INDEPENDENT BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands)

	Years Ended December 31,	
	2017	**2016**
Net income	$ 3,054	$ 4,136
Other comprehensive income (loss):		
Unrealized holding gain (loss) on securities available for sale	120	(133)
Related tax benefit (expense)	(45)	51
Reclassification adjustment	(12)	8
Related tax benefit (expense)	4	(3)
Comprehensive income	$ 3,121	$ 4,059

 See accompanying notes.

IDAHO INDEPENDENT BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(In thousands, except share data)

	Common Stock						
	Shares	Amount	Capital Surplus	Accumu-lated (Deficit)	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total
Balance at December 31, 2015	8,114,758	$44,883	$41,866	$(10,946)	$(11,809)	$ (67)	$63,927
Stock-based compensation			130				130
Issuance of common stock for stock options exercised	16,349	82	(66)				16
Tax effect of exercised stock options			24				24
Treasury stock acquired, at cost	(497,189)				(4,077)		(4,077)
Net Income				4,136			4,136
Other comprehensive income (loss)						(77)	(77)
Balance at December 31, 2016	7,633,918	$44,965	$41,954	$(6,810)	$(15,886)	$ (144)	$64,079
Stock-based compensation			93				93
Issuance of common stock for stock options exercised	8,162	41	(33)				8
Treasury stock acquired, at cost	(129,713)				(1,333)		(1,333)
Net income				3,054			3,054
Other comprehensive income (loss)						67	67
Balance at December 31, 2017	7,512,367	$45,006	$42,014	$(3,756)	$(17,219)	$ (77)	$65,968

IDAHO INDEPENDENT BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Years Ended December 31, 2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 3,054	$ 4,136
Adjustments to reconcile net income to net cash provided (used) by operating activities:		
Gain on sale of or call of investments	(11)	(15)
Gain on sale of fixed assets	-	(83)
Gain on sale of repossessed assets	(230)	(5)
Depreciation and amortization	887	907
Net amortization of premium and discounts on investments	1,338	886
Provision for deferred income taxes	2,391	546
Net gain on sale of loans held for sale	(2,389)	(2,920)
Originations of loans held for sale	(102,894)	(114,119)
Proceeds from sales of loans held for sale	105,421	117,793
Stock-based compensation expense	93	130
Excess tax benefit from exercise of stock options	-	(24)
Increase in cash surrender value of life insurance	(431)	(468)
Changes in assets and liabilities:		
Interest receivable	(219)	(496)
Other assets	(564)	(786)
Interest payable	7	(3)
Other liabilities	643	1,065
Net cash provided by operating activities	7,096	6,544
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net decrease in CDs held for investment	3,396	2,627
Securities available for sale:		
Purchases	(23,201)	(46,348)
Proceeds from maturities or calls	26,707	22,577
Principal payments	4,500	1,965
Purchases of premises and equipment	(456)	(547)
Net purchases of Federal Home Loan Bank stock	(75)	(31)
Net increase in loans receivable	(39,298)	(33,465)
Proceeds from disposition of premises and equipment	-	974
Capital improvements to other real estate and property owned	(6)	(10)
Proceeds from sale of repossessed assets	174	-
Proceeds from sale of other real estate owned	-	12
Net cash used by investing activities	(28,259)	(52,246)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in deposits	65,980	52,455
Net increase in securities sold under agreements to repurchase	3,442	8,542
Excess tax benefits from exercise of stock options	-	24
Purchases of treasury stock	(1,333)	(4,077)
Proceeds from exercise of stock options	8	16
Net cash provided by financing activities	68,097	56,960

(continues on next page)

(In thousands)

	Years Ended December 31, 2017	Years Ended December 31, 2016
CHANGE IN CASH AND DUE FROM BANKS	46,934	11,258
Cash and due from banks, beginning of period	22,175	10,917
Cash and due from banks, end of period	$ 69,109	$ 22,175
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest	$ 590	$ 545
Income taxes	2,350	200
SUPPLEMENTAL CASH FLOWS DISCLOSURE ON NONCASH INVESTING TRANSACTIONS:		
Acquisition of real estate and other assets in settlement of loans	$ 1	$ 258
Loans made to finance sales of foreclosed assets	1,745	-
Fair value adjustment to securities available for sale, net of deferred income taxes	67	(77)

Note 1 - Summary of Significant Accounting Policies

Nature of business:
Idaho Independent Bank (the "Bank") is a state-chartered, commercial bank operating under the laws of the State of Idaho. The Bank began operations in October 1993 and has branches in Coeur d'Alene, Hayden, Boise (3), Meridian, Nampa, Caldwell, Mountain Home, Ketchum, and Star, Idaho.

Principles of consolidation:
The Bank's consolidated financial statements include the accounts of the Bank and its wholly-owned subsidiary, First Security Corporation. All intercompany transactions and balances have been eliminated in consolidation.

Basis of financial statement presentation:
The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of certain assets and liabilities as of the date of the statement of financial condition and certain revenues and expenses for the period. Actual results could differ, either positively or negatively, from those estimates.

Material estimates that are particularly susceptible to significant change in the near-term include the determination of the allowance for loan losses ("ALLL"), valuation of other real estate owned ("OREO") acquired in connection with foreclosures or in satisfaction of loans, recognition of deferred income tax assets and liabilities, and determining fair value of financial instruments.

Management believes the ALLL is adequate. While management uses currently available information to recognize losses on loans and OREO, future additions to the ALLL or valuation adjustments to OREO may be necessary based on changes in economic conditions or new information that becomes available. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Bank's ALLL and OREO. Such agencies may require the Bank to recognize additions to the ALLL or valuation adjustments based on their judgments of information available to them at the time of their examination. In connection with the determination of the ALLL and OREO, management generally obtains appraisals for significant properties.

Deferred income tax benefits and liabilities are valued based on current federal and state income tax rates. Actual recognition of these deferred tax assets and liabilities will be affected by applicable future tax rates that are in effect when the assets and liabilities become current tax items. At December 31, 2017, the Bank had a net deferred income tax asset in the amount of $4.2 million, reflecting adjustments to the Bank's deferred tax asset accounts, and a valuation allowance of $62,000. Management established the valuation allowance against the deferred income tax asset, in part, because it is uncertain when or if it will realize certain tax benefits. In the future, the Bank may be able to reduce some or all of the valuation allowance upon a determination that, more likely than not, it will be able to realize such tax benefits.

The fair value of financial instruments is subjective in nature and involve uncertainties and matters of significant judgment; therefore, the estimates are not necessarily indicative of the amounts the Bank could realize in a current market exchange.

Cash and cash equivalents:
Cash and cash equivalents include amounts on hand, due from banks, and interest-bearing deposits in other banks, excluding CDs held for investment. Cash and cash equivalents generally have a maturity of 90 days or less. The

Bank is required to maintain a reserve balance with the Federal Reserve Bank, or maintain such reserve in cash on hand. Cash balances on hand were sufficient to meet the required reserves at December 31, 2017 and 2016, of $1.0 million and $847,000, respectively.

CDs held for investment:
CDs held for investment with other financial institutions generally mature within two years and are carried at cost, which approximates fair value.

Trading securities:
Trading securities consist of debt and equity securities held in Rabbi Trusts in conjunction with the Bank's deferred compensation plan and are recorded at fair value. The Financial Accounting Standards Board ("FASB") ASC 710-10-25-15, *Deferred Compensation - Rabbi Trusts*, requires that changes in obligations associated with the deferred compensation plans be recorded in salary expense, while the corresponding change in plan assets be recorded in other income. The changes in obligations and asset values of the plan are equal and offsetting, such that there is no net impact to income. For the years ended December 31, 2017 and 2016, the Bank recorded offsetting salary expense and other noninterest income of $780,000 and $250,000, respectively.

Securities available for sale:
Available for sale securities typically consist of U.S. Treasuries, U.S. agencies, corporate notes, SBA guaranteed loan pools, and mutual funds not classified as trading securities or as held to maturity securities.

Unrealized holding gains and losses, net of tax, on available for sale securities are reported as a net amount in other comprehensive income (loss). Realized gains and losses on the sale of available for sale securities are determined using the specific-identification method and are included in the Consolidated Statements of Income under the Other Income heading. Purchase premiums and discounts are recognized in interest income over the period to maturity.

The Bank periodically evaluates each of its investments in debt and equity securities with a decline in market value below the amortized cost of the investment, to determine if the decline is deemed to be other-than-temporary. If it is determined that the impairment is other than temporary for equity securities, the impairment loss is recognized in earnings equal to the difference between the investment's cost and its fair value. If it is determined that the impairment is other than temporary for debt securities, the Bank will recognize the credit component of an other-than-temporary impairment in earnings and the noncredit component in other comprehensive income (loss) when the Bank does not intend to sell the security and it is more likely than not the Bank will not be required to sell the security prior to recovery. In evaluating investments with declines in value, the Bank considers the length of time and the extent to which the market value has been less than cost, the financial condition and near-term prospects of the issuer, and the Bank's intent or plans to sell with regard to the investment.

Federal Home Loan Bank of Des Moines ("FHLB") stock:
FHLB stock is a required investment for institutions that are members of the FHLB. The required investment in FHLB common stock is based on a predetermined formula and is carried at par value ($100 per share) on the Balance Sheet. The Bank may request redemption at par value of any stock in excess of the amount the Bank is required to hold. FHLB stock is restricted as to purchase, sale, and redemption. The Bank views its investment in FHLB stock as a long-term investment. Accordingly, when evaluating for impairment, the value is determined based on the ultimate recovery of the par value rather than recognizing temporary declines in value.

Loans held for sale:
Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated market value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income.

Loans receivable and allowance for loan losses:
The Bank grants commercial, real estate, and consumer loans to its customers. A substantial portion of the loan portfolio is represented by commercial and real estate loans made to borrowers and/or secured by collateral located in Idaho. The ability of the Bank's debtors to honor their contracts is dependent upon the real estate market and/or general economic conditions in the Bank's market areas.

Loans are stated at the amount of unpaid principal, adjusted for partial charge-offs, deferred loan fees and related costs, and an allowance for loan losses. Interest on loans is typically calculated by using the simple interest method on daily balances of the principal amount outstanding. Interest income is accrued on the unpaid balance. Certain loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the straight-line or effective interest method, depending on loan characteristics.

Loans are generally placed on a nonaccrual status when they are past due over 90 days, unless they are adequately collateralized and in the process of collection. Loans may be placed on nonaccrual status sooner than 90 days when, in the opinion of management, the collection of interest is doubtful. No interest is accounted for as income on nonaccrual loans unless received in cash or until such time as the borrower demonstrates an ability to resume payments of principal and interest. Generally, interest previously accrued but not collected is reversed and charged against income at the time a loan is placed on nonaccrual status. Loans may be returned to accrual status when none of the principal and interest is due and unpaid, and the Bank expects payment of the remaining contractual principal and interest, or when the loan otherwise becomes well secured and in the process of collection.

A loan is considered impaired when, based on current information and events, it is probable the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's financial condition and prior payment record, the amount of the shortfall in relation to the principal and interest owed, and an assessment of the borrower's ability to pay in the future. Impairment is measured on a loan-by-loan basis for non-homogeneous loan types by the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the estimated fair value of the collateral if the loan is collateral dependent.

The ALLL is maintained at a level deemed adequate by management to provide for estimated loan losses and risk in the loan portfolio through charges to operating expense. The ALLL is based on a continuing review of loans, which includes consideration of actual net loan loss experience, changes in the size and character of the loan portfolio, identification of individual problem situations that may affect the borrower's ability to pay, and an evaluation of current economic conditions. Loan losses are recognized through charges to the ALLL.

Other Real Estate Owned acquired in settlement of loans:
OREO acquired through foreclosure or deeds in lieu of foreclosure is stated at the lower of cost or estimated fair value. When the property is acquired, any excess of the loan balance over the estimated fair value is charged to the ALLL. The Bank generally obtains independent appraisals of OREO properties at the time of acquisition to assist in estimating fair value. Holding costs, subsequent write-downs to fair value, if any, or any disposition gains or losses are included in noninterest expenses. Significant costs of development and improvement of OREO are capitalized.

Earnings per share:
Earnings per share are computed by dividing net income by the total weighted average number of common shares outstanding and the additional dilutive effect of stock options during the respective periods. The dilutive effect of stock options is determined using the treasury stock method. Options to purchase 42,578 and 76,106 shares were outstanding but excluded in the computation of diluted earnings per share for December 31, 2017 and 2016, respectively, as the exercise price was greater than the average market price of the common shares.

Comprehensive income (loss):
Comprehensive income (loss) consists of net income (loss) and other comprehensive income (loss). Other comprehensive income (loss) includes unrealized gains and losses on securities available for sale, which are also recognized as separate components of equity.

Premises and equipment:
Premises and equipment are stated at cost less accumulated depreciation and amortization over estimated useful lives, which range from 2 to 40 years. Depreciation and amortization expense is computed using primarily the straight-line method for financial statement purposes. Accelerated depreciation methods are used for federal income tax purposes. Normal costs of maintenance and repairs are charged to expense as incurred.

Bank owned life insurance:
The carrying amount of bank owned life insurance approximates its fair value. Fair value of bank owned life insurance is estimated using the cash surrender value, net of surrender charges, if any.

Valuation of long-lived assets:
The Bank, using its best estimates based on reasonable and supportable assumptions and projections, reviews assets for impairment whenever events or changes in circumstances have indicated that the carrying amount of its assets might not be recoverable. In accordance with FASB ASC 360, *Property, Plant, and Equipment*, impaired assets are reported at the lower of cost or fair value. At December 31, 2017 and 2016, no significant property, plant, or equipment assets had been written down for impairment.

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

Advertising costs:
Costs incurred for advertising, merchandising, community investment, and business development are classified as advertising and business development and are expensed as incurred.

Income taxes:
Deferred income taxes are reported for temporary differences between items of income or expense reported in the financial statements and those reported for income tax purposes. Deferred taxes are estimated using the asset and liability approach. Under this method, a deferred tax asset or liability is determined based on management's estimate of the enacted tax rates that will be in effect when the differences between the financial statement carrying amounts and tax basis of existing assets and liabilities are expected to be reported in the Bank’s income tax returns. The deferred tax provision for the year is equal to the net change in the net deferred tax asset from the beginning to the end of the year, less amounts applicable to the change in value related to investments available for sale. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date.

As of December 31, 2017, management determined the amount of the deferred tax asset valuation allowance to be $62,000 by evaluating the nature and amount of historical and projected future taxable income, the scheduled reversal of deferred tax assets and liabilities, and the timing and amount of net operating loss carryforwards. The ability to utilize deferred tax assets is a complex process requiring in-depth analysis of, among many variables, statutory, judicial, and regulatory guidance, the level of loss carryforwards, and estimates of future taxable income and tax rates. The amount of deferred tax assets recognized in the future could be impacted by changes to any of these variables.

FASB ASC 740-10, *Income Taxes* requires recognition and measurement of uncertain tax positions using a "more-likely-than-not" approach. The Bank’s approach to FASB ASC 740-10 consisted of an examination of its financial statements, its income tax provision, and its federal and state income tax returns. The Bank analyzed its tax positions including the permanent and temporary differences as well as the major components of income and expense. As of December 31, 2017, the Bank did not believe it had any uncertain tax positions that would rise to the level of having a material effect on its financial statements. In addition, the Bank had no accrued interest or penalties related to income taxes as of December 31, 2017. It is the Bank’s policy to record interest and penalties as a component of income tax expense.

Stock options:
At December 31, 2017, the Bank had in effect a stock-based compensation plan for employees, as well as the Board of Directors, which is described more fully in Note 13. The Bank accounts for the plan under the fair value recognition provision of FASB ASC 718, *Compensation – Stock Compensation,* which requires companies to recognize in the statement of income the grant-date fair value of stock options and other equity-based forms of compensation issued to employees and directors over the requisite service period (generally the vesting period). The fair value of each option grant is estimated by the Bank as of the grant date using the Black-Scholes option-pricing model. This involves assumptions calculated using management’s best estimates at the time of the grant, which impacts the fair value of the option calculated under the Black-Scholes methodology and, ultimately, the expense that will be recognized over the life of the option. Actual results could materially differ, either positively or negatively, from those estimates.

Recent accounting pronouncements:
In May 2014, the FASB issued Accounting Standards Update (“ASU”) 2014-09, *Revenue From Contracts With Customers (Topic 606)*. The ASU outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. The ASU applies to all contracts with customers except those that are within the scope of other topics, such as certain financial instruments (e.g. receivables, debt securities, and transfers of financial assets). The guidance in this ASU was effective for reporting periods beginning after December 15, 2016. However, in August 2015, the FASB issued ASU 2015-04, which delayed the effective date of

ASU 2014-09 for reporting periods beginning after December 15, 2017. The Bank's primary source of revenue is interest income from receivables. Accordingly, the adoption of the ASU is not expected to have a material impact on the Bank's financial condition or results of operations.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. The ASU will change the manner in which leases are accounted for, particularly for operating lease arrangements with a term of more than 12 months will be reflected on the Bank's balance sheet as a right of use asset and a corresponding lease liability. For public business entities, the guidance in this ASU is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2018. Once adopted, the Bank expects to report right-of-use assets and liabilities for substantially all of its operating leases commitments. However, based on current leases, the adoption is not expected to have a material impact on the Bank's financial condition or results of operations.

In March 2016, the FASB issued ASU 2016-09, *Improvements to Employee Share-Based Payment Accounting*. The ASU simplifies several aspects of the accounting for share-based payment transactions, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. For public business entities, the guidance in this ASU was effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2016. The adoption of ASU No. 2016-09 did not have a material impact on the Bank's financial condition or results of operations.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326)*. The ASU amends the guidance on the impairment of financial instruments. The ASU adds an impairment model known as the current expected credit loss ("CECL") model that is based on expected losses rather than incurred losses. Under the new guidance, the Bank recognizes as an allowance its estimate of expected credit losses, which the FASB believes will result in more timely recognition of losses when compared to the model currently used for establishing the ALLL. For public business entities that are not SEC filers, the guidance in this ASU is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2020. While the Bank is currently evaluating the provisions of this ASU to determine the impact on the Bank's financial condition or results of operations, it expects the ALLL to increase as a result of the adoption of this ASU. The extent of this increase will depend upon economic conditions and the composition of the Bank's loan portfolio at the time of adoption.

In March 2017, the FASB issued ASU 2017-08, *Receivables – Nonrefundable Fees and Other Costs (Subtopic 310-20)*. The ASU shortens the amortization period for certain callable debt securities held at a premium. The ASU is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2018. The adoption of ASU is not expected to have a material impact on the Bank's financial condition or results of operations.

Reclassifications:
Certain reclassifications have been made to prior year's financial statements to conform to the current year's presentation. The reclassifications had no effect on previously reported net income or equity.

Subsequent events:
Subsequent events are events or transactions that occur after the date of the balance sheet but before the consolidated financial statements are available to be issued. The Bank recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the statement of financial condition, including the estimates inherent in the process of preparing of the financial statements. The Bank's consolidated financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statement of financial condition but arose after the date of the statement of

financial condition and before the financial statements are available to be issued.

The Bank has evaluated subsequent events through February 9, 2018**,** which is the date the financial statements were available to be issued.

Note 2 - Securities Available for Sale

The carrying amounts and estimated fair values of securities available for sale are summarized as follows:

December 31, 2017	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(in thousands)			
U.S. Treasury and agency securities	$ 8,798	$ -	$ (20)	$ 8,778
Corporate bonds	24,984	4	(101)	24,887
SBA guaranteed loan pools	28,694	112	(84)	28,722
Mutual funds	1,000	-	(35)	965
	$ 63,476	$ 116	$ (240)	$ 63,352

December 31, 2016	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(in thousands)			
U.S. Treasury and agency securities	$ 11,052	$ 7	$ (9)	$ 11,050
Corporate bonds	37,258	35	(159)	37,134
SBA guaranteed loan pools	23,499	55	(126)	23,428
Mutual funds	1,000	-	(35)	965
	$ 72,809	$ 97	$ (329)	$ 72,577

The contractual maturities of securities available for sale at December 31, 2017, are shown below. Expected maturities may differ from contractual maturities because issuers may have amortizing structures and/or have the right to call or prepay obligations with or without penalty.

	Amortized Cost	Estimated Fair Value
	(in thousands)	
Maturing in one year or less	$ 19,313	$ 19,288
Maturing in one to five years	15,511	15,419
Maturing in five to ten years	6,210	6,185
Maturing in more than ten years	21,442	21,495
Mutual funds	1,000	965
Total	$ 63,476	$ 63,352

As of December 31, 2017 and 2016, the investment securities shown below had aggregate fair values that were less than their amortized cost, and therefore contained unrealized losses. At December 31, 2017, there were 74 securities and one mutual fund with unrealized losses, compared to 69 securities and one mutual fund at December 31, 2016, with unrealized losses. The Bank has evaluated these securities and determined the decline in value was temporary and primarily attributable to changes in market interest rates subsequent to their purchase. The Bank expects the fair value of these securities to recover as the securities approach their maturity dates or sooner if market yields for such securities decline. The Bank does not believe that these securities are other than temporarily impaired because of their credit quality or related to any issuer or industry specific event. In addition, management did not intend to sell these securities, nor did available evidence suggest it was more likely than not that management would be required to sell these securities.

The fair value of temporarily impaired securities, the amount of unrealized losses, and the length of time individual securities have been in a continuous unrealized loss position as of the periods indicated are shown below.

	Less Than 12 Months		12 Months or More		Total	
December 31, 2017	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
			(in thousands)			
U.S. Treasury and agency securities	$ 4,283	$ (8)	$ 3,496	$ (12)	$ 7,779	$ (20)
Corporate bonds	11,110	(28)	10,053	(73)	21,163	(101)
SBA guaranteed loan pools	12,285	(56)	4,564	(28)	16,849	(84)
Mutual funds	-	-	965	(35)	965	(35)
	$ 27,678	$ (92)	$ 19,078	$ (148)	$ 46,756	$ (240)

	Less Than 12 Months		12 Months or More		Total	
December 31, 2016	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
			(in thousands)			
U.S. Treasury and agency securities	$ 4,511	$ (9)	$ -	$ -	$ 4,511	$ (9)
Corporate bonds	20,120	(155)	498	(4)	20,618	(159)
SBA guaranteed loan pools	16,433	(119)	916	(7)	17,349	(126)
Mutual funds	-	-	965	(35)	965	(35)
	$ 41,064	$ (283)	$ 2,379	$ (46)	$ 43,443	$ (329)

During 2017, the Bank sold one available for sale security for $1.4 million, resulting in a gain of $1,040. During 2016, there were no sales of available for sale securities. At December 31, 2017 and 2016, U.S. Treasury and agency securities and SBA guaranteed loan pools with an amortized cost of $37.5 million and $34.6 million and a fair value of $37.5 million and $34.5 million, respectively, were pledged for securities sold under agreements to repurchase (see Note 8).

At December 31, 2017 and 2016, the Bank's investment portfolio did not contain any securities of an issuer, other than the U.S. Government, its agencies, and U.S. Government sponsored entities that had an aggregate value in excess of 10% of the Bank's stockholder's equity at those dates.

Note 3 - Loans Receivable and Allowance for Loan Losses

The following table sets forth the composition of the Bank's loan portfolio, excluding loans held for sale:

	December 31, 2017		December 31, 2016	
	Balance	Percent of Total	Balance	Percent of Total
	(dollars in thousands)			
Commercial and industrial	$ 61,427	17.0%	$ 49,050	15.3%
Owner occupied commercial real estate	80,504	22.2	73,140	22.8
Non-owner occupied commercial real estate	58,091	16.1	50,612	15.8
Land and land development	33,427	9.2	32,761	10.2
Real estate construction	42,488	11.7	40,953	12.8
1-4 family real estate	23,446	6.5	25,547	8.0
Home equity	27,229	7.5	24,904	7.8
Consumer	13,695	3.8	12,133	3.8
Other	21,652	6.0	11,337	3.5
Total loans	361,959	100.0%	320,437	100.0%
Less:				
Deferred loan fees	607		525	
Allowance for loan losses	6,522		6,124	
Loans receivable, net	$354,830		$313,788	

At December 31, 2017, loans totaling $139.4 million were pledged as collateral at the Federal Reserve Bank or the FHLB for overnight borrowings and FHLB advances (see Note 7).

Contractual interest rates on loans fall into the following fixed and variable components:

	2017	2016
	(in thousands)	
Fixed	$ 43,694	$ 40,834
Variable	318,265	279,603
Total loans receivable	$ 361,959	$ 320,437

Allowance for Loan Losses. The following tables summarize the changes in the ALLL and loans receivable that were evaluated individually and collectively for impairment at the dates indicated:

	Commercial & Industrial	Owner Occupied Commercial Real Estate	Non-Owner Occupied Commercial Real Estate	Land & Land Develop.	Real Estate Construction	1-4 Family Real Estate	Home Equity	Consumer	Other	Un-allocated	Total
						(in thousands)					
At or for the Year Ended December 31, 2017											
Allowance for loan losses:											
Beginning balance	$ 846	$ 779	$ 703	$ 1,226	$ 737	$ 255	$ 277	$ 201	$ 150	$ 950	$ 6,124
Charge-offs	(60)	-	-	-	-	-	-	(25)	-	-	(85)
Recoveries	9	-	2	382	-	4	-	14	72	-	483
Provision (recapture)	530	509	106	(1,016)	16	(63)	90	(18)	162	(316)	-
Ending balance	$ 1,325	$ 1,288	$ 811	$ 592	$ 753	$ 196	$ 367	$ 172	$ 384	$ 634	$ 6,522
Ending balance: individually evaluated for impairment	$ 20	$ 4	$ -	$ 67	$ -	$ -	$ -	$ -	$ -	$ -	$ 91
Ending balance: collectively evaluated for impairment	$ 1,305	$ 1,284	$ 811	$ 525	$ 753	$ 196	$ 367	$ 172	$ 384	$ 634	$ 6,431
Loans receivable:											
Ending balance	$ 61,427	$ 80,504	$ 58,091	$ 33,427	$ 42,488	$ 23,446	$ 27,229	$ 13,695	$ 21,652	-	$ 361,959
Ending balance: individually evaluated for impairment	$ 20	$ 95	$ -	$ 166	$ -	$ -	$ -	$ 1	$ -	-	$ 282
Ending balance: collectively evaluated for impairment	$ 61,407	$ 80,409	$ 58,091	$ 33,261	$ 42,488	$ 23,446	$ 27,229	$ 13,694	$ 21,652	-	$ 361,677

(in thousands)

	Commercial & Industrial	Owner Occupied Commercial Real Estate	Non-Owner Occupied Commercial Real Estate	Land & Land Develop.	Real Estate Construction	1-4 Family Real Estate	Home Equity	Consumer	Other	Un-allocated	Total
At or for the Year Ended December 31, 2016											
Allowance for loan losses:											
Beginning balance	$ 580	$ 1,179	$ 623	$ 1,431	$ 366	$ 245	$ 330	$ 136	$ 81	$ 1,143	$ 6,114
Charge-offs	(35)	-	-	(361)	-	-	-	(47)	-	-	(443)
Recoveries	12	145	-	163	-	2	-	12	119	-	453
Provision (recapture)	289	(545)	80	(7)	371	8	(53)	100	(50)	(193)	-
Ending balance	$ 846	$ 779	$ 703	$ 1,226	$ 737	$ 255	$ 277	$ 201	$ 150	$ 950	$ 6,124
Ending balance: individually evaluated for impairment	$ -	$ 9	$ -	$ 73	$ -	$ -	$ -	$ 1	$ -	$ -	$ 83
Ending balance: collectively evaluated for impairment	$ 846	$ 770	$ 703	$ 1,153	$ 737	$ 255	$ 277	$ 200	$ 150	$ 950	$ 6,041
Loans receivable:											
Ending balance	$ 49,050	$ 73,140	$ 50,612	$ 32,761	$ 40,953	$ 25,547	$ 24,904	$ 12,133	$ 11,337	-	$ 320,437
Ending balance: individually evaluated for impairment	$ -	$ 233	$ 301	$ 202	$ 304	$ -	$ -	$ 4	$ -	-	$ 1,044
Ending balance: collectively evaluated for impairment	$ 49,050	$ 72,907	$ 50,311	$ 32,559	$ 40,649	$ 25,547	$ 24,904	$ 12,129	$ 11,337	-	$ 319,393

Impaired Loans. The Bank performs regular credit reviews of the loan portfolio to help assess the credit quality of the portfolio and the adherence to underwriting standards. Periodic credit reviews of the loan portfolio may also identify loans that are considered potentially impaired. Typically, factors used in determining if a loan is impaired, include, but are not limited to: (1) loans internally designated as special mention or substandard, (2) loans that are on nonaccrual status, or (3) loans that are modified and are deemed to be troubled debt restructurings ("TDRs"). Potentially impaired loans are referred to management, who review and designate the loans to be classified as impaired. A loan is considered impaired when, based on current information and events, management determines it is probable the Bank will not collect all amounts due, including scheduled interest payments, according to the contractual terms of a loan. When the Bank identifies a loan as impaired, management measures the impairment using the current fair value of the collateral less selling costs, discounted cash flows, or the loan's market price. If it is determined that the value of the impaired loan is less than the recorded investment in the loan, the Bank either recognizes this impairment with a specific allowance recorded in the ALLL or charges the amount of the impairment against the ALLL.

The Bank's impaired loans at December 31, 2017, and December 31, 2016, are presented by loan class in the tables below.

At December 31, 2017	Unpaid Principal Balance (1)	Recorded Investment with no Allowance	Recorded Investment with an Allowance	Related Allowance
	(in thousands)			
Commercial & industrial	$ 20	$ -	$ 20	$ 20
Owner occupied commercial real estate	95	-	95	4
Non-owner occupied commercial real estate	-	-	-	-
Land & land development	166	-	166	67
Real estate construction	-	-	-	-
1-4 family real estate	-	-	-	-
Home equity	-	-	-	-
Consumer	1	1	-	-
Other	-	-	-	-
Total	$ 282	$ 1	$ 281	$ 91

At December 31, 2016	Unpaid Principal Balance (1)	Recorded Investment with no Allowance	Recorded Investment with an Allowance	Related Allowance
	(in thousands)			
Commercial & industrial	$ -	$ -	$ -	$ -
Owner occupied commercial real estate	233	-	233	9
Non-owner occupied commercial real estate	340	301	-	-
Land & land development	597	1	201	73
Real estate construction	304	304	-	-
1-4 family real estate	-	-	-	-
Home equity	-	-	-	-
Consumer	4	-	4	1
Other	-	-	-	-
Total	$ 1,478	$ 606	$ 438	$ 83

(1) The unpaid principal balance of impaired loans represents the principal owed by the borrower. The recorded investment of impaired loans is typically less than the unpaid principal balance primarily due to charge-offs and interest payments made on loans while on nonaccrual status.

The average recorded investment in impaired loans and the related interest income recognized for cash payments received were as follows:

	Year Ended December 31, 2017		Year Ended December 31, 2016	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
	(in thousands)			
Commercial & industrial	$ 4	$ 1	$ 75	$ 6
Owner occupied commercial real estate	152	11	1,283	190
Non-owner occupied commercial real estate	60	10	304	11
Land & land development	175	12	293	34
Real estate construction	122	18	101	4
1-4 family real estate	-	-	20	-
Home equity	-	-	-	-
Consumer	2	-	5	-
Other	-	-	-	-
Total	$ 515	$ 52	$ 2,081	$ 245

Troubled Debt Restructurings. Included in certain categories of impaired loans are TDRs on which the Bank has granted certain material concessions to the borrower as a result of the borrower experiencing financial difficulties. At December 31, 2017, and December 31, 2016, the Bank had $262,000 and $438,000 of TDRs consisting of loans that were modified at one time and were performing in accordance with their modified terms. In addition to these amounts, the Bank had TDRs of $0 and $604,000 at December 31, 2017, and December 31, 2016, identified as nonaccrual loans. The concessions granted by the Bank may include, but are not limited to: (1) a modification in which the maturity date, timing of payments, or frequency of payments is modified, (2) an interest rate lower than the current market rate for new loans with similar risk, or (3) a combination of the above.

If a borrower on a restructured accruing loan has demonstrated performance under the previous terms and shows the capacity to continue to perform under the restructured terms, the loan will remain on accrual status. Otherwise, the loan will be placed on nonaccrual status until the borrower demonstrates a sustained period of performance, which generally requires six consecutive months of payments, inclusive of consecutive payments made prior to restructuring. Loans identified as TDRs are evaluated for impairment using the present value of the expected cash flows or the estimated fair value of the collateral if the loan is collateral-dependent. The fair value is determined, when possible, by an appraisal or evaluation of the property less estimated costs related to liquidation of the collateral. The appraisal or evaluation amount may also be adjusted for current market conditions. Adjustments to reflect the present value of the expected cash flows or the estimated fair value of collateral-dependent loans are a component in determining an appropriate ALLL, and as such, may result in increases or decreases to the provision for loan losses in current and future earnings.

There were no loans identified as TDRs for the year ended December 31, 2017, and no loans identified as TDRs within the previous 12 months had a payment default. There was one real estate construction loan of $304,000 identified as a TDR in 2016 and that subsequently defaulted and was placed on nonaccrual status in 2016. The recorded investment in the loan was $304,000 at December 31, 2016. Payment default is generally defined as 90 days or more past due. Payment default would also include any loan that may be less than 90 days past due and where the borrower has been notified that the loan is in default.

Nonaccrual Loans. Loans are generally placed on a nonaccrual status when they are past due for over 90 days, that is, unless they are adequately collateralized and are in the process of collection. No interest is accounted for as income on nonaccrual loans unless received in cash or until such time as the borrower demonstrates an ability to resume payments of principal and interest. Generally, interest previously accrued but not collected is reversed and charged against income at the time a loan is placed on nonaccrual status.

Loans receivable identified as nonaccrual loans are presented by loan class in the table below.

	December 31, 2017	December 31, 2016
	(in thousands)	
Commercial:		
Commercial & industrial	$ 20	$ -
Owner occupied commercial real estate	-	-
Non-owner occupied commercial real estate	-	301
Land & land development	-	1
Real estate construction	-	304
Consumer, Residential, & Other		
1-4 family real estate	-	-
Home equity	-	-
Consumer	-	-
Other	-	-
Total	$ 20	$ 606

Credit Quality Indicators. The Bank utilizes internal risk ratings for its credit quality indicators. The internal risk ratings: (1) provide a basis for evaluating, monitoring, and reporting the overall quality of the loan portfolio, (2) promptly identify deterioration of loan quality and the need for remedial action, and (3) emphasize areas requiring upgrading of policies, procedures, or documentation.

The internal risk ratings are as follows:

Grade 1 – Excellent. Prime loans based on liquid collateral with adequate margins or supported by recent strong financials. This grade class includes loans secured by cash collateral.

Grade 2 – Better than Average Risk. Desirable loans of less stature than Grade 1, but with strong financials or secured by other collateral with a readily verifiable liquidation value and liquidity. This grade class includes loans secured by readily marketable securities as well as some unsecured loans to individuals with unquestionable integrity, cash flow, and with liquid primary and secondary sources of payment.

Grade 3 – Average Risk. Satisfactory loans of average or slightly below average financial strength, having some deficiency or vulnerability to changing economic or industry conditions, but currently performing and collectable. This grade class may include secured loans to a borrower with net worth sufficient to support the advance, but whose supporting assets may be illiquid.

Grade 4 – Watch. Loans that are currently collectable but are potentially weak and may have elevated credit risk factors, but not to the point of justifying a classification of Substandard. Loans in this category have some type of deficiency or vulnerability, which presents a greater risk than average, but they are currently performing and collectable. These loans have potential problems that require greater attention than the average loan, as they may deteriorate and constitute undue or unwarranted risk if not monitored adequately.

Grade 5 – Special Mention. Loans that are generally related to situations that may be temporary or may be corrected by management. These loans have actual or potential weaknesses that may, if not checked or corrected, weaken or cause some type of future jeopardy. Grade 5 credits are similar in severity to a Grade 4 credit. The characteristics of a Grade 5 credit may include improperly structured loans, inadequate loan agreements or covenants, incomplete or inadequate documentation, or inadequate controls over the collateral.

Grade 6 – Substandard. Loans that are inadequately protected by the current worth and paying capacity of the borrower(s)/guarantor(s), and/or of the collateral pledged. Loans in this class have a well-defined weakness that jeopardizes debt liquidation. Grade 6 loans are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Grade 7 – Doubtful. Loans with an element of probable loss and definite exposure if liquidated at the present time. This grade class includes credits requiring immediate and drastic action and secured loans with insufficient collateral and/or other sources to fully pay the Bank.

Grade 8 – Loss/Charged Off. Loans that have been charged off.

The credit quality indicators by loan class at December 31, 2017 and December 31, 2016, were as follows:

At December 31, 2017	Commercial & Industrial	Owner Occupied Commercial Real Estate	Non-Owner Occupied Commercial Real Estate	Land & Land Development	Real Estate Construction
			(in thousands)		
Commercial Credit Risk Profile by Internally Assigned Grade					
Grade:					
Average risk or better	$ 58,039	$ 79,032	$ 58,033	$ 30,227	$ 42,488
Watch	168	1,211	58	3,200	-
Special mention	-	-	-	-	-
Substandard	1,727	261	-	-	-
Doubtful	1,493	-	-	-	-
Total	$ 61,427	$ 80,504	$ 58,091	$ 33,427	$ 42,488

	1-4 Family Real Estate	Home Equity	Consumer	Other
		(in thousands)		
Consumer, Residential, and Other Credit Risk Profile by Internally Assigned Grade				
Grade:				
Average risk or better	$ 22,342	$ 27,053	$ 13,687	$ 21,652
Watch	1,104	176	8	-
Special mention	-	-	-	-
Substandard	-	-	-	-
Doubtful	-	-	-	-
Total	$ 23,446	$ 27,229	$ 13,695	$ 21,652

At December 31, 2016	Commercial & Industrial	Owner Occupied Commercial Real Estate	Non-Owner Occupied Commercial Real Estate	Land & Land Development	Real Estate Construction
			(in thousands)		
Commercial Credit Risk Profile by Internally Assigned Grade					
Grade:					
Average risk or better	$ 48,898	$ 71,420	$ 50,248	$ 28,372	$ 40,649
Watch	129	1,430	63	4,217	-
Special mention	-	-	-	-	-
Substandard	23	290	301	172	304
Doubtful	-	-	-	-	-
Total	$ 49,050	$ 73,140	$ 50,612	$ 32,761	$ 40,953

	1-4 Family Real Estate	Home Equity	Consumer	Other
		(in thousands)		
Consumer, Residential, and Other Credit Risk Profile by Internally Assigned Grade				
Grade:				
Average risk or better	$ 24,388	$ 24,639	$ 12,133	$ 11,337
Watch	1,159	265	-	-
Special mention	-	-	-	-
Substandard	-	-	-	-
Doubtful	-	-	-	-
Total	$ 25,547	$ 24,904	$ 12,133	$ 11,337

Aging Analysis. The following tables present an aging analysis of loans receivable by loan class at December 31, 2017, and December 31, 2016.

At December 31, 2017	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater	Total Past Due	Current	Total Loans Receivable	Loans > 90 Days and Accruing
				(in thousands)			
Commercial:							
Commercial & industrial	$ -	$ 20	$ -	$ 20	$ 61,407	$ 61,427	$ -
Owner occupied commercial real estate	-	-	-	-	80,504	80,504	-
Non-owner occupied commercial real estate	-	-	-	-	58,091	58,091	-
Land & land development	-	-	-	-	33,427	33,427	-
Real estate construction	-	-	-	-	42,488	42,488	-
Consumer, Residential, & Other:							
1-4 family real estate	76	-	-	76	23,370	23,446	-
Home equity	-	-	-	-	27,229	27,229	-
Consumer	18	2	-	20	13,675	13,695	-
Other	-	-	-	-	21,652	21,652	-
Total	$ 94	$ 22	$ -	$ 116	$ 361,843	$ 361,959	$ -

At December 31, 2016	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater	Total Past Due	Current	Total Loans Receivable	Loans > 90 Days and Accruing
				(in thousands)			
Commercial:							
Commercial & industrial	$ -	$ -	$ -	$ -	$ 49,050	$ 49,050	$ -
Owner occupied commercial real estate	-	-	-	-	73,140	73,140	-
Non-owner occupied commercial real estate	-	-	301	301	50,311	50,612	-
Land & land development	-	-	1	1	32,760	32,761	-
Real estate construction	-	-	304	304	40,649	40,953	-
Consumer, Residential, & Other:							
1-4 family real estate	-	-	-	-	25,547	25,547	-
Home equity	-	-	-	-	24,904	24,904	-
Consumer	-	-	-	-	12,133	12,133	-
Other	-	-	-	-	11,337	11,337	-
Total	$ -	$ -	$ 606	$ 606	$ 319,831	$ 320,437	$ -

Note 4 - Premises and Equipment

Major classifications of premises and equipment at December 31 are summarized as follows:

	2017	2016
	(in thousands)	
Land	$ 3,365	$ 3,365
Buildings	17,726	17,552
Leasehold improvements	1,323	1,247
Construction in progress	102	211
Computer equipment and software	3,451	3,405
Furniture, fixtures, and other equipment	7,638	7,677
Total cost	33,605	33,457
Less accumulated depreciation and amortization	18,243	17,665
Net book value	$ 15,362	$ 15,792

Depreciation and amortization expense for premises and equipment for the years ended December 31, 2017 and 2016, was $887,000 and $907,000, respectively.

Note 5 - Other Real Estate Owned

The following table presents the activity related to OREO for the years ended December 31:

	2017	2016
	(in thousands)	
Balance at beginning of year	$ 1,029	$ 768
Additions	7	267
Reductions	-	(6)
Valuation allowance	-	-
Balance at end of year	$ 1,036	$ 1,029

OREO properties are recorded at the lower of the recorded investment in the loan or the fair market value of the property, less expected selling costs. Net expenses related to holding OREO for the years ended December 31, 2017 and 2016, were $21,000 and $12,000, respectively. The Bank recorded a gain on sale of OREO for the year ended December 31, 2016, of $5,000.

As of December 31, 2017 and 2016, the Bank held no foreclosed residential real estate. The Bank had no residential real estate loan in the process of foreclosure as of December 31, 2017, and one in the process of foreclosure as of December 31, 2016.

Note 6 - Deposits

Major classifications of deposits at December 31 were as follows:

	2017	2016
	(in thousands)	
Demand	$ 229,141	$ 205,479
NOW and Money Market	247,524	208,279
Savings	85,801	81,929
Time, under $250,000	14,660	14,934
Time, $250,000 and over	1,280	1,805
Total deposits	$ 578,406	$ 512,426

At December 31, 2017, overdrafts totaling $103,000 were reclassified as loans receivable.

Scheduled maturities of time deposits are as follows (dollars in thousands):

Years ending December 31,	
2018	$ 11,049
2019	2,432
2020	1,998
2021	144
2022	287
Thereafter	30
Total	$ 15,940

Note 7 - Notes Payable and Other Borrowed Funds

The Bank has an operating line of credit with the FHLB totaling $82.8 million and access to the Federal Reserve Bank discount window totaling $13.0 million as of December 31, 2017. The amount available from the FHLB and the Federal Reserve Bank is based on the Bank’s eligible collateral that is pledged to each line of credit. The FHLB line of credit is collateralized by single-family mortgages, certain commercial real estate loans, and small business loans. Borrowings from the Federal Reserve Bank discount window are collateralized by certain commercial real estate loans and commercial loans. The Bank has unsecured lines of credit for overnight federal funds totaling $26.0 million with three correspondent banks as of December 31, 2017. The interest rate payable on these lines varies based on a number of factors, including the rates available that day in the federal funds market.

There were no overnight borrowings at December 31, 2017 and 2016. The Bank has a $4.0 million, 15-year note payable to the FHLB at 5.08% per annum. The note requires the payment of interest monthly, with the principal due upon maturity on February 21, 2020. At December 31, 2017, the Bank's unused credit lines with the FHLB, the Federal Reserve Bank, and correspondent banks totaled $78.0 million, $13.0 million, and $26.0 million, respectively, and are subject to certain collateral requirements. The interest rate payable on these lines varies based on a number of factors, including the rates available that day in the federal funds market.

Information concerning notes payable and overnight borrowings is summarized as follows:

	2017	2016
	(dollars in thousands)	
Notes Payable:		
Average balance during the year	$ 4,000	$ 4,000
Maximum month-end balance during the year	4,000	4,000
Average interest rate during the year	5.08%	5.08%
Overnight Borrowings:		
Average balance during the year	$ 46	$ 4,616
Maximum month-end balance during the year	-	9,200
Average interest rate during the year	0.83%	0.53%

Note 8 - Securities Sold Under Agreements to Repurchase, Net

Securities sold under agreements to repurchase, and securities sold under reverse repurchase agreements have been shown net in the Balance Sheet. Securities sold under agreements to repurchase typically mature overnight, but in some instances are established for fixed periods of time. All securities sold under agreements to repurchase transactions were conducted with deposit customers of the Bank. Securities sold under reverse repurchase agreements were delivered to the financial institution that arranged the transaction. The financial institution may have sold, loaned, or otherwise disposed of such securities to other parties in the normal course of operations and have agreed to resell to the Bank substantially identical securities at the maturities of the agreements. Information concerning securities sold under agreements to repurchase, net of securities sold under reverse repurchase agreements, is summarized as follows:

	2017	2016
	(dollars in thousands)	
Average balance during the year	$ 29,672	$ 24,086
Maximum month-end balance during the year	33,463	26,464
Average interest rate during the year	0.14%	0.12%

The following is a schedule of the class and fair value of securities sold under agreements to repurchase at December 31, 2017:

	Overnight	Fixed Term	Total
	(in thousands)		
U.S. Treasury and agency securities	$ 8,778	$ -	$ 8,778
SBA guaranteed loan pools	28,722	-	28,722
Total	$ 37,500	$ -	$ 37,500

Note 9 - Commitments and Contingencies

Lease commitments and contracts:
The Bank has entered into five operating lease agreements for branch and office space that have initial or remaining lease terms in excess of one year as of December 31, 2017. Certain lease payments may be adjusted periodically in accordance with the specific lease. Changes are typically based on the Consumer Price Index. The estimated future minimum annual rental payments under the branch and office leases at December 31, 2017, exclusive of taxes and other charges, are summarized as follows (in thousands):

Years ending December 31,	
2018	$ 362
2019	324
2020	310
2021	232
2022	79
Thereafter	23
Total	$ 1,330

Total rental expense for 2017 and 2016 amounted to $356,000 and $355,000, respectively, of which $57,655 was paid in each of those years to related parties (see Note 11).

Commitments to extend credit:
In the normal course of business, the Bank makes various commitments and incurs certain contingent liabilities that are not presented in the accompanying financial statements. The commitments and contingent liabilities include various guarantees and commitments to extend 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 agreement. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer’s creditworthiness on a case-by-case basis. The amount of collateral obtained, if it is deemed necessary by the Bank upon extension of the credit, is based on management’s credit evaluation of the borrower. Collateral held, if any, varies but may include deposits, securities, accounts receivable, inventory, fixed assets, and/or real estate properties.

Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. These guarantees are primarily issued to support public and private borrowing arrangements. Most of these arrangements mature within two years and are expected to expire without being drawn upon.

A reserve for probable losses is maintained at a level management considers adequate to provide for potential losses and risk related to such commitments through changes to operating expense. Losses are recognized through charges to the reserve. As of December 31, 2017, the balance of the reserve was $40,000.

At December 31, 2017 and 2016, commitments to extend credit were as follows:

	2017	2016
	(in thousands)	
Unfunded commitments under bankcard arrangements	$ 11,516	$ 11,730
Unfunded commitments under lines of credit and undisbursed contruction loans	122,898	102,334
Letters of credit	3,792	2,432
Total commitments	$ 138,206	$ 116,496

In addition, the Bank originates and subsequently sells residential real estate loans into the secondary market. Loans sold into the secondary market are sold with limited recourse to the Bank, meaning the Bank may be obligated to repurchase or provide indemnities for any loans that are not underwritten in accordance with the applicable investor underwriting guidelines. Historically, such repurchases and calls upon indemnities have been limited.

Legal proceedings:
Periodically, and in the ordinary course of business, various claims and lawsuits are brought by and against the Bank, such as claims to enforce liens, condemnation proceedings on properties in which the Bank holds security interests, claims involving the making and servicing of real property loans, and other issues incident to the business. In the opinion of management, the ultimate liability, if any, resulting from such claims or lawsuits existing at December 31, 2017, is not expected to have a material adverse effect on the financial position or results of operation or cash flows.

Note 10 - Income Taxes

The components of provision for income tax expense consist of the following:

	Years Ended December 31,	
	2017	2016
	(in thousands)	
Current tax expense		
Federal	$ 1,703	$ 198
State	374	35
	2,077	233
Deferred tax expense		
Federal	$ 603	$ 1,208
State	146	293
Deferred tax asset valuation allowance	(73)	(955)
Deferred tax asset revaluation	1,715	-
	2,391	546
Provision for income tax expense	$ 4,468	$ 779

The components of the net deferred income tax assets and liabilities in the statements of financial condition are as follows:

	December 31, 2017	December 31, 2016
	(in thousands)	
Deferred tax assets:		
Allowance for loan losses	$ 1,758	$ 2,404
Deferred compensation	1,626	2,359
Net operating loss carryforward	520	1,547
Accrued expenses	628	726
Deferred gains	594	179
Equity based compensation	286	462
Net unrealized loss on securities available for sale	33	88
Other	28	548
Total deferred tax assets before valuation allowance	5,473	8,313
Less valuation allowance	(62)	(163)
Total deferred tax assets	5,411	8,150
Deferred tax liabilities:		
Accumulated depreciation	462	637
Deferred loan fees	474	530
FHLB dividends	94	136
Prepaid expenses	38	64
Other	161	169
Total deferred tax liabilities	1,229	1,536
Net deferred tax asset	$ 4,182	$ 6,614

There was a current income tax receivable at December 31, 2017 and 2016, of $302,000 and $29,000, respectively. At December 31, 2017, the Bank had net operating loss carryforwards for state income tax purposes of $10.5 million, respectively, which will expire between 2030 and 2033.

Deferred income tax assets and liabilities are valued using current federal and state income tax rates. Actual recognition of these deferred tax assets and liabilities will be affected by the tax rates that are applicable when the assets and liabilities become current tax items. The effect of a change in tax laws or rates on deferred income tax assets and liabilities are recognized in the period that includes the enactment date. As a result of the Tax Cuts and Jobs Act that was signed into law on December 22, 2017, the Bank revalued its deferred tax assets and liabilities to account for the future impact of lower corporate income tax rates. The revaluation resulted in a one-time deferred income tax expense of $1.7 million. After the revaluation, the Bank had a net deferred income tax asset in the amount of $4.2 million at December 31, 2017, which also includes a $62,000 valuation allowance to the deferred tax asset account. Management determined and made the valuation allowance against the deferred income tax asset, in part, because it is uncertain when it will realize such tax benefits.

The difference between income taxes at the statutory federal rate of 34% and the Bank's actual tax provision is presented as follows:

	Year Ended December 31, 2017	2016
	(dollars in thousands)	
Federal income tax expense at statutory rates	$ 2,557	$ 1,671
Effect of permanent timing differences	(169)	(142)
State income taxes, net of federal benefit	368	240
Other	70	(35)
Change in valuation allowance	(73)	(955)
Deferred tax revaluation	1,715	-
Provision for Income tax expense	$ 4,468	$ 779
Effective tax rates	59.4%	15.9%

Currently, the Bank is subject to U.S. federal income tax and income tax in the State of Idaho. The Bank recognizes interest and penalties related to unrecognized tax benefits as income tax expense in the Statements of Income. During the years ended December 31, 2017 and 2016, the Bank recognized no interest and penalties related to unrecognized tax benefits.

Management believes the Bank has appropriate support for the income tax positions taken, and to be taken, on its tax returns and that its accruals for tax liabilities are adequate for the open years based on an assessment of many factors, including past experience and interpretations of tax law. The Bank had no unrecognized tax benefits at December 31, 2017 and 2016.

Note 11 - Related Party Transactions

Loans to related parties:
In the normal course of business, the Bank makes loans to its executive officers, directors, and affiliates of these individuals. In keeping with federal regulations, the loans to such persons were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with others and did not involve more than the normal risk of collectability or present other unfavorable terms, except for loans to executive officers of the Bank and family members who are also employees of the Bank, which were made pursuant to the Bank's Employee Loan Program and were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other employees of the Bank, and did not involve more than the normal risk of collectability or present other unfavorable terms. The Bank provides an Employee Loan Program as a benefit to all of its employees, including executive officers, pursuant to which employees may receive loans from the Bank on more favorable terms than those provided to non-employee customers. The Bank believes its Employee Loan Program complies with applicable federal regulations.

Activity for loans to its executive officers, directors, and affiliates of these individuals is as follows:

	December 31, 2017	December 31, 2016
	(in thousands)	
Balance, beginning of year	$ 419	$ 168
Principal additions	1,498	327
Principal payments	(139)	(76)
Balance, end of year	$ 1,778	$ 419

The Bank also accepts deposits from its executive officers, directors, and affiliated companies on substantially the same terms for comparable transactions with unrelated parties. The aggregate dollar amounts of these deposits were $1.0 million and $1.1 million at December 31, 2017 and 2016, respectively.

Operating leases:
The Bank leases part of its Hayden Branch and part of its Hayden operations facilities under a lease dated October 20, 1992, and modified on December 26, 2007, from Wynn Investments, LLC, a limited liability company owned by the Executive Chairman of the Board and members of his family, including the President / Chief Executive Officer of the Bank. Payments under the lease for the Hayden Branch and the Hayden operations facilities amounted to $57,655 and $57,655 for each of 2017 and 2016, respectively.

Note 12 - Employee Benefit Plan and Incentive Program

The Bank has a 401(k) profit sharing plan (the "Plan") covering employees of the Bank who meet certain age and service requirements. Participants may contribute up to 100% of their compensation to the Plan up to the Internal Revenue Code limit. The Bank may elect to make discretionary matching and/or profit sharing contributions each year. Plan participants vest in the Bank's matching contributions over five years according to the Plan. The Bank's contributions to the Plan were $238,000 and $211,000 for the years ended December 31, 2017 and 2016, respectively.

During 2001, the Bank initiated a deferred compensation plan utilizing a Rabbi Trust. A Rabbi Trust is a grantor trust that allows the employee to immediately diversify the deferred compensation into non-employer securities. On December 12, 2005, the Bank created a second Rabbi Trust in order to segregate and earmark the benefits that accrued under the deferred compensation plan before January 1, 2005, the effective date of Internal Revenue Code Section 409A ("409A"), from the benefits accruing after such date that will be subject to 409A. In accordance with the provisions of FASB ASC 710-10-25-15, *Deferred Compensation - Rabbi Trusts*, the assets and liabilities of the plan are presented in investments and other liabilities in the Consolidated Balance Sheets, respectively. The assets held by the trust are classified as trading securities with changes recorded to other income, and changes in the deferred compensation liability recorded to salaries expense. There were no contributions to the trust in the years ended December 31, 2017 and 2016. Payments from the trust in the years ended December 31, 2017 and 2016, were $186,000 and $161,000, respectively. Assets held in the Rabbi Trusts were $4.4 million and $3.8 million at December 31, 2017 and 2016, respectively.

The Bank has an Executive Nonqualified Retirement plan for the benefit of certain employees. The program may provide supplemental income to the participants following retirement. Participants accrue benefits ratably each year until retirement. The Bank is recording the salary obligation over the estimated remaining service lives of the participants. Expenses related to this program were $308,000 and $293,000 for the years ended December 31, 2017 and 2016, respectively. At December 31, 2017 and 2016, an estimated obligation of $3.1 million and $3.0 million, respectively, was included in other liabilities.

Note 13 - Stock Options

In April 2016, the shareholders of the Bank approved the Idaho Independent Bank 2016 Long-Term Equity Incentive Plan (the "2016 Plan"). In May 2004, the shareholders of the Bank approved the Idaho Independent Bank 2004 Long-Term Equity Incentive Plan (the "2004 Plan"). As of December 31, 2017, options to purchase 645,636 shares are outstanding under the 2016 and 2004 Plans to employees and directors. The options granted under the plans may be exercised any time after they have vested. The 2004 Plan expired during 2014; therefore, no further options will be granted under the 2004 plan. The exercise price for options granted is at least the fair market value of the optioned shares on the date of grant.

The following table presents the activity related to options under all plans for the years ended December 31, 2017 and 2016.

	2017		2016	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at beginning of year	636,314	$ 7.56	536,609	$ 7.24
Granted	67,300	11.10	138,650	8.13
Exercised	(8,162)	4.62	(16,349)	5.03
Forfeited	(20,268)	10.26	(22,596)	5.90
Expired	(29,548)	24.70	-	-
Outstanding at end of year	645,636	$ 7.15	636,314	$ 7.56
Options exercisable at year end	528,601		516,464	
Fair value of options granted during the year	$ 1.66		$ 1.44	

The following table summarizes information about stock options outstanding at December 31, 2017:

	Options Outstanding			Exercisable Options		
Range of Exercise Price	Number Outstanding	Weighted-Average Remaining Contractual Life (years)	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Remaining Contractual Life (years)	Weighted-Average Exercise Price
$ 0.00 - $ 5.00	104,630	4.8	$ 3.00	88,270	4.8	$ 3.00
$ 5.01 - $10.00	431,128	4.6	6.70	368,753	4.0	6.51
$10.01 - $15.00	67,300	9.9	11.10	29,000	9.9	11.10
$15.01 - $20.00	42,578	0.6	15.71	42,578	0.6	15.71
	645,636	4.9	$ 7.15	528,601	4.2	$ 6.91

The following is a summary of the intrinsic value of stock options at December 31, 2017, or exercised during the year ended December 31, 2017:

	Intrinsic Value [1]
	(in thousands)
Options outstanding at December 31, 2017	$3,001,296
Options exercisable at December 31, 2017	2,613,705
Options exercised in 2017	75,315

[1] Market value of options assuming they were vested and exercised as of December 31, 2017.

Total compensation of $181,000 from nonvested options at December 31, 2017, will be recognized in 2018 through 2022. The expense will be recognized over a weighted average period of 2.5 years. It is the Bank's present policy to issue new shares for the exercise of stock options.

Stock-based compensation costs are based on the estimated fair value of grants calculated as of the grant date using the Black-Scholes option-pricing model. The fair value of stock options granted is recognized as compensation expense in the period the options vest. Compensation expense is recognized in the operating activities section of the statement of cash flows. For the years ended December 31, 2017, and 2016 there were 67,300 and 138,650 stock options granted.

The following assumptions were used in estimating the fair value of options granted in 2017 and 2016:

	Options Granted in November 2017	Options Granted in May 2016	Options Granted in July 2016
Risk free interest rate	1.89%	1.11%	0.96%
Expected dividend yield	0.00%	0.00%	0.00%
Expected volatility	14.90%	19.38%	22.03%
Expected forfeiture rate	0.00%	0.00%	0.00%
Weighted-average expected life (yrs)	3.81	3.64	4.00

The Black-Scholes option-pricing model calculates the value of grants utilizing the risk free interest rate, the Bank's expected dividend yield, expected stock price volatility, expected life of stock options, and the estimated forfeiture rate of stock options. The Bank based the estimated risk-free rate on the U.S. Treasury yield curve in effect at the time of grant. The Bank has not paid, nor does it currently have any plans to pay, cash dividends, thus a 0% dividend yield has been assumed for the model. Calculation of expected volatility used in the Black-Scholes model is based on historical volatility observations. The expected life for use in the model was calculated based in part on an analysis of historical exercises of stock options.

FASB ASC 718 requires the Bank to estimate potential forfeitures of stock options and adjust compensation cost accordingly. The Bank has a limited number of option holders, and because of its historically moderate to low levels of employee turnover, the Bank anticipates minimal personnel changes. The estimate of forfeitures will be adjusted over the requisite service period to the extent that actual forfeitures differ, or are expected to differ, from such estimates. Any changes in estimated forfeitures will be recognized through a cumulative catch-up adjustment in the period of change and will likely impact the amount of stock compensation to be recognized in future periods.

It should be noted that the Black-Scholes model is only one of the methods available for estimating the value of stock options, and the Bank's use of the model should not be interpreted as a prediction of the actual value that may be realized on the exercise of options. It is highly likely that the actual value of the options will be significantly different, and the value actually realized, if any, will depend upon the excess of the market value of the Bank's common stock over the option exercise price at the time of exercise.

Note 14 - Concentrations of Credit Risk

Most of the Bank's loans, commitments, and standby letters of credit have been granted to customers and/or are secured by collateral located in the Bank's market areas. As such, significant changes in economic conditions or real estate prices in Idaho or with its primary industries could adversely affect the Bank's ability to collect loans. The concentrations of credit by type of loan are set forth in Note 3.

The Bank places its cash with adequately capitalized financial institutions. The amount on deposit fluctuates and may exceed the insured limits of the Federal Deposit Insurance Corporation, and the Bank is therefore exposed to credit risk on such deposits.

Note 15 - Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by state and federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under 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 classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. Banks (Basel III rules) became effective for the Bank on January 1, 2015, with full compliance with all of the requirements being phased in over a multi-year schedule, and full phased in by January 1, 2019. The Basel III rules include a new Common Equity Tier 1 capital ratio and require a minimum capital adequacy. The Basel III rules require the Bank have a Tier 1 leverage ration of 4.0%, a Common Equity Tier 1 ratio of 4.5%, a Tier 1 risk-based ratio of 6.0%, and a total risk-based ratio of 8.0%. The Bank is also required to establish a "conservation buffer" consisting of common equity Tier 1 capital equal to 2.5% of risk-weighted assets. An institution that does not meet the conservation buffer will be subject to restrictions on certain activities including payment of dividends, stock repurchases, and discretionary bonuses to executive officers. Management believes, as of December 31, 2017 and 2016, that the Bank met all capital adequacy requirements to which it is subject.

As of December 31, 2017, the most recent notification from the Federal Deposit Insurance Corporation and the State of Idaho Department of Finance categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier 1 risk-based, Common Equity Tier 1, and Tier 1 leverage ratios as set forth in the following tables. Management believes that there have been no conditions or events since receipt of the notification that changed the Bank's well capitalized status.

The Bank's actual and required minimum capital amounts and ratios are presented in the tables below.

	Actual		Minimum Required For Capital Adequacy Purposes		Minimum Required to Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(dollars in thousands)			
December 31, 2017:						
Tier 1 capital (to average assets)	$ 65,628	9.59%	$ 27,366	≥ 4.00%	$ 34,208	≥ 5.00%
Common Equity Tier 1 capital (to risk-weighted assets)	65,628	14.45%	20,436	≥ 4.50%	29,519	≥ 6.50%
Tier 1 capital (to risk-weighted assets)	65,628	14.45%	27,248	≥ 6.00%	36,331	≥ 8.00%
Total risk-based capital (to risk-weighted assets)	71,317	15.70%	36,331	≥ 8.00%	45,413	≥ 10.00%
December 31, 2016:						
Tier 1 capital (to average assets)	$ 62,588	10.17%	$ 24,626	≥ 4.00%	$ 30,782	≥ 5.00%
Common Equity Tier 1 capital (to risk-weighted assets)	62,588	14.17%	19,873	≥ 4.50%	28,706	≥ 6.50%
Tier 1 capital (to risk-weighted assets)	62,588	14.17%	26,498	≥ 6.00%	35,330	≥ 8.00%
Total risk-based capital (to risk-weighted assets)	68,124	15.43%	35,330	≥ 8.00%	44,163	≥ 10.00%

The Bank has an ongoing stock repurchase program. In 2017, 129,713 shares were repurchased at a weighted-average price of $10.27. In 2016, 497,189 shares were repurchased at a weighted-average price of $8.20. As of December 31, 2017, management had authorization to repurchase up to $820,000 of additional shares through December 20, 2018.

Note 16 - Fair Value Measurements

The fair value estimates that follow are subjective in nature and involve uncertainties and matters of significant judgment; therefore, they are not necessarily indicative of the amounts the Bank could realize in a current market exchange. The Bank has not included certain material items in its disclosure, such as the value of its long-term relationships with lending and deposit clients, since this is an intangible and not a financial instrument. Additionally, the estimates do not include any potential tax ramifications. There may be inherent weaknesses in calculation techniques and changes in the underlying assumptions used, including discount rates and estimates of future cash flows that could materially affect the results. For all of these reasons, the aggregation of the fair value calculations presented herein do not represent, and should not be construed to represent, the underlying value of the Bank.

FASB ASC 820-10, *Fair Value Measurements and Disclosures,* establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to quoted prices for identical instruments in active markets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under FASB ASC 820-10 are described below:

Level 1 - Quoted prices for identical instruments in active markets.

Level 2 - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable.

Level 3 - Instruments whose significant value drivers are unobservable.

The following table summarizes the Bank's financial instruments that were measured at fair value at December 31, 2017 and 2016.

Description of Financial Instrument	Fair Value	At December 31, 2017 Level 1	Level 2	Level 3
			(in thousands)	
Recurring:				
Trading securities				
Common stock	$ 1,420	$ 1,420	$ -	$ -
Mutual funds / Exchange Traded Funds				
Income funds	278	278	-	-
Equity funds	2,672	2,672	-	-
	4,370	4,370	-	-
Securities available for sale				
U.S. agency securities	8,778	-	8,778	-
Corporate bonds	24,887	-	24,887	-
SBA guaranteed loan pools	28,722	-	28,722	-
Mutual funds				
Income Funds	965	965	-	-
	63,352	965	62,387	-
Nonrecurring:				
Impaired loans [1]	191	-	-	191
Other real estate owned	1,036	-	-	1,036

Description of Financial Instrument	Fair Value	At December 31, 2016 Level 1	Level 2	Level 3
			(in thousands)	
Recurring:				
Trading securities				
Common stock	$ 1,502	$ 1,502	$ -	$ -
Mutual funds / Exchange Traded Funds				
Income funds	371	371	-	-
Equity funds	1,903	1,903	-	-
	3,776	3,776	-	-
Securities available for sale				
U.S. Treasury securities	1,997	-	1,997	-
U.S. agency securities	9,053	-	9,053	-
Corporate bonds	37,134	-	37,134	-
SBA guaranteed loan pools	23,428	-	23,428	-
Mutual funds				
Income funds	965	965	-	-
	72,577	965	71,612	-
Nonrecurring:				
Impaired loans [1]	657	-	-	657
Other real estate owned	1,029	-	-	1,029

[1] Impaired loans that have been written down to fair value or for which a specific reserve has been established.

The following table presents significant quantitative information about Level 3 fair value instruments measured at fair value on a non-recurring basis at December 31, 2017 and 2016.

	At December 31, 2017			
Description of Financial Instrument	Fair Value	Valuation Technique	Unobservable Inputs	Average Discount
	(Dollars in thousands)			
Impaired loans	191	Present value of expected cash flows	Discount rate applied to expected cash flows	32%
Other real estate owned	1,036	Appraisal	Adjustments to reflect current conditions and selling costs	14%

	At December 31, 2016			
Description of Financial Instrument	Fair Value	Valuation Technique	Unobservable Inputs	Average Discount
	(Dollars in thousands)			
Impaired loans	$ 301	Appraisal	Adjustments to reflect current conditions and selling costs	7%
Impaired loans	356	Present value of expected cash flows	Discount rate applied to expected cash flows	19%
Other real estate owned	1,029	Appraisal	Adjustments to reflect current conditions and selling costs	14%

The Bank used the following methods and significant assumptions to estimate fair value:

Securities. The fair values of trading securities and securities available for sale are determined, when possible, by obtaining quoted prices on nationally recognized securities exchanges. If quoted prices are not available, then fair values are estimated using pricing models from an investment service based on the securities relationship to other benchmark quoted securities.

Impaired loans. The fair values of impaired loans are determined using the present value of the expected cash flows or the estimated fair value of the collateral if the loan is collateral-dependent. The fair value is determined, when possible, by an appraisal of the property less estimated costs related to liquidation of the collateral. The appraisal amount may also be adjusted for current market conditions. Adjustments to reflect the fair value of collateral-dependent loans are a component in determining an appropriate ALLL. As a result, adjustments to the fair value of impaired loans may result in increases or decreases to the provision for loan losses in current and future earnings. There were no impaired loans that are measured for impairment using the fair value of the collateral at December 31, 2017.

Other Real Estate Owned. The fair values of real estate acquired through foreclosure or deeds in lieu of foreclosure are generally based on an appraisal of the property less estimated costs and discounts related to liquidation of the property. The appraisal amount may also be adjusted for current market conditions. Subsequent adjustments to the fair value of OREO are included in noninterest expenses.

Note 17 - Fair Value of Financial Instruments

The following presents the carrying amount, estimated fair value, and placement in the fair value hierarchy of the Bank's financial instruments at December 31, 2017 and 2016.

	At December 31, 2017				
	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
			(in thousands)		
Financial Assets:					
Cash and cash equivalents	$ 69,109	$ 69,109	$ 69,109	$ -	$ -
CDs held for investment	156,715	156,715	156,715	-	-
Trading securities	4,370	4,370	4,370	-	-
Securities available for sale	63,352	63,352	965	62,387	-
FHLB Stock	903	903		903	
Loans held for sale	4,585	4,585	-	4,585	-
Loans receivable, net	354,830	350,847	-	-	350,847
Bank owned life insurance	14,673	14,673	14,673	-	-
Financial Liabilities:					
Deposits	578,406	578,388	-	578,388	-
Securities sold under agreements to repurchase	29,906	29,906	29,906	-	-
Notes payable	4,000	4,231	-	4,231	-

	At December 31, 2016				
	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
			(in thousands)		
Financial Assets:					
Cash and cash equivalents	$ 22,175	$ 22,175	$ 22,175	$ -	$ -
CDs held for investment	160,111	160,111	160,111	-	-
Trading securities	3,776	3,776	3,776	-	-
Securities available for sale	72,577	72,577	965	71,612	-
FHLB Stock	828	828		828	
Loans held for sale	4,723	4,723	-	4,723	-
Loans receivable, net	313,788	312,140	-	-	312,140
Bank owned life insurance	14,242	14,242	14,242	-	-
Financial Liabilities:					
Deposits	512,426	512,434	-	512,434	-
Securities sold under agreements to repurchase	26,464	26,464	26,464	-	-
Notes payable	4,000	4,385	-	4,385	-

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See Note 16 for a description of the level in the fair value hierarchy.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments.

Cash and cash equivalents and CDs held for investment:
The carrying amount approximates fair value.

Trading securities and securities available for sale:
The fair values of securities are determined, when possible, by obtaining quoted prices on nationally recognized securities exchanges. If quoted prices are not available, then fair values are estimated using quoted prices of securities with similar characteristics.

Federal Home Loan Bank stock:
The carrying value of FHLB stock approximates fair value based on the respective redemption provisions.

Loans held for sale:
The fair value of mortgage loans held for sale is based on commitments on hand from investors or prevailing market prices.

Loans receivable:
Fair values for variable-rate loans that reprice frequently and have no significant change in credit risk are based on carrying values. For commercial real estate and commercial loans with maturities beyond one year, fair values are estimated using a discounted cash flow analysis, utilizing interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Loans with maturities of less than one year are estimated to have a fair value equal to the carrying value. Fair values for impaired loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

Bank owned life insurance:
The carrying value of bank owned life insurance is recorded at fair value, based upon the cash surrender value of the underlying insurance contracts.

Deposits:
The fair value of demand deposits, savings accounts, and certain money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit maturing beyond one year is estimated using discounted cash flow analyses with rates currently offered for deposits of similar remaining maturities. Certificates with maturities less than one year are valued at carrying values.

Notes payable and securities sold under agreements to repurchase:
The carrying amounts of securities sold under agreements to repurchase approximate their fair values. Fair values of notes payable to the FHLB and securities sold under agreements to repurchase, maturing beyond 90 days, are estimated using discounted cash flow analyses based on the Bank's current incremental borrowing rates for similar types of borrowing arrangements.

Other borrowed funds:
The carrying amount of other borrowed funds approximates their fair values. The loans are for very short periods, typically overnight.

Off-balance-sheet instruments:
Fair values of off-balance-sheet lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the borrower's credit standing. The fair value of such fees at December 31, 2017 and 2016, was not significant.

Note 18 - Earnings Per Share

Earnings per share ("EPS") is computed using the basic and the diluted weighted average number of common shares outstanding during the period. Basic EPS is computed by dividing the Bank's net income or loss available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted EPS is computed by dividing net income or loss by diluted weighted average shares outstanding, which include common stock equivalent shares outstanding using the treasury stock method, unless such shares are anti-dilutive. Common stock equivalents represent the number of shares underlying outstanding stock options awarded under the Bank's stock option plans.

The following table presents the computation of basic and diluted EPS for the periods indicated:

	Year Ended December 31,	
	2017	2016
	(in thousands, except share data)	
Basic EPS:		
Net income	$ 3,054	$ 4,136
Weighted average common shares outstanding	7,587,992	7,936,267
Basic EPS	$ 0.40	$ 0.52
Diluted EPS:		
Net income	$ 3,054	$ 4,136
Weighted average common shares outstanding	7,587,992	7,936,267
Net effect of dilutive stock options	215,571	112,459
Weighted average common shares outstanding and common stock equivalents	7,803,563	8,048,726
Diluted EPS	$ 0.39	$ 0.51

The Bank's stock is quoted on the OTC Pink open market under the symbol IIBK. The average market price per share used in the determination of the dilutive effect of stock options is the average of daily closing market prices for the respective years.

Note 19 - Selected Quarterly Financial Data (unaudited)

Results of operations on a quarterly basis were as follows (in thousands except share data):

	Year Ended December 31, 2017			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest and dividend income	$5,109	$5,659	$6,102	$6,294
Interest expense	138	144	152	163
Net interest income	4,971	5,515	5,950	6,131
Provision for loan losses	-	-	-	-
Net interest income after provision for loan losses	4,971	5,515	5,950	6,131
Noninterest income	1,775	1,792	1,953	1,969
Noninterest expense	5,513	5,433	5,652	5,936
Income before provision for income tax expense	1,233	1,874	2,251	2,164
Provision for income tax expense	450	684	844	2,490
NET INCOME (LOSS)	$783	$1,190	$1,407	($326)
Basic earnings (loss) per share [1]	$0.10	$0.16	$0.19	($0.04)
Diluted earnings (loss) per share [1]	$0.10	$0.15	$0.18	($0.04)

	Year Ended December 31, 2016			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest and dividend income	$4,443	$4,653	$5,023	$5,075
Interest expense	133	134	133	143
Net interest income	4,310	4,519	4,890	4,932
Provision for loan losses	-	-	-	-
Net interest income after provision for loan losses	4,310	4,519	4,890	4,932
Noninterest income	1,147	2,130	2,129	1,823
Noninterest expense	4,622	5,438	5,650	5,255
Income before provision for income tax expense	835	1,211	1,369	1,500
Provision for income tax expense	63	139	238	339
NET INCOME	$772	$1,072	$1,131	$1,161
Basic earnings per share [1]	$0.10	$0.13	$0.14	$0.15
Diluted earnings per share [1]	$0.09	$0.13	$0.14	$0.15

(1) Quarterly earnings (loss) per share may vary from annual earnings (loss) per share due to rounding.

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