Financial Statements
December 31, 2019 and 2018

Gateway Bank, F.S.B.

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Independent Auditor's Report

The Board of Directors and Shareholders
Gateway Bank, F.S.B.
Oakland, California

Report on the Financial Statements

We have audited the accompanying financial statements of Gateway Bank, F.S.B., which comprise the balance sheet as of December 31, 2019, and the related statements of operations, comprehensive loss, shareholders' equity, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

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Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Gateway Bank, F.S.B. as of December 31, 2019, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter
The financial statements of Gateway Bank, F.S.B. as of and for the year ended December 31, 2018, were audited by Vavrinek, Trine, Day & Co. LLP, who joined Eide Bailly LLP on July 22, 2019, and whose report dated June 7, 2019, expressed an unmodified opinion on those statements.

Laguna Hills, California
June 10, 2020

Gateway Bank, F.S.B.
Balance Sheets
December 31, 2019 and 2018

	2019	2018
Assets		
Cash and due from banks	$ 1,828,045	$ 2,307,775
Interest bearing deposits in other banks	2,935,695	206,933
Federal funds sold	30,339,693	19,158,554
Total cash and cash equivalents	35,103,433	21,673,262
Debt securities		
Available for sale	3,566,045	11,834,507
Held to maturity (fair value of $2,265,929)	-	2,285,865
Total debt securities	3,566,045	14,120,372
Loans held for investment, less allowance for loan losses of $1,581,025	83,165,520	68,176,335
Restricted stock, at cost	666,900	762,600
Mortgage servicing rights, at fair value	733,062	1,043,287
Premises and equipment, net	384,407	162,099
Right of use asset	952,251	-
Cash surrender value of bank owned life insurance	2,588,527	2,528,177
Accrued interest receivable and other assets	1,402,918	929,753
	$ 128,563,063	$ 109,395,885
Liabilities and Shareholders' Equity		
Deposits		
Non interest bearing	$ 3,314,826	$ 3,513,326
Interest bearing	92,254,446	88,930,621
Total deposits	95,569,272	92,443,947
FHLB advances	15,000,000	-
Lease liability	952,251	-
Accrued interest payable and other liabilities	1,196,448	1,046,688
Total liabilities	112,717,971	93,490,635
Commitments and Contingencies (Notes 6, 11 and 13)		
Shareholders' Equity		
Preferred stock Series C - no par value; 20,000,000 shares authorized; 12,664,357 shares issued and outstanding	3,687,191	3,687,191
Common stock - $0.10 par value; 100,000,000 shares authorized; 49,179,923 shares issued and outstanding	4,924,824	4,924,824
Additional paid-in-capital	34,323,167	34,323,167
Accumulated deficit	(27,105,545)	(26,724,050)
Accumulated other comprehensive income (loss)	15,455	(305,882)
Total shareholders' equity	15,845,092	15,905,250
	$ 128,563,063	$ 109,395,885

	2019	2018
Interest Income		
Interest and fees on loans	$ 3,960,188	$ 3,331,918
Interest on debt securities	355,094	391,056
Interest on federal funds sold and other	395,711	448,963
Dividends on restricted stock	63,237	75,587
Total interest income	4,774,230	4,247,524
Interest Expense		
Interest on deposits	908,900	679,150
Interest on borrowings	159,485	-
Total interest expense	1,068,385	679,150
Net Interest Income Before Provision for Loan Losses	3,705,845	3,568,374
Provision for Loan Losses	-	-
Net Interest Income After Provision for Loan Losses	3,705,845	3,568,374
Noninterest Income		
Loan servicing income	32,026	368,963
Gain on sale of investments	286,417	-
Net gain (loss) on other real estate sales and valuation allowance adjustments	14,839	(42,153)
Other income	222,553	180,293
Total noninterest income	555,835	507,103
Noninterest Expense		
Salaries and employee benefits	1,585,842	1,552,827
Occupancy and equipment	430,678	438,625
Legal fees	687,757	426,435
Professional and consulting fees	412,024	331,016
Data processing	360,978	1,076,205
Other expense	1,165,896	1,102,456
Total noninterest expense	4,643,175	4,927,564
Loss Before Income Tax Expense	(381,495)	(852,087)
Income Tax Expense	-	-
Net Loss	$ (381,495)	$ (852,087)
Earnings (loss) per common share	$ (0.01)	$ (0.03)

	2019	2018
Net Loss	$ (381,495)	$ (852,087)
Other Comprehensive Income (Loss)		
Reclassification adjustment for net realized gains	(286,417)	-
Changes in net unrealized gains (losses) on investments classified as available-for-sale	607,754	(212,396)
Total other comprehensive income (loss)	321,337	(212,396)
Comprehensive Loss	$ (60,158)	$ (1,064,483)

	Preferred Stock		Common Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	Shares	Amount	Shares	Amount				
Balance, January 1, 2018	12,664,357	$ 3,687,191	14,179,923	$ 1,424,824	$ 27,980,559	$ (25,871,963)	$ (93,486)	$ 7,127,125
Issuance of common stock, net of issuance costs of $657,392	-	-	35,000,000	3,500,000	6,342,608	-	-	9,842,608
Net loss	-	-	-	-	-	(852,087)	-	(852,087)
Other comprehensive loss	-	-	-	-	-	-	(212,396)	(212,396)
Balance, December 31, 2018	12,664,357	3,687,191	49,179,923	4,924,824	34,323,167	(26,724,050)	(305,882)	15,905,250
Net loss	-	-	-	-	-	(381,495)	-	(381,495)
Other comprehensive income	-	-	-	-	-	-	321,337	321,337
Balance, December 31, 2019	12,664,357	$ 3,687,191	49,179,923	$ 4,924,824	$ 34,323,167	$ (27,105,545)	$ 15,455	$ 15,845,092

	2019	2018
Operating Activities		
Net loss	$ (381,495)	$ (852,087)
Adjustments to reconcile net loss to net cash from operating activities		
Depreciation and amortization	63,410	42,194
Amortization on securities	16,944	47,761
Provision for loan losses	-	-
Decrease in fair value of mortgage servicing rights	310,225	21,407
Increase in cash surrender value of life insurance	(60,350)	(59,442)
Gain on sale of investments	(286,417)	-
Net (gain) loss on other real estate sale and valuation allowance adjustments	(14,839)	42,153
Changes in other assets and liabilities		
Accrued interest receivable and other assets	(473,165)	150,613
Accrued interest payable and other liabilities	275,910	(872,306)
Net Cash from Operating Activities	(549,777)	(1,479,707)
Investing Activities		
Proceeds from redemption of Federal Home Loan Bank stock	95,700	24,000
Proceeds from sales of investment securities	15,030,292	-
Proceeds from principal repayments of investment securities	1,254,163	3,248,595
Purchase of AFS securities	(1,300,000)	(1,100,000)
Purchase of HTM securities	(3,839,318)	-
Net change in loans	(15,272,469)	7,665,959
Purchase of premises and equipment	(285,718)	-
Proceeds from sale of other real estate owned	298,123	806,394
Net Cash from Investing Activities	(4,019,227)	10,644,948
Financing Activities		
Net increase (decrease) in deposits	2,999,175	(18,260,361)
Proceeds from long-term FHLB advances	15,000,000	-
Proceeds from issuance of stock, net of issuance costs	-	9,842,608
Net Cash from Financing Activities	17,999,175	(8,417,753)
Change in Cash and Cash Equivalents	13,430,171	747,488
Cash and Cash Equivalents, Beginning of Year	21,673,262	20,925,774
Cash and Cash Equivalents, End of Year	$ 35,103,433	$ 21,673,262
Supplemental Disclosure of Cash Flow Information		
Cash paid during the year for		
Interest expense	$ 1,067,776	$ 680,187
Income taxes	$ -	$ -
Non Cash Activities		
Other real estate acquired in foreclosure	$ 283,284	$ -
Transfer of HTM securities to AFS	$ 6,098,357	$ -

See Notes to Financial Statements

Note 1 - Summary of Significant Accounting Policies

The accounting and reporting policies of Gateway Bank, F.S.B. ("the Bank") are in accordance with accounting principles generally accepted in the United States of America and conform to practices within the banking industry.

A summary of the Bank's significant accounting policies follows:

Nature of Operations

The Bank was incorporated in June 1990. The Bank consolidated its operations in 2015 and currently occupies one location in the Chinatown district of Oakland, California. All banking and administrative operations are housed in the Chinatown branch location with the Bank providing traditional banking products to the surrounding community.

The Bank operates under a charter granted by the Office of the Comptroller of Currency ("OCC") and its deposit accounts are insured by the Federal Deposit Insurance Corporation ("FDIC"). The Bank is also an approved Community Development Financial Institution ("CDFI") with a stated mission to provide banking services to people and communities who are underserved by mainstream commercial banks and lenders. The Bank's stock began trading in the over-the-counter markets (ticker symbol GWBK) in 2019 and therefore is a public business entity for financial reporting purposes.

Subsequent Events

The Bank has evaluated subsequent events for recognition and disclosure through June 10, 2020, which is the date the financial statements were available to be issued. See Note 20 for additional subsequent event considerations relative to the COVID-19 pandemic and Note 11 for disclosure of a large settlement gain received and recognized into income in 2020.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term are mortgage servicing rights and the determination of the allowance for loan losses.

Cash and Cash Equivalents

For purposes of reporting cash flows cash and cash equivalents include cash, time deposits with other financial institutions with maturities of 90 days or less and federal funds sold. Generally, federal funds are sold for one day periods.

Cash and Due from Banks

Banking regulations require that all banks maintain a percentage of their deposits as reserves in cash or on deposit with the Federal Reserve Bank. The Bank complied with the reserve requirements as of December 31, 2019. The Bank maintains amounts due from banks that may exceed federally insured limits. The Bank has not experienced any losses in such accounts.

Debt Securities

Debt securities are classified in three categories and accounted for as follows: debt securities that the Bank has the positive intent and ability to hold to maturity are classified as held-to-maturity and are measured at amortized cost; debt securities bought and held principally for the purpose of selling in the near term are classified as trading securities and are measured at fair value, with unrealized gains and losses included in earnings; debt securities not classified as either held-to-maturity or trading securities are deemed as available-for-sale and are measured at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of shareholders' equity. Gains or losses on sales of debt securities are determined on the specific identification method. Premiums and discounts are amortized or accreted using the interest method over the expected lives of the related securities.

Management evaluates debt securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation. For debt securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a debt security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: OTTI related to credit loss, which must be recognized in the income statement and OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis.

Loans Held for Investment

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at their outstanding unpaid principal balances reduced by any charge-offs or specific valuation accounts and net of any deferred fees or costs on originated loans, or unamortized premiums or discounts on purchased loans. Loan origination fees and certain direct origination costs are deferred and recognized in interest income using the level-yield method without anticipating prepayments. Premiums and discounts on loans purchased are grouped by type and certain common risk characteristics and amortized or accreted as an adjustment of yield over the weighted-average remaining contractual lives of each group of loans, adjusted for prepayments when applicable, using methodologies which approximate the interest method.

Loans on which the accrual of interest has been discontinued are designated as nonaccrual loans. The accrual of interest on loans is discontinued when principal or interest is past due 90 days or when, in the opinion of management, there is reasonable doubt as to collectability based on contractual terms of the loan. When loans are placed on nonaccrual status, all interest previously accrued but not collected is reversed against current period interest income. Income on nonaccrual loans is subsequently recognized only to the extent that cash is received and the loan's principal balance is deemed collectible. Interest accruals are resumed on such loans only when they are brought current with respect to interest and principal and when, in the judgment of management, the loans are estimated to be fully collectible as to all principal and interest.

The Bank's real estate loan portfolio consists primarily of long-term loans (15-30 years) collateralized by first and second deeds of trust on one to four unit residential real estate properties. A substantial portion of the real estate loan portfolio is comprised of adjustable-rate mortgages. The interest rate and payment terms of these mortgages adjust on a periodic basis in accordance with various published indices. The majority of these adjustable-rate mortgages have terms which limit the amount of interest rate adjustment that can occur each year and over the life of the mortgage.

Allowance for Loan Losses

The allowance for loan losses for loans held for investment is established through a provision for loan losses charged to operating income. Originated loans are charged against the allowance for loan losses when management believes that the collectability of the principal is unlikely. The allowance is an amount that management believes will be adequate to absorb probable losses inherent in existing loans, based on evaluations of the collectability, impairment, and prior loss experience of loans. The evaluations take into consideration such factors as changes in the nature and size of the portfolio, overall portfolio quality, loan concentrations, specific problem loans, and current economic conditions that may affect the borrower's ability to pay.

All specifically identifiable and quantifiable losses are immediately charged off against the allowance. However, for a variety of reasons, not all losses are immediately known to the Bank and, of those that are known, the full extent of the loss may not be quantifiable at that point in time. The balance of the Bank's allowance for loan losses is meant to be an estimate of these unknown but probable losses inherent in the portfolio.

The Bank's Internal Asset Review Committee, Board of Directors, and Executive Loan Committee assess the adequacy of the allowance for loan losses at least quarterly. The Bank's method for assessing the appropriateness of the allowance for loan losses includes specific allowances for impaired loans, formula allowance factors for pools of credits, and allowances for changing qualitative factors (e.g., interest rates, growth, economic conditions, etc.). Allowance factors for loan pools are based on historical loss experience by loan type. Allowances for impaired loans are based on analysis of individual credits. Allowances for changing environmental factors are management's best estimate of the probable impact these changes have had on the loan portfolio as a whole.

The Bank defines a loan as impaired when it is probable the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's original effective interest rate. As a practical expedient, impairment may be measured based on the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. When the measure of the impaired loan is less than the recorded investment in the loan, the impairment is recorded through a valuation allowance charged to earnings.

In situations related to loans where, for economic or legal reasons related to a borrower's financial difficulties, the Bank grants a concession for other than an insignificant period of time to the borrower that the Bank would not otherwise consider, the related loan is classified as a troubled debt restructuring ("TDR"). The Bank strives to identify borrowers in financial difficulty early and work with them to modify to more affordable terms before their loan reaches nonaccrual status.

These modified terms may include rate reductions, principal forgiveness, payment forbearance and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. In cases where the Bank grants the borrower new terms that provide for a concession (e.g., reduction of either interest or principal), the loan is deemed impaired and the Bank therefore measures any impairment on the restructuring as noted above for impaired loans. TDR loans are generally classified as impaired until they are fully paid off or charged off. Loans that are in nonaccrual status at the time they become TDR loans, remain in nonaccrual status until the borrower demonstrates a sustained period of performance which the Bank generally believes to be six consecutive months of payments. Otherwise, TDR loans are subject to the same nonaccrual and charge-off policies as noted above with respect to their restructured principal balance.

Portfolio segments identified by the Bank include residential real estate, multifamily, commercial real estate and commercial loans. Relevant risk characteristics for these portfolio segments generally include debt service coverage ratio, loan-to-value ratio and financial performance.

Mortgage Servicing Rights

When mortgage loans are sold with servicing retained, servicing rights are initially recorded at fair value with the income statement effect recorded in gains on sales of loans. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income.

The Bank services residential mortgage loans, which represents its single class of servicing rights, primarily for Government Sponsored Entities ("GSE") and other private investors. The Bank has elected to measure all mortgage servicing rights at fair value. Under the fair value measurement method, the Bank measures servicing rights at fair value at each reporting date and reports changes in fair value of servicing assets in earnings in the period in which the changes occur, and are included with loan servicing income (expense) in the statement of operations. The fair values of servicing rights are subject to significant fluctuations as a result of changes in estimated and actual prepayment speeds and default rates and losses. See Note 4 for more information on the valuation of servicing rights.

Servicing fee income, which is reported on the statement of operations as loan servicing income (expense), is recorded for fees earned for servicing loans, net of fair value adjustments. The fees are based on a contractual percentage of the outstanding principal; or a fixed amount per loan and are recorded as income when earned. Servicing fees totaled $342,352 and $390,370 for the years ended December 31, 2019 and 2018, respectively.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been relinquished. Control over transferred assets is deemed to be surrendered when the assets have been isolated from the Bank, 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 the Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Restricted Stock and Equity Securities

The Bank is a member of the Federal Home Loan Bank ("FHLB") system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. FHLB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on the ultimate recovery of par value. Both cash and stock dividends are reported as income. The Bank's investment in FHLB stock was $666,900 and $762,600 at December 31, 2019 and 2018, respectively.

Pursuant to the adoption of ASU 2016-01 in 2019, the Bank elected the measurement alternative for measuring equity securities without readily determinable fair values at cost less impairment, plus or minus observable price changes in orderly transactions. The carrying amount of equity securities without readily determinable fair values is $280,000 as of December 31, 2019 and includes investment in Pacific Coast Bankers' Bank ("PCBB") and other bankers bank stock. A gain of $80,000 was recorded to income upon adoption of the ASU and during the year ended December 31, 2019. Adjustments to the carrying value of PCBB stock at adoption and during the year 2019 were based on observable activity in the stock. All other bankers bank stock is recorded at cost.

Premises and Equipment

Premises and equipment are carried at cost. Depreciation is determined using the straight-line method over the estimated useful lives of the related assets, which is three to five years for equipment and five to ten years for furniture. Leasehold improvements are amortized over the life of the asset or the term of the related lease, including lease extension options expected to be exercised, whichever is shorter. When assets are sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recognized in earnings for the period. The cost of maintenance and repairs is charged to expense as incurred.

Leases

The Bank determines if an arrangement contains a lease at contract inception and recognize right-of-use ("ROU") assets and operating lease liabilities based on the present value of lease payments over the lease term. While operating leases may include options to extend the term, the Bank does not take into account the options in calculating the ROU asset and lease liability unless it is reasonably certain such options will be reasonably exercised. The present value of lease payments is determined based on the Bank's incremental borrowing rate and other information available at lease commencement. Leases with an initial term of 12 months or less are not recorded in the balance sheets. Lease expense is recognized on a straight-line basis over the lease term. The Bank has elected to account for lease agreements with lease and non-lease components as a single lease component. Refer to - Accounting Standards Adopted in 2019 below and Note 6, *Leases* for further discussion on the Bank's leasing arrangements and related accounting.

Foreclosed Assets

Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. If fair value declines subsequent to foreclosure, a valuation allowance is recorded through expense. Operating costs after acquisition are expensed.

Revenue Recognition - Noninterest Income

The Bank adopted the provisions of ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) in 2019. Results for reporting periods beginning after December 31, 2018 are presented under Topic 606, while prior period amounts have not been adjusted and continue to be reported in accordance with Topic 605. The Bank recognizes revenue as it is earned and noted no impact to its revenue recognition policies as a result of the adoption of ASU 2014-09. All of the Bank's revenue from contracts with customers within the scope of ASC 606 is recognized in non-interest income.

Income Taxes

Deferred income tax assets are computed using the balance sheet method, which recognizes a liability or asset representing the tax effects, based on current tax law, of future deductible or taxable amounts attributable to events that have been recognized in the financial statements. A valuation allowance is established to reduce the deferred tax asset to the level at which it is "more likely than not" that the tax asset or benefits will be realized. Realization of tax benefits of deductible temporary differences and operating loss carryforwards depends on having sufficient taxable income of an appropriate character within the carryforward periods. The Bank recognized uncertain tax positions in the financial statements only if, based on its merits, the position is more likely than not to be sustained on audit by the taxing authorities. Interest and penalties related to uncertain tax positions are recorded as part of income tax expense.

Repurchase and Recourse Liability

A repurchase and recourse liability included in accrued interest payable and other liabilities is established through a provision for loan repurchases charged to earnings for loans the Bank has sold with recourse. The Bank provides industry standard representations and warranties to purchasers of the loans sold. In the event of a breach of these representations and warranties, the Bank may be required to repurchase a mortgage loan or indemnify the purchaser, and any subsequent loss on the mortgage loan may be borne by the Bank. If there is no breach of a representation and warranty provision, the Bank has no obligation to repurchase the loan or indemnify the investor against loss. For loans that are sold with recourse, the Bank is subject to risk of loss resulting from borrowers who default on their contractual obligation to repay their mortgage if the Bank does not receive sufficient proceeds upon ultimate foreclosure and liquidation of the property to cover the amount of the mortgage plus expenses the Bank incurs, regardless of whether there was any violation of representation and warranties.

Repurchase demands and claims for indemnification payments are reviewed on a loan-by-loan basis to validate if there has been a breach requiring repurchase or a make-whole payment. The Bank actively contests claims to the extent it does not consider them valid. In cases where the Bank repurchases loans, it bears the subsequent credit loss on the loans with such credit losses, if any, recorded in other expense, net in the statements of operations. The Bank seeks to manage the risk of repurchase and associated credit exposure through underwriting and quality assurance practices and by servicing mortgage loans to meet investor standards.

Dividends

Upon declaration by the Board of Directors, all shareholders of record will be entitled to receive dividends. The Office of Comptroller of the Currency ("OCC") restricts the total dividend payment of any bank in any calendar year to the net income for that year to date plus retained income for the preceding two years. During 2009, the Bank was ordered by the OCC to suspend all dividend payments without receiving pre-approval of the OCC (see Note 15 for further discussion of regulatory matters). As such, no dividends were declared or paid in the years ended December 31, 2019 and 2018.

Comprehensive Loss

Comprehensive loss is comprised of net loss and other comprehensive loss. The Bank's sources of other comprehensive loss include the net unrealized losses on the Bank's available-for-sale debt securities. The amount reclassified out of other accumulated comprehensive income relating to realized gains in 2019 was $286,417.

Earnings (Loss) Per Share ("EPS")

Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity. The Bank has an operating loss and therefore only reports basic EPS. Weighted-average shares outstanding used in the computation of basic earnings per share were 49,179,923 and 28,040,961 in 2019 and 2018, respectively.

Fair Value Measurements

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Current accounting guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of inputs that may be used to measure fair value:

Level 1 - Quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 - Significant other observable inputs (other than Level 1 prices) such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 - Significant unobservable inputs that reflect an entity's own assumptions about the factors that market participants would use in pricing an asset or liability.

See Note 16 for more information and disclosures relating to the Bank's fair value measurements.

Recently Adopted Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09 *Revenue from Contracts with Customers*, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU replaces most existing revenue recognition guidance in GAAP. The new standard was effective for the Bank in 2019. Adoption of ASU 2014-09 did not have a material impact on the Bank's financial statements and related disclosures as the Bank's primary sources of revenues are derived from interest and dividends earned on loans, debt securities, and other financial instruments that are not within the scope of ASU 2014-09. The Bank's revenue recognition pattern for revenue streams within the scope of ASU 2014-09, including but not limited to service charges on deposit accounts, did not change significantly from current practice. The standard permits the use of either the full retrospective or modified retrospective transition method. The Bank elected to use the modified retrospective transition method which requires application of ASU 2014-09 to uncompleted contracts at the date of adoption however, periods prior to the date of adoption were not retrospectively revised as the impact of the ASU on uncompleted contracts at the date of adoption was not material.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments–Overall: Recognition and Measurement of Financial Assets and Financial Liabilities*. The new standard was effective for the Bank in 2019. Adoption of ASU 2016-01 did not have a material impact on the Bank's financial statements, but the Bank did record an $80,000 gain on equity securities without a readily determinable market value upon adoption of the ASU. Changes made to the current measurement model primarily affect the accounting for equity securities with readily determinable fair values, where changes in fair value impact earnings instead of other comprehensive income. Equity securities without readily marketable fair values are to be carried at amortized cost, less impairment (if any) plus or minus changes resulting from observable price changes in orderly transactions for an identical investment or similar investment of the same issuer. The accounting for other financial instruments, such as loans, investments in debt securities, and financial liabilities is largely unchanged.

The Bank adopted ASU 2016-02, *Leases (Topic 842)* and ASU 2018-11, *Leases (Topic 842): Targeted Improvements,* referred to herein as Topic 842, effective June 30, 2019 when it first became a public business entity. The new guidance establishes the principles to report transparent and economically neutral information about the assets and liabilities that arise from leases. Entities are required to recognize ROU assets and lease liabilities that arise from leases in the balance sheet and to disclose qualitative and quantitative information about lease transactions, such as information about variable lease payments and options to renew and terminate leases. Upon adoption, the Bank elected to use the modified retrospective transition approach and recorded an ROU asset and lease liability of approximately $1.0 million.

Recent Accounting Guidance Not Yet Effective

In June 2016, the FASB issued ASU No. 2016-13, *Measurement of Credit Losses on Financial Instruments (Topic 326).* This ASU significantly changes how entities will measure credit losses for most financial assets and certain other instruments that aren't measured at fair value through net income. This includes, but is not limited to, loans, leases, held-to-maturity securities, loan commitments, and financial guarantees. ASU No. 2016-13 is effective for interim and annual reporting periods beginning after December 15, 2022. The Bank is currently evaluating the provisions of ASU No. 2016-13 for potential impact on its financial statements and disclosures.

Note 2 - Debt Securities

The amortized cost and fair values of debt securities with gross unrealized gains and losses as of December 31, 2019, were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-Sale				
Mortgage-backed agency securities	$ 1,138,820	$ 13,012	$ (6,082)	$ 1,145,750
Subordinated debt securities	2,411,770	8,525	-	2,420,295
	$ 3,550,590	$ 21,537	$ (6,082)	$ 3,566,045

The amortized cost and fair values of debt securities with gross unrealized gains and losses as of December 31, 2018 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-Sale				
Mortgage-backed agency securities	$ 12,140,389	$ -	$ (305,882)	$ 11,834,507
Held-to-Maturity				
Mortgage-backed agency securities	$ 2,285,865	$ 28,476	$ (48,412)	$ 2,265,929

The scheduled maturities of subordinated debt securities is as follows as of December 31, 2019:

	Available-for-Sale Securities	
	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 1,111,770	$ 1,120,295
Due in one year to five years	1,300,000	1,300,000
	$ 2,411,770	$ 2,420,295

A maturity schedule of mortgage-backed securities is not presented as they are not due at a single maturity date.

Unrealized losses have been in a continuous loss position for less than 12 months as of December 31, 2019. Unrealized losses have not been recognized into income because the issuer bonds are of high credit quality, management does not intend to sell, it is not more likely than not that management would be required to sell the securities prior to their anticipated recovery and the decline in fair value is largely due to changes in interest rates. The fair value is expected to recover as the bonds approach maturity.

During the year ended December 31, 2019 the Bank sold securities available for sale recognizing gross gains of $286,417 and gross losses of $0 on proceeds of $15,030,292. No securities were sold in 2018.

Securities with a carrying value of approximately $964,000 were pledged at December 31, 2019 to secure the borrowing arrangements discussed in Note 8.

In 2019, the Bank transferred held-to-maturity securities with a fair value of $6,098,357 to available for sale.

Note 3 - Loans and Allowance for Loan Losses

Loans consist of the following at December 31:

	2019	2018
Loans Held for Investment		
Residential real estate	$ 60,226,829	$ 44,257,871
Multi-Family real estate	10,333,341	13,320,145
Commercial real estate	7,016,996	11,924,147
Commercial	6,958,428	-
Total loans held for investment	84,535,594	69,502,163
Deferred loan costs and premiums, net	210,951	255,197
Allowance for loan losses	(1,581,025)	(1,581,025)
	$ 83,165,520	$ 68,176,335

The following table presents the recorded investment in loans and impairment method as of December 31, 2019, and the activity in the allowance for loan losses for the year then ended, by portfolio segment:

	Residential Real Estate	Multi-Family Real Estate	Commercial Real Estate	Commercial	Total
Allowance for credit losses					
Beginning balance	$ 1,355,442	$ 97,289	$ 128,294	$ -	$ 1,581,025
Charge-offs	-	-	-	-	-
Recoveries	-	-	-	-	-
Provision	(59,032)	31,247	(23,629)	51,414	-
Ending balance	$ 1,296,410	$ 128,536	$ 104,665	$ 51,414	$ 1,581,025
Reserves					
Specific	$ 325,000	$ -	$ -	$ -	$ 325,000
General	971,410	128,536	104,665	51,414	1,256,025
	$ 1,296,410	$ 128,536	$ 104,665	$ 51,414	$ 1,581,025
Loan evaluated for impairment					
Individually	$ 4,129,970	$ -	$ -	$ -	$ 4,129,970
Collectively	56,096,859	10,333,341	7,016,996	6,958,428	80,405,624
	$ 60,226,829	$ 10,333,341	$ 7,016,996	$ 6,958,428	$ 84,535,594

The following table presents the recorded investment in loans and impairment method as of December 31, 2018, and the activity in the allowance for loan losses for the year then ended, by portfolio segment:

	Residential Real Estate	Multi-Family Real Estate	Commercial Real Estate	Commercial	Total
Allowance for credit losses					
Beginning balance	$ 1,537,022	$ 42,102	$ 90,859	$ -	$ 1,669,983
Charge-offs	(88,958)	-	-	-	(88,958)
Recoveries	-	-	-	-	-
Provision	(92,622)	55,187	37,435	-	-
Ending balance	$ 1,355,442	$ 97,289	$ 128,294	$ -	$ 1,581,025
Reserves					
Specific	$ 678,308	$ -	$ -	$ -	$ 678,308
General	677,134	97,289	128,294	-	902,717
	$ 1,355,442	$ 97,289	$ 128,294	$ -	$ 1,581,025
Loan evaluated for impairment					
Individually	$ 6,140,875	$ -	$ -	$ -	$ 6,140,875
Collectively	38,116,996	13,320,145	11,924,147	-	63,361,288
	$ 44,257,871	$ 13,320,145	$ 11,924,147	$ -	$ 69,502,163

The Bank categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, collateral adequacy, credit documentation, and current economic trends, among other factors. The Bank analyzes loans individually by classifying the loans as to credit risk. This analysis typically includes larger, non-homogeneous loans such as commercial real estate and commercial and industrial loans. This analysis is performed on an ongoing basis as new information is obtained. The Bank uses the following definitions for risk ratings:

Pass - Loans listed as pass include larger non-homogeneous loans not meeting the risk rating definitions above and smaller, homogeneous loans not assessed on an individual basis.

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

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

Impaired - A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Additionally, all loans classified as troubled debt restructurings are considered impaired.

Based on the most recent analysis performed, the risk category of loans by class of loans is as follows as of December 31, 2019:

	Pass	Special Mention	Substandard	Impaired	Total
Residential real estate	$ 56,096,859	$ -	$ -	$ 4,129,970	$ 60,226,829
Multi-Family real estate	10,333,341	-	-	-	10,333,341
Commercial real estate	6,958,428	-	-	-	6,958,428
Commercial	7,016,996	-	-	-	7,016,996
	$ 80,405,624	$ -	$ -	$ 4,129,970	$ 84,535,594

Based on the most recent analysis performed, the risk category of loans by class of loans is as follows as of December 31, 2018:

	Pass	Special Mention	Substandard	Impaired	Total
Residential real estate	$ 38,116,996	$ -	$ -	$ 6,140,875	$ 44,257,871
Multi-Family real estate	13,320,145	-	-	-	13,320,145
Commercial real estate	11,924,147	-	-	-	11,924,147
	$ 63,361,288	$ -	$ -	$ 6,140,875	$ 69,502,163

Past due and nonaccrual loans were as follows as of December 31, 2019:

	Still Accruing		
	30-89 Days Past Due	Over 90 Days Past Due	Nonaccrual
Residential real estate	$ 1,113,806	$ -	$ 293,778

Past due and nonaccrual loans were as follows as of December 31, 2018:

	Still Accruing		
	30-89 Days Past Due	Over 90 Days Past Due	Nonaccrual
Residential real estate	$ -	$ -	$ 1,645,000

Individually impaired loans were as follows as of December 31, 2019:

	Unpaid Principal Balance	With Allowance		Without Allowance	
		Recorded Investment	Related Allowance	Recorded Investment	Related Allowance
Residential real estate	$ 4,725,057	$ 2,486,616	$ 325,000	$ 1,643,354	$ -

Individually impaired loans were as follows as of December 31, 2018:

	Unpaid Principal Balance	With Allowance		Without Allowance	
		Recorded Investment	Related Allowance	Recorded Investment	Related Allowance
Residential real estate	$ 6,813,362	$ 2,762,242	$ 678,308	$ 3,378,633	$ -

The average recorded investment in impaired loan balances during years ended December 31, 2019 and 2018, was approximately $5.1 million and $7.0 million, respectively. Interest income recognized on residential real estate impaired loans amounted to approximately $256,000 and $350,000 for 2019 and 2018, respectively.

The Bank had 16 loans identified as troubled debt restructurings ("TDR's") at December 31, 2019, and has allocated $325,000 of specific reserves thereon. The Bank has committed to lend no additional amounts as of December 31, 2019, to customers with outstanding loans that are classified as TDR's.

During the year ended December 31, 2019 and 2018, the Bank did not modify any loans in a TDR. There were no TDR's for which there was a payment default within twelve months following a modification during 2019 and 2018. A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms.

Note 4 - Mortgage Servicing Rights

Activity in the Bank's loan servicing portfolio associated with its capitalized mortgage servicing assets consisted of the following for the years ended December 31, 2019 and 2018:

	2019	2018
Beginning balance	$ 139,853,021	$ 162,424,384
Principal paydowns, prepayments, and settlements	(19,362,482)	(22,571,363)
Ending balance	$ 120,490,539	$ 139,853,021

The number of loans and principal balance of the total loans serviced were as follows as of December 31:

	2019		2018	
	Count	Balance	Count	Balance
Federal Home Loan Bank	34	$ 3,356,166	40	$ 4,022,438
Fannie Mae	776	117,134,373	875	135,830,583
	810	$ 120,490,539	915	$ 139,853,021

Changes in mortgage servicing rights for the years ended December 31, 2019 and 2018, are as follows:

	2019	2018
Beginning balance, at fair value	$ 1,043,287	$ 1,064,694
Changes in market value	(310,225)	(21,407)
Ending balance, at fair value	$ 733,062	$ 1,043,287

The significant assumptions used in estimating the fair value of servicing rights were as follows as of December 31:

	2019	2018
Weighted average prepayment rate	14.10%	11.10%
Weighted average contractual life (in months)	59	72
Weighted average discount rate	12.01%	12.00%

Note 5 - Premises and Equipment

Premises and equipment consist of leasehold improvements, software, furniture, and equipment and are stated at cost, less accumulated depreciation and amortization, which are calculated on a straight-line basis over the estimated useful life of the property or the term of the lease (if less). Premises and equipment are as follows at December 31:

	2019	2018
Furniture and equipment	$ 295,507	$ 233,082
Leasehold improvements	805,886	772,936
Software	240,754	50,412
	1,342,147	1,056,430
Less accumulated depreciation and amortization	(957,740)	(894,331)
	$ 384,407	$ 162,099

Total depreciation and amortization expense relating to premises and equipment for the years ended December 31, 2019 and 2018, was $63,410 and $42,194, respectively.

Note 6 - Leases

ASU 2016-02, *Leases (Topic 842),* and related amendments were adopted on June 30, 2019, using the modified retrospective transition method whereby comparative periods were not restated. No cumulative effect adjustment to the opening balance of retained earnings was required. The Bank elected the package of practical expedients permitted under the new standard, which allowed carry forward historical lease classifications, account for lease and nonlease components as a single lease component, and not to recognize a ROU asset and lease liability for short-term leases. The amount of the lease liability and ROU asset is impacted by the lease term and the discount rate applied to determine the present value of future lease payments.

The Bank leases its one location in Oakland California with the term extending to January 31, 2025. There is a 5-year renewal option available which is not included in the measurement of ROU assets and lease liabilities as it is not considered reasonably certain of exercise.

Balance sheet and supplemental information at December 31, 2019, are shown below.

Operating Lease Right-of-Use Asset	$ 952,251
Operating Lease Liability	$ 952,251
Weighted Average Remaining Lease Term, in Years	5.09
Weighted Average Discount Rate	5.50%

The Bank elected, for all classes of underlying assets, not to separate lease and non-lease components and instead to account for them as a single lease component. Variable lease cost primarily represents variable payments such as common area maintenance and utilities. The following table represents lease costs and other lease information for the year ended December 31, 2019:

Operating lease cost	$ 211,058
Variable lease cost	3,317
Total lease costs	$ 214,375

Cash Paid for Amounts Included in the Measurement of Lease Liabilities	$ 214,702
Right-of-Use Assets Obtained in Exchange for Lease Obligations	$ 1,037,087

For the year ended December 31, 2018, rent expense was $209,664.

Maturities of lease liabilities for the periods indicated:

Year Ending	
2020	$ 215,160
2021	215,160
2022	215,160
2023	215,160
2024	215,160
Thereafter	17,930
Total lease payments	1,093,730
Less imputed interest	(141,479)
Present value of net future minimum lease payments	$ 952,251

Note 7 - Deposits

Interest-bearing deposits consist of the following at December 31:

	2019	2018
NOW accounts	$ 6,797,979	$ 7,349,159
Savings	17,866,019	20,686,987
Money market accounts	17,588,727	10,227,015
Certificates of deposit, under $250,000	45,797,510	46,540,822
Certificates of deposit, $250,000 or more	4,204,211	4,126,638
	$ 92,254,446	$ 88,930,621

The scheduled maturities of time certificate of deposit accounts as of December 31, 2019, were as follows:

Year Ending December 31	
2020	$ 48,008,885
2021	1,315,464
After 2021	677,372
	$ 50,001,721

Note 8 - Borrowings

Total borrowing capacity with the FHLB at December 31, 2019 was approximately $31.1 million based on loan and securities collateral pledged with a market value of approximately $40.5 million. One long-term advance in the amount of $15.0 million was outstanding at December 31, 2019, with an interest rate of 1.96%, maturing on June 17, 2021. Remaining borrowing capacity at December 31, 2019 was approximately $16.1 million.

The Bank also has a secured federal funds line of credit with a correspondent bank as of December 31, 2019, in the amount of $300,000 collateralized by a money market deposit account in the same amount. No amounts were outstanding on the above borrowing arrangements as of December 31, 2019.

Note 9 - Other Expense

Other expense for the years ended December 31, 2019 and 2018, consists of the following:

	2019	2018
Provision for repurchase liability	$ 150,000	$ -
Director fees	75,800	61,800
Regulatory assessments	217,497	280,773
Agency loan fees	181,444	215,520
Insurance	126,593	154,720
Other real estate expenses	10,322	42,458
Other operating expenses	404,240	347,185
	$ 1,165,896	$ 1,102,456

Note 10 - Income Taxes

Income tax expense for the years ended December 31, 2019 and 2018, consists of the following:

	2019	2018
Current Expense		
Federal	$ -	$ -
State	-	-
	-	-
Change in valuation allowance	(130,000)	(260,000)
Deferred expense	130,000	260,000
Income tax expense	$ -	$ -

The following is a summary of the components of the net deferred tax asset accounts recognized in the accompanying balance sheets at December 31:

	2019	2018
Deferred Tax Assets		
Depreciation differences	$ 92,000	$ 96,000
Net operating loss carryforwards	11,734,000	11,666,000
Repurchase liability	131,000	86,000
Other items	72,000	95,000
	12,029,000	11,943,000
Valuation Allowance	(11,310,000)	(11,440,000)
Deferred Tax Liabilities		
Allowance for loan losses	(436,000)	(436,000)
Federal Home Loan Bank dividends	(47,000)	(54,000)
Mortgage servicing rights	(217,000)	(13,000)
Other items	(19,000)	-
	(719,000)	(503,000)
Net deferred tax assets (liabilities)	$ -	$ -

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Due to the uncertainty of future realizability, management has offset all net deferred tax assets with a valuation allowance.

The Bank has a net operating loss ("NOL") carry forwards of approximately $31.2 million and $56.7 million and at December 31, 2019 for federal and California tax purposes, respectively. The NOLs begin to expire in 2031 for federal tax purposes and 2029 for California tax purposes.

Note 11 - Commitments and Contingencies and Subsequent Event

Commitments to Extend Credit

The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the accompanying balance sheet.

The Bank's exposure to credit losses in the event of nonperformance by the other parties for commitments to extend credit is represented by the contractual amount of these instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

As of December 31, 2019 and 2018, the Bank had no commitments to extend credit.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any conditions established in the contract. Commitments generally have fixed expiration dates of not more than 12 months and may require payment of a fee. Since many of the commitments are not expected to be drawn upon, the total commitment amounts may not represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include marketable investment securities, accounts receivable, inventory, property, plant and equipment, and real properties.

The Bank grants real estate mortgage, commercial, and consumer loans to customers principally in California. In management's judgment, a concentration exists in residential real estate loans which represented approximately 71% of total loans at December 31, 2019.

Although management believes the loans within these concentrations have no more than the normal risk of collectability, a substantial decline in the performance of the economy in general or a decline in real estate values in the Bank's primary service areas in particular could have an adverse impact on the collectability of these loans.

Litigation

In the normal course of business, the Bank is involved in various other legal proceedings. In the opinion of management, any liability resulting from such proceedings would not have a material adverse effect on the financial statements, except as discussed in Note 13. On January 2, 2020, settlement proceeds of $664,832 was received from a former CEO of the Bank in full satisfaction of a Superior Court judgment rendered on July 26, 2019. This amount will be recognized as income in the year 2020.

Note 12 - Related-Party Transactions

During the normal course of business, the Bank may enter into loans with related parties, including executive officers and directors. For years ended December 31, 2019 and 2018, there were no related party borrowings. Related party deposits amounted to approximately $10.2 million and $1.5 million as of December 31, 2019 and December 31, 2018, respectively.

Note 13 - Repurchase and Recourse Liability

The following table summarizes the activity in the repurchase and recourse liability for the Bank's residential real estate loans for the years ended December 31, 2019 and 2018:

	2019	2018
Beginning of period	$ 291,810	$ 291,810
Provisions for losses	150,000	-
Losses incurred	-	-
End of period	$ 441,810	$ 291,810

Amounts accrued are based on the Bank's historical loss experience for similar loans sold to investors, management's assessment of credit risk inherent in transactions processed, industry experience, and other relevant factors. Amounts are located in other liabilities on the balance sheets.

A significant component of the accrual at December 31, 2019 relates to a first amended complaint filed against the Bank by the Trustee in the bankruptcy of Lehman Brothers Holdings, Inc., for contractual indemnification. The amended complaint relates to approximately 90 loans sold by the Bank to Lehman Brothers Bank. These loans were resold by Lehman Brothers Bank to Fannie Mae, Freddie Mac, or RMBS, for mortgage backed securities. The Trustee settled repurchase claims made by these entities; and the Trustee asserts that the Bank is obligated to indemnify the Trustee for a portion of the settlements. The Trustee alleges that it has sustained approximately $14 million of damages resulting from loans purchased from the Bank.

The original complaint was filed in 2016, and the first amended complaint was filed in 2018. The case has progressed slowly, and the parties are engaged in a court-ordered alternative dispute resolution process. In 2019, counsel for the Bank completed a loan-level analysis of the claim; the results were shared with counsel for Lehman as part of the ongoing settlement negotiations. Management anticipates participating in a mediation in the second half of 2020.

Management has been informed by legal counsel that the Trustee’s claim may be subject to offsets and defenses. However, due to the complexity of the case and the risks involved, it is likely that the case will be resolved through compromise and settlement. Therefore, management believes that it is probable that the Bank will sustain losses.

In setting the reserve at $442,000 as of December 31, 2019, the Board considered various factors including the progress of the case, a loan-level analysis of the loans at issue, the Bank’s historical experience with repurchase claims, the experience of other financial institutions in resolving similar claims, and the views of legal counsel.

Note 14 - Employee Benefit Plans

In October 1995, the Bank adopted the Gateway 401(k) Employee Savings Plan. The plan is available to all employees of the Bank who are at least 21 years of age and have completed three months of service. Under provisions of the plan, participants may contribute up to 100% of their pretax income each year up to a dollar limit which is established by law. The Bank's contribution to the plan is discretionary and is allocated among participants based on their annual compensation and the total compensation of all eligible participants. The Bank's contributions vest at a rate of 25% for each year of service beginning after the first completed year of service. The Bank did not make a contribution to the plan during the years ended December 31, 2019 and 2018.

Note 15 - Regulatory Matters

Consent Order: On October 26, 2011 the Bank consented to the issuance of a Consent Order ("the Order") by the Office of the Comptroller of the Currency ("OCC"). The Order places significant requirements on the Bank, as summarized below.

1. Capital: The Bank shall have and maintain a tier 1 capital ratio to total assets of at least nine percent (9%) and a total risk-based capital ratio to risk-weighted assets of at least thirteen percent (13%).

2. Strategic Plan and Capital Plan: The Board shall review and approve a written comprehensive long-term business plan. The business plan shall be based on a comprehensive review of the Bank's operations, including risks and returns of each of its business lines, current and projected capital levels, available resources and market conditions.

3. Compliance Management: The Bank must create a Board Compliance Committee to ensure effective monitoring of the Bank's compliance with the consent order. The committee must consist of a minimum of three independent directors.

4. Allowance for Loan Losses: The Bank must develop and maintain an effective allowance for loan losses program to ensure the risk associated in the loan portfolio are effectively captured and recognized in a timely manner.

5. Concentration Management: The Bank is required to develop and maintain an effective concentration management program that the Board will monitor to ensure the Bank manages its assets and liability concentrations in a safe and sound manner.

6. Books and Records: The Bank is required to develop and maintain accurate books and records, and submit a plan to improve the quality of its regulatory reporting and ensure all aspects of the books and records are maintained in an effective manner.

7. Operating Restrictions: The Bank must comply with various operating restrictions including: restrictions on growth, managerial changes, employment/ severance agreements (as well as other contracts) and capital distributions.

While the Bank is not in full compliance with the Order, management believes substantial progress has been made toward full compliance.

There is no assurance the Bank will be successful in executing the terms of this Order. If the Bank is not successful in its compliance with the requirements of the Order it may receive a prompt corrective action and may be required to sell, liquidate or merge the Bank or in the event of a material decline in the capital levels, could be subject to FDIC receivership.

Capital Requirements: The Bank is subject to various regulatory capital requirements administered by the Federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary actions by regulators that, if undertaken, could have a direct 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 classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

In July 2013, the federal bank regulatory agencies approved the final rules implementing the Basel Committee on Banking Supervision's capital guidelines for U.S. banks. The new "Basel III" rules became effective on January 1, 2015, with certain of the requirements phased-in over a multi-year schedule, and fully phased in by January 1, 2019. The rules include a new common equity Tier 1 ("CET1") capital to risk-weighted assets ratio with minimums for capital adequacy and prompt corrective action purposes of 4.5% and 6.5%, respectively. The minimum Tier 1 capital to risk-weighted assets ratio was raised from 4.0% to 6.0% under the capital adequacy framework and from 6.0% to 8.0% to be well-capitalized under the prompt corrective action framework. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital.

In addition, the Basel III rules introduced the concept of a "conservation buffer" of 2.5% applicable to the three capital adequacy risk-weighted asset ratios (CET1, Tier 1, and Total). If the actual risk-weighted capital ratios fall below the capital adequacy minimum ratios plus the phased-in conservation buffer amount then dividends, share buybacks and discretionary bonuses to executives could be limited in amount. At December 31, 2019, the Bank was not limited by the conservation buffer.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total, Tier 1 and CET1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined).

As of December 31, 2019, the OCC has categorized the Bank as "adequately-capitalized" under the regulatory framework for Prompt Corrective Action ("PCA") due to the existence of the regulatory Order discussed above with minimum capital levels included. Additionally, the OCC has recently deemed the Bank to be engaged in statutorily "unsafe and unsound practices" within the meaning of 12 USC 1818(b) which provides the basis for the issuance of a Cease and Desist Order or other enforcement action. This statutory designation also provides the OCC with the ability to impose more stringent PCA requirements on the Bank by requiring that it comply with one or more provisions of the PCA category that is one step below the Bank's current category of "adequately-capitalized", which would be the "undercapitalized" category. If "undercapitalized", capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. To date, the OCC has yet to take any action relative to these now available additional enforcement actions.

The following table sets forth the Bank's actual capital amounts and ratios as of December 31, 2019, and also the amounts and ratios generally required under capital adequacy rules and the prompt corrective rules to be considered well-capitalized (dollar amounts in thousands):

	Actual Capital		To Be Adequately Capitalized		Corrective Action Framework	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital (to risk-weighted assets)	$ 16,603	27.2%	$ 4,888	8.0%	$ 6,110	10.0%
Tier 1 capital (to risk-weighted assets)	$ 15,830	25.9%	$ 3,666	6.0%	$ 4,888	8.0%
CET1 capital (to risk-weighted assets)	$ 12,143	19.9%	$ 2,749	4.5%	$ 3,971	6.5%
Tier 1 capital (to average assets)	$ 15,830	12.9%	$ 4,923	4.0%	$ 6,154	5.0%

The following table sets forth the Bank's actual capital amounts and ratios as of December 31, 2018, and also the amounts and ratios generally required under capital adequacy rules and the prompt corrective rules to be considered well-capitalized (dollar amounts in thousands):

	Actual Capital		To Be Adequately Capitalized		Corrective Action Framework	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital (to risk-weighted assets)	$ 16,857	32.9%	$ 4,100	8.0%	$ 5,125	10.0%
Tier 1 capital (to risk-weighted assets)	$ 16,205	31.6%	$ 3,075	6.0%	$ 4,100	8.0%
CET1 capital (to risk-weighted assets)	$ 12,518	24.4%	$ 2,306	4.5%	$ 3,331	6.5%
Tier 1 capital (to average assets)	$ 16,205	14.5%	$ 4,466	4.0%	$ 5,583	5.0%

Note 16 - Fair Value Measurements

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

Securities: The fair values of securities available for sale are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1) or matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2).

Mortgage Servicing Rights: The Bank engages an independent third party to perform a valuation of its mortgage servicing rights periodically. Mortgage servicing rights are valued using discounted cash flow modeling techniques that require estimates regarding future cash flows, actual and expected prepayment speeds, discount rates, servicing costs, and other economic factors. Certain adjustments are made to the model inputs to reflect the specific characteristics of the Bank's portfolio (Level 3).

Collateral-Dependent Impaired Loans: The Bank does not record loans at fair value on a recurring basis. However, from time to time, fair value adjustments are recorded on these loans to reflect partial write-downs, through charge-offs or specific reserve allowances, that are based on fair value estimates of the underlying collateral. The fair value estimates for collateral-dependent impaired loans are generally based on recent real estate appraisals or broker opinions, obtained from independent third parties, which are frequently adjusted by management to reflect current conditions and estimated selling costs (Level 3).

Other Real Estate Owned: Nonrecurring adjustments to certain real estate properties classified as other real estate owned are measured at the lower of carrying amount or fair value, less costs to sell. In cases where the carrying amount exceeds the fair value, less costs to sell, an impairment loss is recognized. Fair values are generally based on third party appraisals of the property which are commonly adjusted by management to reflect current conditions and selling costs (Level 3).

Appraisals for other real estate owned are performed by certified general appraisers whose qualifications and licenses have been reviewed and verified by the Bank. Once received, a member of the loan department reviews the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison to independent data sources such as recent market data or industry wide-statistics. The Bank also compares the actual selling price of collateral that has been sold to the most recent appraised value to determine what additional adjustments, if any, should be made to the appraisal values on any remaining other real estate owned to arrive at fair value. No significant adjustments to appraised values have been made as a result of this comparison process as of December 31, 2019.

The following table summarizes the Bank's financial instruments and nonfinancial items that were measured at fair value on a recurring and nonrecurring basis as of December 31, 2019:

	Fair Value	Level 1	Level 2	Level 3
Assets (Liabilities) Measured at Fair Value on A Recurring Basis				
Mortgage-backed securities	$ 1,145,750	$ -	$ 1,145,750	$ -
Subordinated debt securites	2,420,295	-	2,420,295	-
Mortgage servicing rights	733,062	-	-	733,062
	$ 4,299,107	$ -	$ 3,566,045	$ 733,062

The following table summarizes the Bank's financial instruments and nonfinancial items that were measured at fair value on a recurring and nonrecurring basis as of December 31, 2018:

	Fair Value	Level 1	Level 2	Level 3
Assets (Liabilities) Measured at Fair Value on A Recurring Basis				
Mortgage-backed securities	$ 11,834,507	$ -	$ 11,834,507	$ -
Mortgage servicing rights	1,043,287	-	-	1,043,287
Assets (Liabilities) Measured at Fair Value on A Nonrecurring Basis				
Collateral dependent loans	217,800	-	-	217,800
	$ 13,095,594	$ -	$ 11,834,507	$ 1,261,087

Below is the roll-forward of Level 3 financial instruments measured at fair value on a recurring basis for the years ended December 31, 2019 and 2018:

	2019 Mortgage Servicing Rights	2018 Mortgage Servicing Rights
Beginning balance	$ 1,043,287	$ 1,064,694
Total unrealized gains or (losses)	(310,225)	(21,407)
Ending balance	$ 733,062	$ 1,043,287

Fair value estimates are determined as a specific point in time utilizing quoted market prices, where available, or various assumptions and estimates. As the assumptions and estimates change, the fair value of the financial instruments will change.

The use of assumptions and various techniques, as well as the absence of secondary markets for certain financial instruments, will likely reduce the comparability of value disclosures between companies. The following table identifies the unobservable inputs, the values used, and the basis for their determination as of December 31, 2019:

Asset Type	Fair Value	Valuation Technique	Unobservable	Rate
Mortgage servicing rights	$ 733,062	Discounted cash flow	Constant prepayment rate	14.10%
			Discount rate	12.01%
			Cost to service	$96/loan/year

The use of assumptions and various techniques, as well as the absence of secondary markets for certain financial instruments, will likely reduce the comparability of value disclosures between companies. The following table identifies the unobservable inputs, the values used, and the basis for their determination as of December 31, 2018:

Asset Type	Fair Value	Valuation Technique	Unobservable	Rate
Mortgage servicing rights	$ 1,043,287	Discounted cash flow	Constant prepayment rate	11.10%
			Discount rate	12.00%
			Cost to service	$95/loan/year
Collateral dependent loans	$ 217,800	Third party appraisals	Comparable sales	Third-party provided
			Anticipated costs to sell	10.00%

Note 17 - Preferred Stock - Series C

In December 2015, the Bank issued 10 million shares of Series C Perpetual Non-Cumulative, no par value, Preferred Stock for $0.30 per share. The shares carry a liquidation value of $0.30 per share.

The shares are not callable by the holders but are convertible to common stock on a one for one basis at the discretion of the Bank should the Board of Directors determine that the ability to raise capital in a future capital raise event would be impaired by the existence of the Series C Preferred Stock, or in the case of a business combination. Dividends are to be paid annually at annual rate of 6.67%, if and when declared by the Bank's Board of Directors. To the extent no dividend is declared, dividends are noncumulative. As of December 31, 2019 and 2018, no dividends had been declared and the Bank is currently subject to dividend restrictions by the regulatory order discussed in Note 15. The stock is nonvoting.

Note 18 - Capital Raise

On May 2, 2018, the Bank closed on a private offering in which 35 million shares of common stock were issued at a price of $0.30 per share, resulting in new contributed capital of $10.5 million. This amount is reflected as common equity of the Bank, net of issuance costs of $657,392.

Note 19 - Fair Value of Financial Instruments

The fair value of a financial instrument is the amount at which the asset or obligation could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Fair value estimates are made at a specific point in time based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the entire holdings of a particular financial instrument. Because no market value exists for a significant portion of the financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature, involve uncertainties and matters of judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on financial instruments both on and off the balance sheet without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Additionally, tax consequences related to the realization of the unrealized gains and losses can have a potential effect on fair value estimates and have not been considered in many of the estimates.

The fair value hierarchy level and estimated fair value of significant financial instruments at December 31, 2019 and 2018 are summarized as follows (dollars in thousands):

		2019		2018	
	Fair Value Hierarchy	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets					
Cash and cash equivalents	Level 1	$ 35,103	$ 35,103	$ 21,673	$ 21,673
Debt securities available for sale	Level 2	3,566	3,566	11,835	11,835
Debt securities held to maturity	Level 2	-	-	2,286	2,266
Loans, net	Level 3	83,166	83,166	68,176	68,176
Restricted stock	Level 2	667	667	763	763
Liabilities					
Noninterest-bearing deposits	Level 1	3,315	3,315	3,513	3,513
Interest-bearing deposits	Level 2	92,254	92,254	88,931	88,931
FHLB advances	Level 2	15,000	15,000	-	-

Note 20 - Subsequent Events (COVID-19)

The Bank has evaluated subsequent events for recognition and disclosure through June 10, 2020, which is the date the financial statements were available to be issued. Since the start of 2020, a strain of coronavirus ("COVID-19") has spread globally, including the United States. The COVID-19 pandemic has caused disruption of regional and global economic activity, emergency actions by the Federal Reserve and other U.S. governmental authorities, significant declines in interest rates and equity market valuations, heightened volatility in the financial markets, the shutdown of countries' borders and directives for residents within the Bank's primary market area to stay at home or in their place of residence and for certain business to suspend some or all of their business activities. These actions have affected the Bank's operations and are expected to impact our financial results in 2020.

The Bank is taking actions to support its customers in a manner consistent with current guidance provided by Federal banking regulatory authorities. As of May 11, 2020, the Bank has approved payment relief for 18 loan customers with an outstanding balance of approximately $18.3 million. Payment relief was provided through deferral of payments (16 loans) and through conversion to interest-only payments (2 loans).

The Bank has also participated in the Paycheck Protection Program (PPP) through the Small Business Administration and funded approximately $16.4 million in PPP loans as of May 11, 2020. Loan fees of approximately $615,000 have been earned on funded PPP loans. Loan fees will be recognized over the contractual life of the underlying loans, adjusted for prepayments.

In addition to the general impact of COVID-19, certain provisions of the CARES Act as well as other recent legislative and regulatory relief efforts are expected to have a material impact on the Bank's operations. While it is not possible to know the full universe or extent of these impacts, the Bank is disclosing potentially material items of which we are currently aware.