Community
BANK OF THE BAY

2013
Annual Report

Dear Community Bank of the Bay Shareholder,

The annual shareholder letter typically focuses on the preceding year's results, but in this case we are having difficulty thinking of 2013 in isolation. To us 2013 marked the end of what we saw as the first phase of our development that began with the 2009–2010 recapitalization of the Bank. During this period, our main focus was internal as we honed our vision and worked to build a solid foundation suitable for the next phase of our growth. While our initial progress was hindered by the length and depth of what is now being called "the Great Recession," we believe that with a strong 2013 in hand, we are ready to consider this phase complete and focus our energies on the next chapter in our development.

Before we discuss our future initiatives, we ought to reflect on what we accomplished together in phase one. Obviously it all started with your support, as you entrusted us with approximately $7.5 million in new equity capital during a very difficult economic period. Your faith in us during that difficult time continues to inspire us, and focus us on task. Soon thereafter, we added an additional $2.3 million of low cost preferred stock from the U.S. Department of Treasury's Community Development Fund.

With adequate capital in place we set out to build a bank that could make a positive impact on our communities by bringing true relationship banking to the small to mid-sized businesses and non-profit organizations in the Bay Area. We enhanced our leadership by adding a number of very successful and deeply committed business and community leaders to our board, and experienced bankers to our team. We opened new offices in Danville and San Jose to expand our market reach, and sold our Oakland headquarters building and moved into more efficient offices to better deploy assets. Since September 30, 2009, we have rather quietly grown Total Assets by $104 million (12.8% in 2013 and 147% overall), Deposits by $90 million (15% in 2013 and 150% overall) and Loans by $79 million (16.2% in 2013 and 164% overall). In addition, we became a Preferred Lender with the U.S. Small Business Administration and made and sold over $17 million of SBA guaranteed loans.

As a result of these and many other efforts, we saw a steadily improving financial performance, and in 2013 we reported increased pre-tax profits in every quarter and full year after tax net income of $2,032,132, a 46.3% increase from 2012 - the best in our eighteen-year history. In recognition of our results, we were awarded Super Premier Performer status from industry watcher The Findley Reports for the second year in a row - and the only two times the Bank has received this award in its history.

Equally important to us as California's first certified Community Development Financial Institution ("CDFI") is that we remain true to our mission of promoting economic resilience and sustainability in all the communities we serve. In recognition of our efforts, 2013 marked the fourth year in a row where the Bank earned the maximum Bank Enterprise Award available from the U.S. Treasury's CDFI Fund. This award is granted annually to financial institutions that are positively impacting community development by supplying credit to worthy small to medium businesses, and non-profit organizations.

So what next for Community Bank of the Bay? What will change and what will our Bank look like in the coming years? While nothing will change with our VALUE statement - we will remain mission driven and dedicated to the goal of building an exceptional bank. Simply put, the biggest change is that we plan to become a much more VISABLE member of the COMMUNITY. It is time to put the period of "quiet growth" behind us. We're proud of our story and we're going to tell it.

We are committing more resources to improving our on-line and mobile presence and increasing investments in marketing and advertising. We intend to be more prominently involved with key economic and community partnerships, and lead in areas that we are especially dedicated, such as economic and environmental sustainability. Even now we are in the process of enhancing and re-launching the Bay Area Green Fund, to our knowledge the first FDIC insured money market account that allows depositors to target capital flows to environmentally sustainable businesses and projects. Look for this and other important initiatives to be introduced throughout the coming quarters.

We believe that these efforts to enhance our market presence will be important to our continued growth and profitability as we pursue our goal to build Community Bank of the Bay into one of the Bay Area's leading community banks. We hope that you are pleased with our progress to date, and equally excited about our future. We thank you for believing in us and being our partner, not just as a shareholder but as a client and referral source as well.

Please join us for our shareholder meeting on Wednesday, May 28 at 5:00 p.m., at Community Bank of the Bay headquarters, 180 Grand Avenue Oakland, so we can meet directly.

Sincerely,

Chairman of the Board

President & CEO

Report of Independent Auditors and
Financial Statements

Community Bank of the Bay

December 31, 2013 and 2012

MOSS ADAMS LLP

Certified Public Accountants | Business Consultants

Acumen. Agility. Answers.

CONTENTS

MOSS-ADAMS LLP
Certified Public Accountants | Business Consultants

REPORT OF INDEPENDENT AUDITORS

The Board of Directors and Shareholders
Community Bank of the Bay

Report on Financial Statements
We have audited the accompanying financial statements of Community Bank of the Bay (the Bank), which comprise the balance sheets as of December 31, 2013 and 2012, and the related statements of operations, comprehensive income, shareholders' equity, and cash flows for the years 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Bank'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 Bank'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 obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Community Bank of the Bay as of December 31, 2013 and 2012, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Moss Adams LLP

Stockton, California
April 11, 2014

COMMUNITY BANK OF THE BAY

ASSETS

	DECEMBER 31, 2013	DECEMBER 31, 2012
Cash and due from banks	$ 22,600,028	$ 27,460,537
Federal funds sold	200,000	500,007
Total cash and cash equivalents	22,800,028	27,960,544
Interest-bearing deposits in banks	10,169,744	4,672,748
Available-for-sale investment securities	9,479,124	8,526,868
Loans, held for sale	1,429,209	1,667,775
Loans, less allowance for loan losses of $2,397,299 in 2013 and $2,349,484 in 2012	123,915,036	105,978,563
Premises and equipment, net	623,104	294,157
Bank-owned life insurance	3,674,584	3,557,327
Other real estate owned	-	80,569
Interest receivable and other assets	3,281,958	2,646,978
Total assets	$ 175,372,787	$ 155,385,529

LIABILITIES AND SHAREHOLDERS' EQUITY

	2013	2012
Deposits		
Non-interest-bearing	$ 52,458,888	$ 61,100,904
Interest-bearing	98,130,275	69,853,866
Total deposits	150,589,163	130,954,770
Federal Home Loan Bank advances and other borrowings	4,945,000	7,000,000
Interest payable and other liabilities	815,744	700,444
Total liabilities	156,349,907	138,655,214
Commitments and contingencies (Note 10)		
Shareholders' equity		
Preferred stock, no par value; 10,000,000 shares authorized; 4,060 shares issued and outstanding in 2013 and 2012	4,060,000	4,060,000
Class A common stock, voting, no par value; 10,000,000 shares authorized; 4,131,924 and 4,115,424 shares issued and outstanding in 2013 and 2012	20,876,079	20,422,249
Class B common stock, non-voting, no par value; 10,000,000 shares authorized; 56,844 shares issued and outstanding in 2013 and 2012	1,421,100	1,421,100
Accumulated deficit	(7,268,801)	(9,223,985)
Accumulated other comprehensive (loss) income, net of taxes	(65,498)	50,951
Total shareholders' equity	19,022,880	16,730,315
Total liabilities and shareholders' equity	$ 175,372,787	$ 155,385,529

	YEARS ENDED DECEMBER 31, 2013	2012
INTEREST INCOME		
Interest and fees on loans	$ 6,876,359	$ 6,010,731
Interest on investment securities	160,412	164,938
Interest on federal funds sold	164	1,123
Interest on deposits in banks	85,505	67,991
	7,122,440	6,244,783
INTEREST EXPENSE		
Interest expense on deposits	344,560	280,670
Interest on borrowings	144,520	154,585
Total interest expense	489,080	435,255
Net interest income	6,633,360	5,809,528
PROVISION FOR LOAN LOSSES	225,000	725,962
Net interest income after provision for loan losses	6,408,360	5,083,566
NON-INTEREST INCOME		
Service charges	291,677	329,640
Government grant	323,000	415,000
Gain on sale of securities	24,031	219,734
Gain on sale of loans, net	561,120	242,938
Other income	434,836	1,106,530
Total non-interest income	1,634,664	2,313,842
NON-INTEREST EXPENSES		
Salaries and employee benefits	3,276,246	2,844,387
Stock option expense	396,455	329,672
Occupancy and equipment	1,042,192	882,741
Loss on sale of other assets	18,500	-
Write-down on other real estate owned	80,570	26,908
Write-down on other asset owned	25,810	-
Other expenses	1,966,067	1,926,830
Total non-interest expenses	6,805,840	6,010,538
Net operating income before provision for income taxes	1,237,184	1,386,870
INCOME TAX (BENEFIT) EXPENSE	(799,200)	800
Net income	2,036,384	1,386,070
Dividends on preferred stock	81,200	60,900
Net income available to common shareholders	$ 1,955,184	$ 1,325,170
NET INCOME PER SHARE – BASIC	$ 0.47	$ 0.32
NET INCOME PER SHARE – DILUTED	$ 0.47	$ 0.32

	YEARS ENDED DECEMBER 31, 2013	2012
Net income	$ 2,036,384	$ 1,386,070
Unrealized (loss) gain on available-for-sale securities, net of tax	(100,589)	113,209
Reclassification adjustment for net gain realized and reported in net income, net of tax	(15,860)	(219,734)
Other comprehensive loss	(116,449)	(106,525)
Total comprehensive income	$ 1,919,935	$ 1,279,545

	Preferred Stock	Class A Common Stock		Class B Common Stock		Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
		Shares	Amount	Shares	Amount			
Balances, January 1, 2012	$ 4,060,000	4,115,424	$ 20,092,577	56,844	$ 1,421,100	$ (10,549,155)	$ 157,476	$ 15,181,998
Stock option exercised	-	-	-	-	-	-	-	-
Stock option expense	-	-	329,672	-	-	-	-	329,672
Dividend paid on preferred stock	-	-	-	-	-	(60,900)	-	(60,900)
Net income	-	-	-	-	-	1,386,070	-	1,386,070
Other comprehensive loss	-	-	-	-	-	-	(106,525)	(106,525)
Balances, December 31, 2012	4,060,000	4,115,424	20,422,249	56,844	1,421,100	(9,223,985)	50,951	16,730,315
Stock option exercised	-	16,500	57,375	-	-	-	-	57,375
Stock option expense	-	-	396,455	-	-	-	-	396,455
Dividend paid on preferred stock	-	-	-	-	-	(81,200)	-	(81,200)
Net income	-	-	-	-	-	2,036,384	-	2,036,384
Other comprehensive loss	-	-	-	-	-	-	(116,449)	(116,449)
Balances, December 31, 2013	$ 4,060,000	4,131,924	$ 20,876,079	56,844	$ 1,421,100	$ (7,268,801)	$ (65,498)	$ 19,022,880

STATEMENTS OF CASH FLOWS

	YEARS ENDED DECEMBER 31,	
	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 2,036,384	$ 1,386,070
Adjustments to reconcile net income to net cash from operating activities:		
Provision for loan losses	225,000	725,962
Change in deferred loan origination fees, net	(1,891)	37,901
Depreciation, amortization, and accretion	217,969	257,439
Gain on sale of securities	(24,031)	(219,734)
Proceeds from the sale of loans held for sale	6,004,808	3,320,785
Originations of loans held for sale	(5,169,617)	(4,531,447)
Gain on sale of loans	(596,625)	(242,938)
Loss on sale of other assets	18,500	-
Stock option expense	396,455	329,672
Write-down of other real estate owned	80,570	26,908
Write-down of other asset owned	25,810	236,727
Increase in cash surrender value of bank owned life insurance	(117,257)	(125,716)
Increase in interest receivable and other assets	(913,697)	(683,410)
Increase (decrease) in interest payable and other liabilities	115,299	(713,970)
Net cash from operating activities	2,297,677	(195,751)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sold, called, and matured available-for-sale investment securities	1,269,688	3,009,708
Proceeds from principal repayments from available-for-sale investment securities	1,643,663	1,379,056
Purchases of available-for-sale investment securities	(4,170,275)	(5,113,729)
Purchase of interest-bearing deposits	(5,496,996)	(153,173)
Net increase in loans	(18,159,582)	(8,277,647)
Purchases of premises and equipment	(430,831)	(324,496)
Purchases of FHLB stock	105,100	48,900
Proceeds from sale of premises and equipment	11,282	790,353
Proceeds from sale of other assets owned	214,190	-
Net cash from investing activities	(25,013,761)	(8,641,028)

	YEARS ENDED DECEMBER 31,	
	2013	2012
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net (decrease) increase in demand,		
interest-bearing and savings deposits	(7,731,318)	21,687,689
Net increase in time deposits	27,365,711	3,967,868
Dividends paid on preferred stock	(81,200)	(60,900)
Increase in FHLB borrowings	-	1,000,000
Repayment of FHLB borrowings	(3,000,000)	(1,000,000)
Proceeds from federal funds purchased	945,000	-
Proceeds from exercise of stock options	57,375	-
Net cash from financing activities	17,555,568	25,594,657
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(5,160,516)	16,757,878
CASH AND CASH EQUIVALENTS, beginning of year	27,960,544	11,202,666
CASH AND CASH EQUIVALENTS, end of year	$ 22,800,028	$ 27,960,544
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest expense	$ 475,900	$ 459,985
Income taxes	$ -	$ 241,200
Non-cash investing and financing activities:		
Net loans from the sale of building and land	$ -	$ 2,700,000

NOTE 1 – ORGANIZATION AND NATURE OF BUSINESS

General – Community Bank of the Bay (the Bank) is a California state chartered bank that commenced banking operations on July 22, 1996. The Bank provides a range of banking services to individuals and businesses in the greater San Francisco Bay area, especially businesses employing residents of low and moderate income neighborhoods. The Bank's primary source of revenue is generated from providing loans to customers who are predominately small and middle market businesses and individuals residing in the surrounding areas.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the Bank conform with accounting principles generally accepted in the United States of America and prevailing practices within the banking industry.

Use of estimates – The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The allowance for loan losses is the most significant accounting estimate reflected in the Bank's financial statements. The allowance for loan losses includes charges to reduce the recorded balances of loans receivable to their estimated net realizable value, as appropriate. The allowance is based on estimates, and ultimate losses may vary from current estimates. These estimates for losses are based on individual assets and their related cash flow forecasts, sales values, independent appraisals, the volatility of certain real estate markets, and concern for disposing of real estate in distressed markets. Although management of the Bank believes the estimates underlying the calculation of specific allowances are reasonable, there can be no assurances that the Bank could ultimately realize these values. In addition to providing valuation allowances on specific assets where a decline in value has been identified, the Bank establishes general valuation allowances for losses based on the overall portfolio composition, general market conditions, concentrations, and prior loss experience.

Other significant management judgments and accounting estimates reflected in the Bank's financial statements include:

- Decisions regarding the timing and placement of loans on non-accrual;
- Determination, recognition, and measurement of impaired loans;
- Determination and evaluation of deferred tax assets and liabilities;
- Determination of the fair value of stock option awards;
- Determination of the fair value of financial instruments; and
- Determination of the fair value of other real estate owned.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Concentrations of credit risk – Assets and liabilities that subject the Bank to concentrations of credit risk consist of loans and deposits. Most of the Bank's customers are located within Alameda and Contra Costa counties and the surrounding areas. The Bank's primary lending products are discussed in Note 5 to the financial statements. The Bank did not have any significant concentrations in its business with any one customer or industry. The Bank obtains what it believes to be sufficient collateral to secure potential losses on loans. The extent and value of collateral varies based upon the details underlying each loan agreement.

As of December 31, 2013 and 2012, the Bank had cash deposits at other financial institutions in excess of FDIC insured limits. However, as the Bank places these deposits with major financial institutions and monitors the financial condition of these institutions, management believes the risk of loss to be minimal.

Cash and cash equivalents – For purposes of the statement of cash flows, the Bank considers cash, due from banks, money market funds, federal funds sold, and securities purchased under agreements to resell to be cash equivalents. All have maturities of three months or less.

Available-for-sale investment securities – Available-for-sale securities are reported at fair value, with unrealized gains and losses excluded from earnings and reported, net of taxes, as accumulated other comprehensive income (loss) within shareholders' equity.

Management determines the appropriate classification of its investment securities at the time of purchase and may only change the classification in certain limited circumstances. At December 31, 2013 and 2012, all of the Bank's investments were classified as available for sale.

Gains and losses on the sale of investment securities are computed using the specific identification method. Interest earned on investment securities is reported in interest income, net of applicable adjustments for accretion of discounts and amortization of premiums.

Investments with fair values that are less than amortized cost are considered impaired. Impairment may result from either a decline in the financial condition of the issuing entity or, in the case of fixed interest rate investments, from rising interest rates. At each financial statement date, management assesses each investment to determine if impaired investments are temporarily impaired or if the impairment is other than temporary. This assessment includes a determination of whether the Bank intends to sell the security, or if it is more likely than not that the Bank will be required to sell the security before recovery of its amortized cost basis less any current-period credit losses. For debt securities that are considered other than temporarily impaired and that the Bank does not intend to sell and will not be required to sell prior to recovery of the amortized cost basis, the amount of impairment is separated into the amount that is credit related (credit loss component) and the amount due to all other factors. The credit loss component is recognized in earnings and is calculated as the difference between the security's amortized cost basis and the present value of its expected future cash flows. The remaining difference between the security's fair value and the present value of the future expected cash flows is deemed to be due to factors that are not credit related and is recognized in other comprehensive income (loss).

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investment in Federal Home Loan Bank stock – In order to borrow from the Federal Home Loan Bank (FHLB), the Bank is required to maintain an investment in FHLB capital stock. The investment of $580,100 and $475,000 at December 31, 2013 and 2012, respectively, is carried at cost, redeemable at par, at the discretion of the FHLB, and included in interest receivable and other assets on the balance sheet.

Loans and loan fees – Loans are reported at their principal outstanding balance net of charge-offs. Loan origination fees and certain direct loan origination costs are deferred and the net amounts are amortized to interest income by a method that approximates a level yield over the contractual life of the underlying loans.

Income recognition on loans – Interest on loans, other than discounted installment loans, is credited to income based on the principal amount outstanding on a daily basis. Interest on discounted installment loans is recognized by a method which approximates the effective interest method. Interest accruals are discontinued on certain loans when collection of principal or interest is considered doubtful, or when a loan becomes contractually past due by 90 days or more with respect to interest or principal. When a loan is placed on non-accrual status, all interest previously accrued but not collected is reversed against current period interest income. Income on such loans is then recognized only to the extent that cash is received and where the future collection of principal is probable. Interest accruals are resumed on such loans when, in the judgment of management, the loans are estimated to be fully collectible as to both principal and interest.

Allowance for loan losses – The allowance for loan losses is established through a provision for loan losses charged to operations. The adequacy of the allowance for loan losses is periodically evaluated by the Bank in order to maintain the allowance at a level that, in the opinion of management, is adequate to absorb losses inherent in existing loans. Management's evaluation of the adequacy of the allowance is based on a consideration of the Bank's historical loss experience, known and inherent risks in the loan portfolio, including adverse circumstances that may affect the ability of the borrower to repay interest and/or principal, the estimated value of any underlying collateral, and an analysis of the levels and trends of delinquencies and charge-offs. Actual results could differ from those estimates.

When a loan or portion of a loan is determined to be uncollectible, the portion deemed uncollectible is charged against the allowance and subsequent recoveries, if any, are credited to the allowance.

The allowance consists of specific, general, and unallocated components. The specific component relates to loans that are classified as impaired. Impaired loans, as defined, are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent. The general component relates to non-impaired loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component may be maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Allowance for loan losses (continued) – A loan is considered impaired if, based on current information and events, it is probable that 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. Generally, the Bank measures impaired loans based on the present value of expected future cash flows discounted at the historical effective interest rate, except that all collateral-dependent loans are measured for impairment based on the fair value of the collateral.

Troubled debt restructuring – In situations where, for economic or legal reasons related to a borrower's financial difficulties, the Bank grants a concession to the borrower that it would not otherwise consider, the related loan is classified as a troubled debt restructuring. The Bank measures any loss on the troubled debt restructuring in accordance with the guidance concerning impaired loans set forth above. Additionally, loans modified in troubled debt restructurings are generally placed on non-accrual status at the time of restructuring. These loans are returned to accrual status after the borrower demonstrates performance with the modified terms for a sustained period of time (generally six months) and has the capacity to continue to perform in accordance with the modified terms of the restructured debt.

Loans held for sale – The Bank has originated government guaranteed loans to customers under the Small Business Administration (SBA) program. The SBA provides guarantees of 75% to 90% of each loan. For some of these loans, the Bank sells the guaranteed portion of the loan to a third party and retains the unguaranteed portion in its own portfolio. Loans held for sale include government loans and are reported at the lower of cost or market value. Cost generally approximates market value, given the short duration of these assets. Gains or losses on the sale of loans that are held for sale are recognized at the time of the sale, subject to the expiration of any warranty or recourse provisions, and determined by the difference between net sale proceeds and the net book value of the loans less the estimated fair value of any retained mortgage servicing rights.

Servicing assets – Periodically, the Bank sells loans and retains the servicing rights. The gain or loss on sale of loans depends in part on the previous carrying amount of the financial assets involved in the transfer, allocated between the assets sold and the retained interests based on their relative fair value at the date of transfer. To obtain fair values, quoted market prices are used, if available. However, quotes are generally not available for retained interests, so the Bank generally estimates fair value based on the present value of future expected cash flows using management's best estimates of the key assumptions – credit losses, prepayment speeds, forward yield curves, and discount rates commensurate with the risks involved.

The Bank accounts for the transfer and servicing of financial assets based on the financial and servicing assets it controls and liabilities it has incurred, derecognizes financial assets when control has been surrendered, and derecognizes liabilities when extinguished.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Servicing assets (continued) – Total servicing assets included in other assets were $344,916 and $230,865 at December 31, 2013 and 2012, respectively. The Bank evaluated the servicing asset for impairment at December 31, 2013 and 2012, and determined that no valuation allowance was needed.

The Bank services loans that have been participated with other financial institutions totaling $26,597,115 and $19,758,370 as of December 31, 2013 and 2012, respectively. These loans were sold without recourse and, therefore, the sold balances are not included on the Bank's balance sheet.

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 rights (free of conditions that prevent 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.

The Bank sells certain portions of government guaranteed loans in the secondary market. These sales are recorded by the Bank when control is surrendered and any warranty period or recourse provision expires. There were no warranty or recourse provisions outstanding at December 31, 2013 for loans sold during 2013 and 2012.

Premises and equipment – Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are provided for in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives using the straight-line basis. The estimated lives used in determining depreciation are:

Leasehold improvements	5 years
Furniture, fixtures, and equipment	3 – 7 years

Leasehold improvements are amortized over the lesser of the useful life of the asset or the term of the lease. The straight-line method of depreciation is followed for all assets for financial reporting purposes, but accelerated methods are used for tax purposes. Deferred income taxes have been provided for the resulting temporary differences.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Bank-owned life insurance – The Bank has purchased insurance on the lives of Bank executives. The policies accumulate asset values to meet future liabilities including payment of employee benefits such as split dollar life insurance agreements, which provide an insurance benefit to the family of the individual on whom the policy is held. The cash surrender value of policies is recorded as an asset on the balance sheets. Increases in the cash surrender value are recorded as other non-interest income in the statements of operations.

Other real estate owned – Other real estate owned is comprised of property acquired through foreclosure in satisfaction of indebtedness. These properties are recorded at fair value less estimated selling costs at the time of foreclosure establishing a new cost basis. Revised estimates to the fair value less cost to sell are reported as adjustments to the carrying amount of the asset, provided that such adjusted value is not in excess of the carrying amount at acquisition. Initial losses on properties acquired through full or partial satisfaction of debt are treated as credit losses and charged to the allowance for loan losses at the time of acquisition. Subsequent declines in value from the recorded amounts, routine holding costs, and gains or losses upon disposition, if any, are included in non-interest income or expense as incurred.

Income taxes – The Bank uses the asset and liability method to account for income taxes. Under such method, deferred tax assets and liabilities are recognized for the future tax consequences of differences between financial statement carrying amounts of existing assets and liabilities and their respective tax basis (temporary differences). Deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the year in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes in the year of enactment.

A valuation allowance is established to the extent that it is more likely than not that the benefits associated with the deferred tax assets will not be fully realized.

The Bank had no unrecognized tax benefits at December 31, 2013 and 2012.

The Bank recognizes interest accrued and penalties related to unrecognized tax benefits in tax expense. During the years ended December 31, 2013 and 2012, the Bank recognized no interest and penalties.

With few exceptions, the Bank is no longer subject to examinations by U.S. federal taxing authorities for years ended before December 31, 2010, and by state authorities for years ended before December 31, 2009.

Comprehensive income – Comprehensive income includes net income and other comprehensive income. The Bank's primary source of comprehensive income is unrealized gains and losses on securities available for sale. Reclassification adjustments result from gains or losses on securities that are realized and included in net income of the current period that also had been included in other comprehensive income as unrealized holding gains or losses in the period in which they arose. Total comprehensive income and the components of accumulated other comprehensive income are presented in the statements of comprehensive income.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Stock-based compensation – The Bank recognizes compensation expense for awards of stock options to employees and directors based on the grant-date fair value of those awards. The fair value of each option granted is estimated on the date of grant using the Black-Scholes options-pricing model. The assumptions used in this model include an estimate of expected volatility, which is based on the historical volatility of the price of similar bank stocks, and an estimate of the expected option term, which is based on consideration of the vesting period and contractual term of the option. In addition, the Bank estimates the number of options expected to be forfeited based on historical forfeiture rates. The risk-free interest rates are equal to the U.S. Treasury yield at the time of the grant and commensurate with the expected term of the grant. Expense is recognized over the vesting period of the options. The Bank's stock compensation plan and related assumptions used in determining the fair value of awards are discussed in Note 11.

Advertising costs – The Bank expenses advertising costs as they are incurred. Advertising expense was $65,594 and $49,439 for the years ended December 31, 2013 and 2012, respectively.

Net income per share – Basic net income per share amounts are computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the year. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock, such as stock options, result in the issuance of common stock which share in the earnings of the Bank. The treasury stock method is applied to determine the dilutive effect of stock options when computing diluted earnings per share. However, dilutive earnings per share amounts are not presented when a net loss occurs because the conversion of potential common stock is anti-dilutive.

Reclassifications – Certain prior year amounts have been reclassified to conform with the current year presentation.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Recent accounting pronouncements – a**doption of new accounting standards –** In February 2013, the FASB issued ASU No. 2013-02, *Comprehensive Income (Topic 220): Reporting Amounts Reclassified Out of Accumulated Other Comprehensive Income.* The ASU requires entities to provide enhanced disclosures to present separately by component reclassifications out of accumulated other comprehensive income. An entity is required to disclose in the notes to the financial statements or parenthetically on the face of the financial statements, the effect of significant items reclassified out of accumulated other comprehensive income on the respective line items of net income, but only if the item reclassified is required under U.S. GAAP to be reclassified to net income in its entirety. ASU No. 2013-02 is effective for fiscal years beginning on or after December 15, 2012. Adoption of this ASU in 2013 did not have a significant impact on the Bank's financial statements.

In January 2014, the FASB issued ASU No. 2014-04, *Receivables—Troubled Debt Restructurings by Creditors (Subtopic 310-40): Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans Upon Foreclosure*, a consensus of the FASB Emerging Issues Task Force. The amendments in this update clarify that an in-substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either: (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure, or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Additionally, the amendments require interim and annual disclosure of both: (1) the amount of foreclosed residential real estate property held by the creditor, and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to local requirements of the applicable jurisdiction. The amendments in this update are effective annual periods, and interim periods within those annual periods, beginning after December 15, 2014. The Bank does not expect this ASU to have an impact on its financial condition or results of operations as it affects presentation only.

NOTE 3 – CASH AND DUE FROM BANKS

Cash and due from banks includes balances with the Federal Reserve Bank and other correspondent banks. The average reserve requirements are based on a percentage of the Bank's deposit liabilities. In addition, the Federal Reserve Bank requires the Bank to maintain a certain minimum balance at all times. At December 31, 2013 and 2012, the Bank's cash balances were sufficient to comply with this reserve requirement and, therefore, no such reserve balances were required to be held with the Federal Reserve Bank.

NOTE 4 – AVAILABLE-FOR-SALE INVESTMENT SECURITIES

The amortized cost and estimated fair value of available-for-sale securities as of December 31, 2013 and 2012 are as follows:

	2013			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Municipal securities (taxable)	$ 1,205,784	$ 7,824	$ (54,724)	$ 1,158,884
Municipal securities (non taxable)	509,194	-	(9,139)	500,055
U.S. agency	500,000	-	(33,245)	466,755
Mortgage-backed securities	3,006,878	11,638	(41,010)	2,977,506
CMOs	2,233,807	39,838	(66)	2,273,579
Corporates	661,019	174	(3,243)	657,950
U.S. Treasury	1,461,683	-	(17,288)	1,444,395
	$ 9,578,365	$ 59,474	$ (158,715)	$ 9,479,124

	2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Municipal securities (taxable)	$ 1,476,275	$ 43,376	$ (18,178)	$ 1,501,473
U.S. agency	500,000	-	(1,950)	498,050
Mortgage-backed securities	2,870,716	29,085	(9,926)	2,889,875
CMOs	2,582,972	41,315	(15,487)	2,608,800
U.S. Treasury	994,813	33,857	-	1,028,670
	$ 8,424,776	$ 147,633	$ (45,541)	$ 8,526,868

Proceeds from the sales of investment securities totaled $1,019,688 and $3,009,708 during the years ended December 31, 2013 and 2012, respectively. Gross realized gains totaled $24,031 and $219,743 during 2013 and 2012, respectively. There were no realized losses during 2013 or 2012.

NOTE 4 – AVAILABLE-FOR-SALE INVESTMENT SECURITIES (CONTINUED)

Available-for-sale investment securities with unrealized losses at December 31, 2013 and 2012 are summarized and classified according to the duration of the loss period as follows:

	2013					
	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Municipal securities (taxable)	$ 821,163	$ (14,514)	$631,092	$ (49,349)	$ 1,452,255	$ (63,863)
U.S. agency	466,755	(33,245)	-	-	466,755	(33,245)
Mortgage-backed securities	2,012,469	(40,983)	356,627	(27)	2,369,096	(41,010)
CMOs	495,370	(66)	-	-	495,370	(66)
Corporates	310,908	(3,243)	-	-	310,908	(3,243)
U.S. Treasury	1,444,395	(17,288)	-	-	1,444,395	(17,288)
	$5,551,060	$ (109,339)	$987,719	$ (49,376)	$ 6,538,779	$ (158,715)

	2012					
	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Municipal securities (taxable)	$ 929,059	$ (18,178)	$ -	$ -	$ 929,059	$ (18,178)
U.S. agency	498,050	(1,950)	-	-	498,050	(1,950)
Mortgage-backed securities	1,863,959	(9,926)	-	-	1,863,959	(9,926)
CMOs	1,029,300	(15,487)	-	-	1,029,300	(15,487)
	$4,320,368	$ (45,541)	$ -	$ -	$ 4,320,368	$ (45,541)

Certain investment securities shown above currently have fair values less than amortized cost and, therefore, contain unrealized losses. The Bank does not have the intent to sell the investments that are temporarily impaired, and it is more likely than not that the Bank will not be required to sell those investments before recovery of the amortized cost basis. The Bank has evaluated these securities and has determined that the decline in value is not other than temporary and is related to the change in market interest rates since purchase. The decline in value is not related to any company or industry specific event. These temporary unrealized losses relate principally to current interest rates for similar types of securities. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. There were 15 and 8 investment securities with unrealized losses at December 31, 2013 and 2012, respectively. The Bank anticipates full recovery of amortized cost with respect to these securities at maturity or sooner in the event of a more favorable market interest rate environment.

NOTE 4 – AVAILABLE-FOR-SALE INVESTMENT SECURITIES (CONTINUED)

The amortized cost and estimated fair value of available-for-sale investment securities at December 31, 2013 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because the issuers of the securities may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
Due in one year or less	$ -	$ -
Due after one year through five years	1,471,966	1,466,833
Due after five years through ten years	3,912,110	3,800,314
Due after ten years	4,194,289	4,211,977
	$ 9,578,365	$ 9,479,124

Investment securities with amortized costs of $3,572,883 and $2,205,605 and estimated fair values of $3,640,141 and $2,269,984 were pledged to secure public funds, lines of credit, and Federal Home Loan Bank advances at December 31, 2013 and 2012, respectively.

NOTE 5 – LOANS

Outstanding loans, by class, are summarized as follows:

	DECEMBER 31,	
	2013	2012
Commercial	$ 50,975,040	$ 43,838,051
Commercial real estate		
Non-owner occupied	37,298,927	36,569,397
Owner occupied	33,297,667	26,151,987
Construction and land	2,854,862	305,138
Consumer	1,922,075	1,497,819
	126,348,571	108,362,392
Deferred loan and costs, net	(36,236)	(34,345)
Allowance for loan losses	(2,397,299)	(2,349,484)
	$ 123,915,036	$ 105,978,563

Salaries and employee benefits totaling $308,000 and $190,375 have been deferred as loan origination costs for the years ended December 31, 2013 and 2012, respectively.

NOTE 5 – LOANS (CONTINUED)

The Bank has certain lending policies and procedures in place that are designed to maximize loan income within an acceptable level of risk. Management reviews and approves these policies and procedures on a regular basis. A reporting system supplements the review process by providing management with frequent reports related to loan production, loan quality, concentrations of credit, loan delinquencies, and non-performing and potential problem loans. Diversification in the loan portfolio is a means of managing risk associated with fluctuations in economic conditions.

Commercial loans are underwritten after evaluating and understanding the borrower's ability to operate profitably and prudently expand its business. Underwriting standards are designed to promote relationship banking rather than transactional banking. Once it is determined that the borrower's management possesses sound ethics and solid business acumen, the Bank's management examines current and projected cash flows to determine the ability of the borrower to repay their obligations as agreed. Commercial loans are primarily made based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory and may incorporate a personal guarantee; however, some short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

Commercial real estate loans are subject to underwriting standards and processes similar to commercial loans, in addition to those of real estate loans. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally largely dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. The properties securing the Bank's commercial real estate portfolio are diverse in terms of type and geographic location. This diversity helps reduce the Bank's exposure to adverse economic events that affect any single market or industry. Management monitors and evaluates commercial real estate loans based on collateral, geography, and risk grade criteria. As a general rule, the Bank avoids financing single-purpose projects unless other underwriting factors are present to help mitigate risk. The Bank also utilizes third-party experts to provide insight and guidance about economic conditions and trends affecting market areas it serves. In addition, management tracks the level of owner-occupied commercial real estate loans versus non-owner occupied loans.

NOTE 5 – LOANS (CONTINUED)

With respect to loans to developers and builders that are secured by non-owner occupied properties that the Bank may originate from time to time, the Bank generally requires the borrower to have had an existing relationship with the Bank and have a proven record of success. Construction loans are underwritten utilizing feasibility studies, independent appraisal reviews, sensitivity analysis of absorption and lease rates, and financial analysis of the developers and property owners. Construction loans are generally based upon estimates of costs and value associated with the completed project. These estimates may be inaccurate. Construction loans often involve the disbursement of substantial funds with repayment substantially dependent on the success of the ultimate project. Sources of repayment for these types of loans may be pre-committed permanent loans from approved long-term lenders, sales of developed property, or an interim loan commitment from the Bank until permanent financing is obtained. These loans are closely monitored by on-site inspections and are considered to have higher risks than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, governmental regulation of real property, general economic conditions, and the availability of long-term financing.

Consumer loans primarily consist of home equity lines of credit and loans and other personal loans. We originate consumer loans utilizing credit history information, debt-to-income ratio, and loan-to-value ratio analysis. We also evaluate the consumer's liquid assets and their ability to supplement cash flow for debt payment. To monitor and manage consumer loan risk, policies and procedures are developed and modified, as needed. This activity, coupled with relatively small loan amounts that are spread across many individual borrowers, minimizes risk. Underwriting standards for home equity loans include, but are not limited to, a maximum loan-to-value percentage of 80%, collection remedies, the number of such loans a borrower can have at one time, and documentation requirements. Personal loans are nearly evenly split between mobile home loans along with a small number of direct auto loans and installment loans. Personal unsecured loans are offered to consumers with additional underwriting procedures in place, including net worth and borrower's verified liquid assets analysis. In general, personal loans usually have a higher degree of risk than other types of loans.

The Bank utilizes an independent third party loan review consultant to review and validate the credit risk program on a periodic basis. Results of these reviews are presented to management and the Bank's Board of Directors. The loan review process complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel, as well as the Bank's policies and procedures.

NOTE 5 – LOANS (CONTINUED)

The following table summarizes the credit quality indicators related to the Bank's loans, by class, as of December 31, 2013:

	Pass	Special Mention	Substandard	Doubtful	Totals
Commercial	$ 46,825,966	$ 1,560,215	$ 2,588,859	$ -	$ 50,975,040
Commercial real estate					
Non-owner occupied	34,322,600	2,171,702	804,625	-	37,298,927
Owner occupied	30,143,550	-	3,154,117	-	33,297,667
Construction and land	2,652,727	-	202,135	-	2,854,862
Consumer	1,922,075	-	-	-	1,922,075
Total	$115,866,918	$ 3,731,917	$ 6,749,736	$ -	$ 126,348,571

The following table summarizes the credit quality indicators related to the Bank's loans, by class, as of December 31, 2012:

	Pass	Special Mention	Substandard	Doubtful	Totals
Commercial	$ 39,545,948	$ 1,089,671	$ 3,202,432	$ -	$ 43,838,051
Commercial real estate					
Non-owner occupied	35,890,068	-	679,329	-	36,569,397
Owner occupied	23,699,574	-	2,452,413	-	26,151,987
Construction and land	-	-	305,138	-	305,138
Consumer	1,346,821	-	150,998	-	1,497,819
Total	$100,482,411	$ 1,089,671	$ 6,790,310	$ -	$ 108,362,392

As a part of the on-going monitoring of the credit quality of the Bank's loan portfolio, management monitors certain credit quality indicators including trends related to risk grade classifications, concentrations, net charge-offs, non-performing loans, and the general economic conditions.

NOTE 5 – LOANS (CONTINUED)

The Bank uses a risk grading system to assign a risk grade to each of its loans. Loans are graded on a scale of 1 to 9, with grades 1 to 5 being termed pass loans and grades 6, 7, 8, and 9 being termed special mention, substandard, doubtful, and loss, respectively. A description of the general characteristics of the nine grades is as follows:

Pass (grades 1 – 5) – These loans generally conform to the Bank's underwriting criteria and evidence an acceptable level of credit risk.

Special Mention (grade 6) – These loans have weaknesses that require management's close attention. These weaknesses expose the Bank to a sufficient degree of risk to warrant classification. If left uncorrected, these weaknesses will result in deterioration of the loan's repayment prospects or the borrower's credit position at a future date. Loans in this category are currently protected, but are potentially weak. The loans may (particularly in the short term) constitute a greater than average credit risk, but do not presently expose the Bank to a sufficient degree of risk to warrant adverse classification. This is a temporary classification pending identification of improvement or deterioration in the criticized asset.

Substandard (grade 7) – Substandard loans are inadequately protected by the current net worth and financial capacity of the borrower or 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 Bank will sustain some loss if the deficiencies are not corrected. Loss potential, while existing in the aggregate amount of substandard loans, does not have to exist in individual loans classified substandard.

Doubtful (grade 8) – Loans classified doubtful have all the weaknesses inherent in those classified as substandard with the added characteristic that the weaknesses make collection in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The probability of loss is extremely high but because of certain important and reasonably specific pending factors which may work to strengthen (or weaken) the loan, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors that may necessitate a doubtful classification include bankruptcy or liquidation procedures, capital injection, or perfecting liens on additional collateral refinancing plans. The Bank considers doubtful to be a temporary classification and will only classify an asset, or portion of an asset, as such when information is not available to conclude as to classification or more clearly define the potential for loss.

Loss (grade 9) – Assets classified loss are considered uncollectible and of such little value that their continuance as assets is not warranted. This classification does not mean that an asset has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off a basically worthless asset even though partial recovery may be affected in the future. Losses are taken in the period in which they are identified as uncollectible.

NOTE 5 – LOANS (CONTINUED)

Age analysis of past due loans – The age analysis of past due loans by class as of December 31, 2013 consisted of the following:

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Recorded Investment > 90 Days and Accruing
Commercial	$ 643,130	$ -	$ -	$ 643,130	$ 50,331,910	$ 50,975,040	$ -
Commercial real estate							
Non-owner occupied	266,691	-	-	266,691	37,032,236	37,298,927	-
Owner occupied	-	-	-	-	33,297,667	33,297,667	-
Construction and land	-	-	-	-	2,854,862	2,854,862	-
Consumer	-	-	-	-	1,922,075	1,922,075	-
Total	$ 909,821	$ -	$ -	$ 909,821	$ 125,438,750	$ 126,348,571	$ -

The age analysis of past due loans by class as of December 31, 2012 consisted of the following:

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Recorded Investment > 90 Days and Accruing
Commercial	$ 400,000	$ 273,261	$ 1,716,180	$ 2,389,441	$ 41,448,610	$ 43,838,051	$ -
Commercial real estate							
Non-owner occupied	-	-	-	-	36,569,397	36,569,397	-
Owner occupied	-	899,013	-	899,013	25,252,974	26,151,987	-
Construction and land	-	-	-	-	305,138	305,138	-
Consumer	-	-	-	-	1,497,819	1,497,819	-
Total	$ 400,000	$ 1,172,274	$ 1,716,180	$ 3,288,454	$ 105,073,938	$ 108,362,392	$ -

NOTE 5 – LOANS (CONTINUED)

Information related to impaired loans by class as of December 31, 2013 and for the year then ended consisted of the following:

	Commercial	Commercial Real Estate Non-Owner Occupied	Commercial Real Estate Owner Occupied	Construction and Land	Consumer	Total
Recorded investment in impaired loans:						
With no specific allowance recorded	$ 426,385	$ 537,934	$ 772,636	$ 202,135	$ -	$ 1,939,090
With a specific allowance recorded	187,418	-	1,406,460	-	-	1,593,878
Total recorded investment in impaired loans	$ 613,803	$ 537,934	$ 2,179,096	$ 202,135	$ -	$ 3,532,968
Unpaid principal balance of impaired loans:						
With no specific allowance recorded	$ 443,400	$ 537,934	$ 928,161	$ 206,320	$ -	$ 2,115,815
With a specific allowance recorded	200,287	-	1,433,180	-	-	1,633,467
Total unpaid principal balance of impaired loans	$ 643,687	$ 537,934	$ 2,361,341	$ 206,320	$ -	$ 3,749,282
Specific allowance	$ 8,991	$ -	$ 48,203	$ -	$ -	$ 57,194
Average recorded investment in impaired loans during the year	1,108,287	608,632	2,082,961	253,637	-	4,053,516
Interest income recognized in impaired loans during the year	60,050	45,548	-	-	-	105,598

Information related to impaired loans by class as of December 31, 2012 and for the year then ended consisted of the following:

	Commercial	Commercial Real Estate Non-Owner Occupied	Commercial Real Estate Owner Occupied	Construction and Land	Consumer	Total
Recorded investment in impaired loans:						
With no specific allowance recorded	$ 903,075	$ 679,329	$ 1,986,826	$ 305,138	$ -	$ 3,874,368
With a specific allowance recorded	699,695	-	-	-	150,998	850,693
Total recorded investment in impaired loans	$ 1,602,770	$ 679,329	$ 1,986,826	$ 305,138	$ 150,998	$ 4,725,061
Unpaid principal balance of impaired loans:						
With no specific allowance recorded	$ 1,291,400	$ 934,382	$ 2,153,454	$ 309,323	$ -	$ 4,688,559
With a specific allowance recorded	722,310	-	-	-	157,841	880,151
Total unpaid principal balance of impaired loans	$ 2,013,710	$ 934,382	$ 2,153,454	$ 309,323	$ 157,841	$ 5,568,710
Specific allowance	$ 46,118	$ -	$ -	$ -	$ 76,177	$ 122,295
Average recorded investment in impaired loans during the year	1,203,660	1,131,398	2,076,350	385,571	152,916	4,949,895
Interest income recognized in impaired loans during the year	-	-	-	-	-	-

NOTE 5 – LOANS (CONTINUED)

Year end non-accrual loans, segregated by class, are as follows:

	DECEMBER 31, 2013	DECEMBER 31, 2012
Commercial	$ 923,335	$ 2,565,719
Commercial real estate		
Non-owner occupied	266,691	-
Owner occupied	1,600,667	1,087,813
Construction and land	202,135	-
Consumer	-	150,998
	$ 2,992,828	$ 3,804,530

Changes in the allowance for loan losses, by class, for the year ended December 31, 2013 were as follows:

	Commercial	Commercial Real Estate	Construction and Land	Consumer	Unallocated	Total
Allowance for credit losses						
Beginning balance	$ 1,253,430	$ 981,565	$ -	$ 95,080	$ 19,409	$ 2,349,484
Charge-offs	(39,051)	(15,818)	-	(147,316)	-	(202,185)
Recoveries	25,000	-	-	-	-	25,000
Provision	(177,690)	283,821	41,401	170,808	(93,340)	225,000
Ending balance	$ 1,061,689	$ 1,249,568	$ 41,401	$ 118,572	$ (73,931)	$ 2,397,299
Period-end amount allocated to:						
Loans individually evaluated for impairment	$ 8,991	$ 48,203	$ -	$ -	$ -	$ 57,194
Loans collectively evaluated for impairment	1,052,698	1,201,365	41,401	118,572	(73,931)	2,340,105
Ending balance	$ 1,061,689	$ 1,249,568	$ 41,401	$ 118,572	$ (73,931)	$ 2,397,299
Loans						
Individually evaluated for impairment	$ 613,803	$ 2,717,030	$ 202,135	$ -	$ -	$ 3,532,968
Collectively evaluated for impairment	50,361,237	67,879,564	2,652,727	1,922,075	-	122,815,603
Ending balance	$ 50,975,040	$ 70,596,594	$ 2,854,862	$ 1,922,075	$ -	$ 126,348,571

NOTE 5 – LOANS (CONTINUED)

Changes in the allowance for loan losses, by class, for the year ended December 31, 2012 were as follows:

	Commercial	Commercial Real Estate	Construction and Land	Consumer	Unallocated	Total
Allowance for credit losses						
Beginning balance	$ 912,233	$ 1,022,421	$ 31,747	$ 46,819	$ -	$ 2,013,220
Charge-offs	(275,493)	(195,974)	-	-	-	(471,467)
Recoveries	78,476	-	-	3,293	-	81,769
Provision	538,214	155,118	(31,747)	44,968	19,409	725,962
Ending balance	$ 1,253,430	$ 981,565	$ -	$ 95,080	$ 19,409	$ 2,349,484
Period-end amount allocated to:						
Loans individually evaluated for impairment	$ 46,118	$ -	$ -	$ 76,177	$ -	$ 122,295
Loans collectively evaluated for impairment	1,207,312	981,565	-	18,903	19,409	2,227,189
Ending balance	$ 1,253,430	$ 981,565	$ -	$ 95,080	$ 19,409	$ 2,349,484
Loans						
Individually evaluated for impairment	$ 1,602,770	$ 2,666,155	$ 305,138	$ 150,998	$ -	$ 4,725,061
Collectively evaluated for impairment	42,235,281	60,055,229	-	1,346,821	-	103,637,331
Ending balance	$ 43,838,051	$ 62,721,384	$ 305,138	$ 1,497,819	$ -	$ 108,362,392

NOTE 5 – LOANS (CONTINUED)

The following table summarizes loans to customers whose loan terms were modified in troubled debt restructurings:

	Year ended December 31, 2013		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings			
Commercial real estate			
Non-owner occupied	1	$ 999,645	$ 799,645
Owner occupied	1	899,013	883,195
	2	$ 1,898,658	$ 1,682,840

	Year ended December 31, 2012		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings			
Commercial and industrial	1	$ 58,200	$ 50,729
Commercial real estate			
Non-owner occupied	1	400,619	267,717
	2	$ 458,819	$ 318,446

During both 2013 and 2012, there were two loans that were modified and considered troubled debt restructurings because specific interest rate concessions or payment term concessions were granted to the borrower. The Bank had no obligations to lend additional funds on the restructured loans as of December 31, 2013 and 2012.

Interest recognized for cash payments received on non-accrual loans was not significant for the years ended December 31, 2013 and 2012. At December 31, 2013 and 2012, there were no loans over 90 days past due that were still accruing interest.

There were no troubled debt restructurings in 2013 that subsequently defaulted. During 2012, there was one owner-occupied commercial real estate troubled debt restructuring to one borrower for $1,149,761 that defaulted subsequently to restructuring and was placed on non-accrual as of December 31, 2012.

NOTE 6 – PREMISES AND EQUIPMENT

Premises and equipment consisted of the following:

	DECEMBER 31, 2013	DECEMBER 31, 2012
Leasehold improvements	$ 238,060	$ 142,500
Furniture, fixtures, and equipment	507,433	775,397
	745,493	917,897
Less accumulated depreciation and amortization	(122,389)	(623,740)
	$ 623,104	$ 294,157

Depreciation and amortization included in occupancy and equipment expense totaled $90,602 and $144,250 for the years ended December 31, 2013 and 2012, respectively. During 2012, the Bank completed the sale of the Oakland building and land.

NOTE 7 – INTEREST-BEARING DEPOSITS

Interest-bearing deposits consisted of the following:

	DECEMBER 31, 2013	DECEMBER 31, 2012
Savings	$ 2,379,102	$ 2,155,885
Money market	37,798,259	36,730,548
NOW accounts	4,541,648	4,921,878
Time, under $100,000	4,957,720	4,552,034
Time, $100,000 or more	48,453,546	21,493,521
	$ 98,130,275	$ 69,853,866

NOTE 7 – INTEREST-BEARING DEPOSITS (CONTINUED)

Aggregate annual maturities of time deposits are as follows:

Years ending December 31,	
2014	$ 39,318,153
2015	11,011,977
2016	2,440,822
2017	278,219
2018	362,095
	$ 53,411,266

Interest expense related to interest-bearing deposits consisted of the following:

	YEAR ENDED DECEMBER 31,	
	2013	2012
Savings	$ 1,140	$ 1,062
Money market	119,303	151,088
NOW accounts	2,336	3,685
Time, under $100,000	18,714	31,786
Time, $100,000 or more	203,067	93,049
	$ 344,560	$ 280,670

The Bank, in the normal course of business, receives deposits from its directors, officers, principal shareholders, and their associates. In management's opinion, these transactions are on substantially the same terms as comparable transactions with other customers of the Bank. The aggregate amount of deposits received from related parties at December 31, 2013 and 2012 was $676,269 and $819,578, respectively.

NOTE 8 – FHLB ADVANCES AND OTHER BORROWINGS

FHLB advances – During 2006, the Bank entered into an arrangement with the FHLB under which it may borrow, on either a short-term or long-term basis, up to 25% of its assets provided that adequate collateral has been pledged. Investment securities with amortized costs totaling $3,500,000 and $2,000,000 and estimated fair market values totaling $3,438,582and $2,057,970 were pledged at December 31, 2013 and 2012, respectively.

The Bank had four and six outstanding secured advances from the FHLB at December 31, 2013 and 2012, respectively, with fixed interest rates ranging from 2.84% to 3.56% and maturity dates ranging from June 2014 to September 2014.

NOTE 8 – FHLB ADVANCES AND OTHER BORROWINGS (CONTINUED)

Lines of credit – The Bank had two unsecured available lines of credit with two of its correspondent banks totaling $6,500,000 and $5,500,000 as of December 31, 2013 and 2012, respectively. There were $945,000 and $0 borrowings outstanding under these arrangements at December 31, 2013 and 2012, respectively. Investment securities with amortized costs totaling $3,500,000 and $2,000,000 and estimated fair values totaling $3,441,910 and $2,058,380 were pledged to collateralize the secured lines of credit at December 31, 2013 and 2012, respectively. The interest rate on these lines of credit is tied to the federal funds rate and was 0.25% at December 31, 2013 and 2012. The Bank has blanket lien financing availability at the FHLB totaling $19,765,200 and $19,711,000 as of December 31, 2013 and 2012, respectively. Additionally, the Bank had collateral borrowing capacity at the FHLB totaling $11,995,006 and $11,373,771 as of December 31, 2013 and 2012, respectively. The Bank had outstanding borrowings from the FHLB totaling $4,000,000 and $7,000,000 as of December 31, 2013 and 2012, respectively.

NOTE 9 – INCOME TAXES

Income tax (benefit) expense for the years ended December 31, 2013 and 2012 consists of the following:

	YEARS ENDED DECEMBER 31,	
	2013	2012
Current		
Federal	$ -	$ -
State	800	800
	800	800
Deferred		
Federal	402,000	540,000
State	149,000	88,000
	551,000	628,000
Change in valuation allowance	(1,351,000)	(628,000)
Income tax (benefit) expense	$ (799,200)	$ 800

The provision for income tax expense differs from amounts computed by applying the statutory federal income tax rate to income before income taxes primarily due to the valuation allowance.

NOTE 9 – INCOME TAXES (CONTINUED)

Deferred tax assets (liabilities) are comprised of the following:

	DECEMBER 31, 2013	DECEMBER 31, 2012
Deferred tax assets		
Net operating loss carryforwards	$ 534,000	$ 1,054,000
Interest on non-accrual loans	65,000	103,000
Write-down on foreclosed real estate	195,000	243,000
Allowance for loan losses	457,000	411,000
Unrealized gain on available for sale investment securities	-	42,000
Other	196,000	188,000
Total deferred tax assets	1,447,000	2,041,000
Deferred tax liabilities		
Federal enterprise award grants	(99,000)	(198,000)
Depreciation on premises and equipment	(91,000)	(3,000)
Unrealized gains on available for sale investment securities	(41,000)	-
Other	(29,000)	(20,000)
	(260,000)	(221,000)
Valuation allowance	(387,800)	(1,820,000)
Net deferred income tax asset	$ 799,200	$ -

Accounting Standards Codification 740 requires that the tax benefit of net operating losses, temporary differences, and credit carryforwards be recorded as an asset to the extent that management assesses that realization is "more likely than not." Realization of the future tax benefits is dependent on the Bank's ability to generate sufficient taxable income within the carryforward period. During the year ended December 31, 2013, the valuation allowance decreased by approximately $1,351,000.

As of December 31, 2013 and 2012, the Bank has federal net operating loss carryforwards (NOLs) totaling approximately $926,342 and $2,273,121, respectively. Additionally, at December 31, 2013 and 2012, the Bank has state net operating loss carryforwards of approximately $3,056,256 and $4,271,243, respectively. Approximately $840,242 of the federal NOLs expire between 2018 and 2024, and approximately $86,100 expire in 2031. Approximately $643,869 of the state NOLs expire between 2014 and 2019, approximately $1,256,404 in state NOLs expire in 2029, and approximately $1,155,983 expire in 2031. The Tax Reform Act of 1986 and the California Conformity Act of 1987 imposes substantial restrictions on the utilization of net operating loss carryforwards when an "ownership change," as defined in the Internal Revenue Code, has occurred. Some of the Bank's federal and state net operating losses have each been limited to usage of approximately $71,500 annually due to ownership changes.

NOTE 10 – COMMITMENTS AND CONTINGENCIES

Lease commitments – The Bank leases certain facilities where it conducts its operations on a month-to-month basis. The Bank has entered into two term leases for its Danville and Oakland locations. The Bank is responsible for common area maintenance, taxes, and insurance to the extent they exceed the base year amounts. The leases expire on October 31, 2017 and on December 31, 2018, respectively.

At December 31, 2013, the future lease rental payable under non-cancellable operating lease commitments for the Bank's Danville and Oakland locations were as follows:

2014	$ 126,477
2015	282,218
2016	290,055
2017	299,760
2018	292,542
Thereafter	216,053
	$ 1,507,105

The minimum rental payments shown above are given for the existing lease obligations and are not a forecast of future rental expense. The Bank recognized rent expense of $418,223 and $200,151 for the years ended December 31, 2013 and 2012, respectively.

Financial instruments with off-balance-sheet risk – The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business in order to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments consist of commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheets.

The Bank's exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and standby letters of credit as it does for loans included on the balance sheets.

At December 31, 2013 and 2012, the Bank had commitments to extend credit of approximately $25,150,680 and $14,899,905, respectively. There were $2,152,375 and $2,272,000 in standby letters of credit issued at December 31, 2013 and 2012, respectively.

NOTE 10 – COMMITMENTS AND CONTINGENCIES (CONTINUED)

Financial instruments with off-balance-sheet risk (continued) – Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some 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 deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, and deeds of trust on residential real estate and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance or financial obligation of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers.

Contingencies – The Bank is subject to legal proceedings and claims that arise in the ordinary course of business. In the opinion of management, the amount of ultimate liability with respect to such actions will not materially affect the financial position or results of operations of the Bank.

NOTE 11 – SHAREHOLDERS' EQUITY

Preferred stock – In January 2009, the Bank issued 1,747 shares of Series A, fixed rate non-cumulative perpetual preferred stock to the U.S. Treasury as part of the Treasury's Capital Purchase Program (CPP). The non-cumulative preferred stock is carried at liquidation value of $1,000 per share and must be redeemed after ten years and carries a fixed dividend rate of 5% with dividends payable quarterly. In September 2010, the Bank redeemed 1,747 shares of Series A preferred stock and issued 4,060 shares of Series A-1, fixed rate non-cumulative preferred stock issued as part of the Treasury's Community Development Capital Initiative (CDCI). The newly issued shares carry an initial fixed dividend rate of 2% increasing to 9% after eight years, with dividends payable quarterly. The Bank paid dividends totaling $81,200 and $60,900 during the years ending December 31, 2013 and 2012, respectively, after receiving approval from the Department of Financial Institutions (DFI) and their shareholders.

Dividend restrictions – Upon declaration by the Board of Directors, all shareholders of record will be entitled to receive dividends. The California Financial Code provides that, unless the Bank receives prior approval from the California Commissioner of Financial Institutions, the total amount of dividend payments a California state-chartered bank can make in any calendar year cannot exceed the lesser of: (1) the Bank's retained earnings, or (2) the Bank's net income for its last three fiscal years, less distributions made to shareholders during the same three-year period. At December 31, 2013 and 2012, the Bank had an accumulated deficit. Therefore, no amount is available for dividends to shareholders. As discussed above, the Bank received approval from the DFI and their shareholders to make dividend payments on the Series A-1 and Series A preferred stock during 2013 and 2012.

NOTE 11 – SHAREHOLDERS' EQUITY (CONTINUED)

Earnings (loss) per share – Earnings (loss) per share (EPS) is calculated based on the weighted average common shares outstanding during the period. Basic EPS excludes dilution and is calculated by dividing net income available to common shareholders by the weighted average common shares outstanding. 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. There was no dilutive effect of stock options in 2012.

	YEAR ENDED DECEMBER 31, 2013		
	Income (Numerator)	Shares (Denominator)	Per-Share Amount
Basic EPS:			
Net income available to common shareholders	$ 1,955,184	4,131,924	$ 0.47
Effect of dilutive securities:			
Stock options	-	27,255	
Diluted EPS:			
Net income available to common shareholders plus assumed conversions	$ 1,955,184	4,159,179	$ 0.47

	YEAR ENDED DECEMBER 31, 2012		
	Income (Numerator)	Shares (Denominator)	Per-Share Amount
Basic EPS:			
Net income available to common shareholders	$ 1,325,170	4,172,268	$ 0.32
Effect of dilutive securities:			
Stock options	-	-	
Diluted EPS:			
Net income available to common shareholders plus assumed conversions	$ 1,325,170	4,172,268	$ 0.32

NOTE 11 – SHAREHOLDERS' EQUITY (CONTINUED)

Stock option plan – The Bank's 2001 Stock Option Plan expired during 2011. The Bank has option grants still outstanding under that Plan. During 2012, the Board of Directors and shareholders approved the adoption of the Community Bank of the Bay 2012 Stock Option Plan. The plan includes both non-statutory stock options, which may be granted to directors, employees, and consultants, and incentive stock options, which may be granted to employees. The price of non-statutory and incentive stock options may not be less than 100%, respectively, of the fair market value of the common stock on the date of the grant.

However, if an individual at the time of the grant owns stock representing more than 10% of the voting rights of all classes of the stock, then the price of the stock options may not be less than 110% of the fair market value of the common stock on the date of the grant. The term of stock options is determined by the Board of Directors, but may not exceed ten years from the date of the grant unless, in the case of an incentive stock option, an individual at the time of grant owns stock representing more than 10% of the voting rights of all classes of the stock, then the maximum term is five years. As of December 31, 2013, $1,221,476 shares of the Bank's common stock are reserved under this plan.

The fair value of each option granted is estimated on the date of grant using the Black-Scholes options-pricing model with the following weighted-average assumptions used for grants in 2013 and 2012, respectively: no expected dividends; expected volatility between 71.29% and 72.16% in 2013 and 76.16% in 2012; risk-free interest rates between 2.51% and 2.72% in 2013 and 0.96% in 2012; and expected options term of ten years.

The following table summarizes information about stock options outstanding at December 31, 2013:

	Shares	Weighted Average Exercise Price
Outstanding at beginning of period	904,088	$ 3.40
Granted	147,500	$ 3.83
Exercised	(16,500)	$ 3.48
Forfeited / canceled	(127,221)	$ 3.45
Expired	(33,670)	$ 3.75
Outstanding at end of period	874,197	$ 3.44

NOTE 11 – SHAREHOLDERS' EQUITY (CONTINUED)

Stock option plan (continued) – The Bank recognized $396,455 and $329,672 in stock option expense for the years ended December 31, 2013 and 2012, respectively. There is approximately $360,313 in unrecognized compensation cost remaining as of December 31, 2013, which is expected to be recognized over a weighted-average period of 3.96 years. The Bank had 474,360 incentive stock options and 399,837 non-statutory stock options outstanding as of December 31, 2013. The Bank had 492,283 incentive stock options and 411,805 non-statutory stock options outstanding as of December 31, 2012.

A summary of options outstanding follows:

	DECEMBER 31,	
	2013	2012
Weighted-average fair value of options granted during the year	$ 3.83	$ 1.94
Intrinsic value of options exercised	$ -	$ -
Options exercisable at year end	631,640	430,131
Weighted-average exercise price	$ 3.48	$ 3.57
Intrinsic value	$ 614,620	$ 23,959
Weighted-average remaining contractual life	6.46 Years	6.68 Years
Options outstanding at year end	874,197	904,088
Weighted-average exercise price	$ 3.44	$ 3.40
Intrinsic value	$ 873,207	$ 49,772
Weighted-average remaining contractual life	7.34 Years	8.00 Years

NOTE 12 – REGULATORY MATTERS

The Bank is subject to various regulatory capital requirements administered by the FDIC. Failure to meet these 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.

NOTE 12– REGULATORY MATTERS (CONTINUED)

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios of total and Tier I capital to risk-weighted assets, and of Tier I capital to average assets. Each of these components is defined in the regulations. Management believes that the Bank met all capital adequacy requirements as of December 31, 2013 and 2012.

To be categorized as well-capitalized, the Bank must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the following table.

	Actual		For Capital Adequacy Purposes		To be well Capitalized under PCA	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2013:						
Total risk-based capital						
(to risk-weighted assets)	$ 20,745,000	15.41%	$ 10,773,000	≥ 0.0%	$ 13,466,000	≥ 0.0%
Tier I capital						
(to risk-weighted assets)	$ 19,052,000	14.15%	$ 5,386,000	≥ 0.0%	$ 8,080,000	≥ 0.0%
Tier I capital						
(to average assets)	$ 19,052,000	10.78%	$ 7,072,000	≥ 0.0%	$ 8,840,000	≥ 0.0%
December 31, 2012:						
Total risk-based capital						
(to risk-weighted assets)	$ 18,039,000	16.71%	$ 8,637,000	≥ 8.0%	$ 10,796,000	≥ 10.0%
Tier I capital						
(to risk-weighted assets)	$ 16,682,000	15.45%	$ 4,318,000	≥ 4.0%	$ 6,478,000	≥ 6.0%
Tier I capital						
(to average assets)	$ 16,682,000	11.30%	$ 5,906,000	≥ 4.0%	$ 7,383,000	≥ 5.0%

NOTE 13 – GOVERNMENT GRANT

In 2013 and 2012, the Bank was awarded $323,000 and $415,000, respectively, by the United States Treasury Department in recognition of its community development activities under the Bank Enterprise Award Program (the BEA). Management believes that the Bank has complied, in all material aspects, with all of the covenants and requirements under the BEA agreement and that it is not, and has not been, in default with any of the terms, requirements, or minimum levels of qualified activities of such agreement.

NOTE 14 – OTHER EXPENSES

Other expenses consisted of the following:

	DECEMBER 31, 2013	DECEMBER 31, 2012
Professional fees	$ 524,518	$ 511,622
Advertising	65,594	49,439
Data processing	402,205	312,936
Regulatory assessments	242,445	197,452
Insurance	69,893	59,430
Other operating expenses	661,412	795,951
Total	$ 1,966,067	$ 1,926,830

NOTE 15 – BENEFIT PLAN AND SALARY CONTINUATION AGREEMENT

Defined contribution plan – The Bank adopted a 401(k) defined contribution plan effective January 1, 1997. All employees of the Bank may participate in the plan upon completion of certain eligibility requirements. The Bank matches employee's contributions on a discretionary basis. There were no discretionary contributions for the years ended December 31, 2013 and 2012.

Salary continuation agreement – In 2006, the Bank adopted a salary continuation agreement to provide retirement benefits for a key executive. This agreement was amended as of December 31, 2008 and terminated during 2012. The estimated present value of these benefits was accrued as an expense from the inception date of the agreement until the termination of the agreement. No expense was recognized under this agreement for the years ended December 31, 2013 and 2012. During 2012, as a result of the termination of the agreement, the accrued liability was reversed and the Bank recorded $656,053 as other income.

NOTE 16 – DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair values of financial instruments are management's estimates of the values at which instruments could be exchanged in a transaction between willing parties. These estimates are subjective and may vary significantly from amounts that would be realized in actual transactions. Further, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on the fair value estimates and have not been considered in any of these estimates. The following table presents estimated fair values of the Bank's financial instruments as of December 31, 2013 and 2012.

The estimated fair values of the Bank's financial instruments are approximately as follows:

	2013			2012	
	Fair Value Hierarchy	Carrying Amounts	Estimated Fair Values	Carrying Amounts	Estimated Fair Values
Financial assets:					
Cash and cash equivalents	Level 1	$ 22,800,028	$ 22,800,028	$ 27,960,544	$ 27,960,544
Interest bearing deposits in banks	Level 2	10,169,744	10,183,624	4,672,748	4,672,748
Securities available for sale	Level 2	9,479,124	9,479,124	8,526,868	8,526,868
FHLB stock	Level 2	580,100	580,100	475,000	475,000
Loans, net	Level 3	125,344,245	129,237,000	107,646,338	109,952,000
Interest receivable	Level 2	423,618	423,618	393,923	393,923
Financial liabilities:					
Non-maturity deposits	Level 2	97,177,897	97,177,897	104,909,215	104,909,215
Time deposits	Level 2	53,411,266	53,677,000	26,045,555	26,119,000
FHLB borrowings	Level 2	4,000,000	4,054,000	7,000,000	7,120,000
Interest payable	Level 2	29,433	29,433	16,253	16,253
Off-balance-sheet liabilities:					
Undisbursed loan commitments	Level 3	-	252,000	-	145,000

The Bank utilizes fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. The Bank groups assets and liabilities at fair value in a three-level valuation hierarchy for disclosure of fair value measurement. The valuation hierarchy is based on the transparency of inputs to the valuation of an asset or liability as of the measurement date.

In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Bank has the ability to access. Fair values determined by Level 2 inputs utilize inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability.

NOTE 16 – DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Bank's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability. Some fair value measurements, such as available-for-sale securities, are performed on a recurring basis, while others such as other real estate owned and impaired loans are performed on a non-recurring basis.

The following table presents information about the Bank's assets and liabilities measured at fair value on a recurring basis as of December 31, 2013 and 2012, as well as assets and liabilities for which a non-recurring change in the fair value has been recorded as of December 31, 2013 and 2012. The table indicates the fair value hierarchy of the valuation techniques utilized by the Bank to determine such fair value.

Description of Assets	December 31, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale securities:				
Municipal securities (taxable)	$ 1,158,884	$ -	$ 1,158,884	$ -
Municipal securities (non-taxable)	$ 500,055	-	500,055	-
Agency	466,755	-	466,755	-
Mortgage-backed securities	2,977,506	-	2,977,506	-
CMOs	2,273,579	-	2,273,579	-
Corporates	657,950	-	657,950	-
U.S. Treasury	1,444,395	-	1,444,395	-
Impaired loans [1]	824,233	-	-	824,233
Total	$ 10,303,357	$ -	$ 9,479,124	$ 824,233

[1] Non-recurring item

Description of Assets	December 31, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale securities:				
Municipal securities (taxable)	$ 1,501,473	$ -	$ 1,501,473	$ -
Agency	498,050	-	498,050	-
Mortgage-backed securities	2,889,875	-	2,889,875	-
CMOs	2,608,800	-	2,608,800	-
U.S.Treasury	1,028,670	-	1,028,670	-
Impaired loans [1]	1,467,502	-	-	1,467,502
Other real estate owned [1]	80,569	-	-	80,569
Other foreclosed assets [1]	258,500	-	-	258,500
Total	$ 10,333,439	$ -	$ 8,526,868	$ 1,806,571

[1] Non-recurring item

NOTE 16 – DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Transfers between levels in the fair value hierarchy are recognized on the actual date of the event or circumstances that caused the transfer, which generally corresponds to the Bank's quarterly valuation process.

Fair value measurements for impaired loans are based on either collateral values supported by appraisals or observed market prices. Any loss recognized on impaired loans is not recorded directly as an adjustment to current earnings but rather as an adjustment component in determining the overall adequacy of the allowance for loan losses. Such adjustments to the estimated fair value of impaired loans may result in increases or decreases to the provision for loan losses recorded in current earnings.

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practicable to estimate that value:

Cash and cash equivalents – For short-term instruments, including cash and due from banks, the carrying amount is a reasonable estimate of fair value.

Interest-bearing deposits in banks – Represent time deposits held at other financial institutions. The fair values are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities.

Securities – Fair values for investment securities are based on quoted market prices when available or through the use of alternative approaches, such as a matrix or model pricing, when market quotes are not readily accessible or available.

FHLB stock and other investments – For FHLB stock and other investments, the carrying amount is a reasonable estimate of fair value.

Loans – For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. The fair values for fixed rate loans are estimated using discounted cash flow analysis, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. The carrying amount of interest receivable approximates its fair value. The Bank's allowance for loan and lease losses is a reasonable estimate of the valuation allowance needed to adjust computed fair values for the quality of certain loans in the portfolio.

Interest receivable and payable – For interest receivable and payable, the carrying amount is estimated to be the fair value.

Impaired loans – The Bank utilizes current appraisals and applies discount factors estimated and modeled for consistency by management to arrive at the estimate of fair value for all collateral dependent loans.

NOTE 16 – DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Other real estate owned – The Bank utilizes current appraisals discounted for estimated selling costs to arrive at the estimate of fair value for all other real estate owned.

Deposit liabilities – The fair values disclosed for non-maturity deposits (e.g., interest and non-interest checking, statement savings, and money market accounts) are, by definition, equal to the amount payable at the reporting date (i.e., their carrying amounts). The fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits. The carrying amount of interest payable approximates its fair value.

FHLB borrowings – The fair value of the borrowings is calculated based on the discounted value of the contractual cash flows using current rates at which such borrowings can currently be obtained.

Secured borrowings – The fair value approximates book value as they represent short-term borrowings connected to the sale of loans.

Commitments to extend credit – The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates.

Limitations – Fair value estimates are made at a specific point in time, based on relevant market information and other 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 Bank's entire holdings of a particular financial instrument.

NOTE 17 – SUMMARY OF QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

The following table sets forth summarized data for the year pertaining to each quarter for 2013 and is unaudited:

	2013 Quarter Ended			
	December 31	September 30	June 30	March 31
Total assets	$ 175,372,787	$ 173,326,356	$ 170,458,407	$ 163,204,245
Gross loans	126,345,571	128,984,037	119,114,415	111,128,669
Deposits	150,589,163	150,531,905	148,165,332	139,129,589
Net interest income	1,648,825	1,813,646	1,608,030	1,562,859
Net income	478,991	381,331	333,443	842,619

NOTE 18 – SUBSEQUENT EVENTS

The Bank has evaluated the effects of subsequent events that have occurred after the period ending December 31, 2013 and through April 11, 2014, which is the date the financial statements were issued.

Board of Directors

William E. Purcell
Chairman, Board of Directors
President, Purcell International

Eddie C. Cheung, M.D., FACG
Clinical Professor of Internal Medicine
& Gastroenterology/Hepatology

Tracey A. Enfantino
General Manager, Environmental Systems

Raymond J. Figone
Owner, Figone Materials Inc.

John J. Hounslow
Retired Bank Executive

Gunter M. Unruh
Vice Chairman, Board of Directors Executive
President, Metric Design & Manufacturing, Inc.

William S. Keller
President & CEO, Community Bank of the Bay

Dimitri V. Koroslev
President, Bay Business Credit

James A. Mayer
Retired Banker

Frank Tsai
Partner, FLG Partners, LLC

Management & Officers

William S. Keller
President & CEO

Michael A. Skubic
President, East Bay Region

Wilbur E. Hobbs, Jr.
SVP, Chief Lending Officer

William X. Smith
SVP, Chief Risk Officer

Jenny Boister
SVP & Manager, Credit Services

David Meyer
SVP, Danville Team Leader

Daniel Fujimoto
VP, Business Development

Chaula M. Pandya
SVP, Chief Financial Officer

Mark Roach
SVP, Silicon Valley Regional Manager

George T. Harrison
SVP, Chief Credit Officer

Margie Perry
SVP, Operations

Rudolph Garcia
SVP & Manager, SBA Lending

Judy Conde
VP, Compliance

Romeo Luz
VP, Business Development

Oakland Office
180 Grand Avenue
Oakland, CA 94612
(510) 433-5400

Danville Office
390 Railroad Avenue
Danville, CA 94526
(925) 838-2902

San Jose Office
50 W. San Fernando Street, 350
San Jose, CA 95113
(408) 298-4900

San Mateo Office
155 Bovet, Suite 150
San Mateo, CA 94402
(650) 389-1010

www.bankcbb.com
Stock Symbol: CBYAA