

# TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY

Consolidated Financial Statements

December 31, 2018 and 2017  
(with Independent Auditor's Report thereon)



## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Stockholders  
Touchmark Bancshares, Inc. and subsidiary  
Alpharetta, Georgia

### Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Touchmark Bancshares, Inc. and subsidiary (the "Company"), which comprise the consolidated balance sheets as of December 31, 2018 and 2017, the related consolidated statements of earnings, comprehensive income, changes in stockholders' equity and cash flows for the years then ended, and the related notes to the consolidated financial statements (collectively, 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

We believe the audit evidence we have 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 Touchmark Bancshares, Inc. and subsidiary as of December 31, 2018 and 2017, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Porter Keadle Moore, LLC*

Atlanta, Georgia  
March 26, 2019

## TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY

## Consolidated Balance Sheets

December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
<b><u>ASSETS</u></b>		
Cash and due from banks	\$ 13,657,277	2,438,577
Federal funds sold	4,300,000	3,742,085
Cash and cash equivalents	17,957,277	6,180,662
Interest-bearing accounts with other banks	5,859,876	1,368,556
Securities available-for-sale	18,861,069	21,526,587
Restricted stock	2,494,600	2,561,400
Loans, net	353,954,340	346,746,535
Premises and equipment, net	1,474,058	1,481,117
Other assets	4,174,468	3,246,250
Total assets	\$ <u>404,775,688</u>	<u>383,111,107</u>
<b><u>LIABILITIES AND STOCKHOLDERS' EQUITY</u></b>		
Liabilities:		
Deposits:		
Non-interest bearing demand	\$ 19,324,082	24,634,285
Interest bearing	312,422,406	283,527,387
Total deposits	331,746,488	308,161,672
Federal Home Loan Bank advances	20,500,000	27,500,000
Other liabilities	3,137,545	2,098,279
Total liabilities	<u>355,384,033</u>	<u>337,759,951</u>
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, no par value, 10,000,000 shares authorized, none issued	-	-
Common stock, \$.01 par value, 50,000,000 shares authorized, 4,475,891 and 4,468,391 issued and outstanding, respectively	44,759	44,684
Additional paid-in capital	46,676,476	46,426,170
Retained earnings (accumulated deficit)	3,098,492	(920,643)
Accumulated other comprehensive loss	(428,072)	(199,055)
Total stockholders' equity	<u>49,391,655</u>	<u>45,351,156</u>
Total liabilities and stockholders' equity	\$ <u>404,775,688</u>	<u>383,111,107</u>

See accompanying notes to consolidated financial statements

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Consolidated Statements of Earnings  
For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Interest income:		
Loans, including fees	\$ 16,975,930	13,813,718
Taxable investments	651,123	560,572
Non-taxable investments	33,800	34,389
Federal funds sold	76,803	50,873
Other	<u>143,630</u>	<u>104,082</u>
Total interest income	<u>17,881,286</u>	<u>14,563,634</u>
Interest expense:		
Deposits	5,147,241	2,877,658
Federal Home Loan Bank advances	461,627	342,429
Federal funds purchased	<u>719</u>	<u>8,422</u>
Total interest expense	<u>5,609,587</u>	<u>3,228,509</u>
Net interest income	12,271,699	11,335,125
Provision for loan losses	<u>100,000</u>	<u>1,825,000</u>
Net interest income after provision for loan losses	<u>12,171,699</u>	<u>9,510,125</u>
Noninterest income:		
Service charges on deposit accounts and other fees	32,703	44,214
Gain on sale of government guaranteed loans	1,975,270	2,202,703
Loan servicing fees	620,202	550,890
Other noninterest income	<u>107,042</u>	<u>119,312</u>
Total noninterest income	<u>2,735,217</u>	<u>2,917,119</u>
Noninterest expense:		
Salaries and employee benefits	3,961,746	4,181,330
Occupancy and equipment	314,226	333,362
Referral fees for government guaranteed loans	978,617	1,177,803
Other operating expense	<u>2,499,675</u>	<u>2,558,250</u>
Total noninterest expense	<u>7,754,264</u>	<u>8,250,745</u>
Earnings before income taxes	7,152,652	4,176,499
Income tax expense	<u>1,790,750</u>	<u>2,305,570</u>
Net earnings	<u>\$ 5,361,902</u>	<u>1,870,929</u>

See accompanying notes to consolidated financial statements.

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
 Consolidated Statements of Comprehensive Income  
 For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Net earnings	\$ <u>5,361,902</u>	<u>1,870,929</u>
Other comprehensive (loss)/income:		
Unrealized (losses)/gains on investment securities available-for-sale arising during the period, net of taxes of \$53,201 and \$10,459	<u>(229,017)</u>	<u>21,293</u>
Total other comprehensive (loss)/income	<u>(229,017)</u>	<u>21,293</u>
Comprehensive income	<u>\$ 5,132,885</u>	<u>1,892,222</u>

See accompanying notes to consolidated financial statements.

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Consolidated Statements of Changes in Stockholders' Equity  
For the Years Ended December 31, 2018 and 2017

	Outstanding Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance, December 31, 2016	3,465,391	\$ 34,654	36,260,695	(2,055,331)	(196,963)	34,043,055
Dividends declared on common shares (\$.17 per share)	-	-	-	(759,626)	-	(759,626)
Issuance of common stock, net issuance costs of \$50,485	1,003,000	10,030	10,019,635	-	-	10,029,665
Stock based compensation expense	-	-	145,840	-	-	145,840
Net earnings	-	-	-	1,870,929	-	1,870,929
Reclassification adjustment for tax rate change	-	-	-	23,385	(23,385)	-
Change in unrealized gain/loss on securities available-for-sale	-	-	-	-	21,293	21,293
Balance, December 31, 2017	4,468,391	44,684	46,426,170	(920,643)	(199,055)	45,351,156
Dividends declared on common shares (\$.30 per share)	-	-	-	(1,342,767)	-	(1,342,767)
Issuance of common stock	7,500	75	75,300	-	-	75,375
Stock based compensation expense	-	-	175,006	-	-	175,006
Net earnings	-	-	-	5,361,902	-	5,361,902
Change in unrealized gain/loss on securities available-for-sale	-	-	-	-	(229,017)	(229,017)
Balance, December 31, 2018	<u>4,475,891</u>	<u>\$ 44,759</u>	<u>46,676,476</u>	<u>3,098,492</u>	<u>(428,072)</u>	<u>49,391,655</u>

See accompanying notes to consolidated financial statements.

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Consolidated Statements of Cash Flows  
For the Years Ended December 31, 2018 and 2017

	2018	2017
Cash flows from operating activities:		
Net earnings	\$ 5,361,902	1,870,929
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation, amortization and accretion	2,478,749	1,248,920
Provision for loan losses	100,000	1,825,000
Deferred income tax expense	40,314	520,214
Stock-based compensation expense	175,006	145,840
Change in:		
Other assets	(1,066,252)	(315,550)
Other liabilities	456,125	(402,906)
Net cash provided by operating activities	7,545,844	4,892,447
Cash flows from investing activities:		
Change in interest bearing accounts at other banks	(4,491,320)	1,104,677
Proceeds from paydowns, calls and maturities of securities available-for-sale	3,268,188	4,052,349
Purchases of securities available-for-sale	(1,001,701)	(995,537)
Proceeds from sale of restricted stock	297,500	531,400
Purchase of restricted stock	(230,700)	(1,133,050)
Purchase of loans	(4,106,637)	(110,307,910)
Increase in loans, net	(5,294,033)	(16,906,652)
Purchases of premises and equipment	(111,091)	(20,688)
Net cash used in investing activities	(11,669,794)	(123,675,411)
Cash flows from financing activities:		
Change in deposits	23,584,816	87,222,130
Sale of common stock	75,375	10,080,150
Stock issuance costs	-	(50,485)
Payment of dividend on common stock	(759,626)	(519,809)
Proceeds from Federal Home Loan Bank advances	20,500,000	22,000,000
Repayment of Federal Home Loan Bank advances	(27,500,000)	(14,250,000)
Net cash provided by financing activities	15,900,565	104,481,986
Net change in cash and cash equivalents	11,776,615	(14,300,978)
Cash and cash equivalents at beginning of the year	6,180,662	20,481,640
Cash and cash equivalents at end of the year	\$ 17,957,277	6,180,662
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest	\$ 5,458,092	3,168,787
Taxes	\$ 1,737,750	1,814,124
Non-cash investing and financing activities:		
Change in dividends payable	\$ 583,141	239,817
Change in unrealized gain/loss on securities available-for-sale, net of tax	\$ (229,017)	21,293

See accompanying notes to consolidated financial statements.

**(1) Summary of Significant Accounting Policies**

The accounting and reporting policies of Touchmark Bancshares, Inc. (the "Company") conform to accounting principles generally accepted in the United States of America and with general practices within the banking industry. The following is a description of the more significant of those policies that the Company follows in preparing and presenting its financial statements.

**Reporting Entity and Nature of Operations**

The Company is a Georgia corporation and was established on April 3, 2007 for the purpose of organizing and managing Touchmark National Bank (the "Bank"). The Company is a one-bank holding company with respect to its subsidiary, Touchmark National Bank. The Bank was opened with the purpose of serving as a community bank. The Bank's service area includes the counties of North Fulton, Gwinnett, DeKalb, Cobb and Forsyth in metropolitan Atlanta, Georgia. On May 10, 2016, the Company was granted approval from the Federal Reserve Bank to become a financial holding company.

**Principles of Consolidation**

The consolidated financial statements include the accounts of the Company and the Bank. All significant intercompany accounts and transactions have been eliminated.

**Use of Estimates in the Preparation of Financial Statements**

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

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for losses on loans, fair market value of securities and financial instruments, the valuation of deferred tax assets, and the disclosure of contingent assets and liabilities.

Management believes the allowance for losses on loans is adequate. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in local economic conditions.

**Subsequent Events**

Management has evaluated subsequent events for potential recognition or disclosure in the financial statements through March 26, 2019, the date on which the financial statements were available to be issued.

**Reclassifications**

Certain 2017 amounts have been reclassified to conform to the presentation used in 2018. These reclassifications had no effect on the operations, financial condition or cash flows of the Company.

**Cash and Cash Equivalents**

Cash and cash equivalents include cash, due from banks and federal funds sold. Cash flows from deposits, federal funds purchased and originations and collections of loans are reported net. The Bank is required to maintain reserve balances in cash or on deposit with the Federal Reserve Bank based on a percentage of deposits. The required reserve balance at December 31, 2018 and 2017 was \$254,000 and \$970,000, respectively.

**Investment Securities**

The Company classifies its securities in one of three categories: trading, available-for-sale, or held to maturity. Trading securities are bought and held principally for the purpose of selling them in the near term. Held to maturity securities are those securities for which the Company has the ability and intent to hold the security until maturity. All other securities not included in trading or held to maturity are classified as available-for-sale. At December 31, 2018 and 2017, all securities were classified as available-for-sale.

Available-for-sale securities are recorded at fair value. Unrealized holding gains and losses, net of the related tax effect, on securities available-for-sale are excluded from earnings and are reported as a separate component of stockholders' equity until realized. Transfers of securities between categories are recorded at fair value at the date of transfer.



(1) **Summary of Significant Accounting Policies, continued**  
**Investment Securities, continued**

Purchase premiums and discounts are recognized in interest income using methods approximating the interest method over the terms of the securities. A decline in the market value of any security below cost that is deemed other than temporary results in a charge to earnings and the establishment of a new cost basis for the security. Realized gains and losses for securities are included in earnings and are derived using the specific identification method for determining the amortized cost of securities sold as of the trade date.

**Restricted Stock**

Restricted stock consists of Federal Reserve Bank and Federal Home Loan Bank of Atlanta (FHLB) stock which represents an equity interest in these entities and is recorded at cost. These stocks do not have a readily determinable fair value because ownership is restricted and lacks a market.

Management has evaluated its holdings in FHLB and Federal Reserve Bank stock and determined par value is ultimately recoverable and therefore determined that FHLB and Federal Reserve Bank stock was not other-than-temporarily impaired. In addition, the Bank has ample liquidity and does not require redemption of its restricted stock holdings in the foreseeable future.

**Loans**

Loans receivable are loans which management has the intent and ability to hold for the foreseeable future or until maturity or pay-off. Loans receivable are reported at their outstanding principal, adjusted for any charge-offs, the allowance for loan losses, deferred fees or costs on originated loans and unamortized premiums or discounts on purchased loans. The Company also purchases loans. The related purchase price premium or discount is amortized or accreted to earnings as a yield adjustment over the estimated life of the loans.

Interest on loans is credited to income on a daily basis based upon the principal amount outstanding. Loan origination costs are recognized as an expense at the time the loan is originated. Loan origination fees up to the origination cost amount are recognized in earnings at the time the loan is originated. Loan origination fees in excess of origination costs are deferred and recognized as an adjustment of the yield of the related loan.

The accrual of interest on loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due. When interest accrual is discontinued, all unpaid accrued interest is reversed, unless management believes that the accrued interest is recoverable through the liquidation of collateral. Interest income is subsequently recognized only to the extent cash payments are received. Loans are returned to accrual status when all the principal and interest amounts contractually due are reasonably assured of repayment within a reasonable time frame.

Loan delinquencies are determined by comparing contractual requirements to the timing of payments received from the borrower. The policies and procedures related to nonaccrual and delinquent loans are applied to all outstanding loans.

**(1) Summary of Significant Accounting Policies, continued**  
**Allowance for Loan Losses**

The allowance for loan losses is increased by provision charges to income and decreased by charge-offs (net of recoveries). Loans are charged against the allowance for loan losses when management believes the collection of the principal is unlikely. The allowance for loan losses is maintained at a level believed adequate by management to absorb estimated probable inherent loan losses and estimated losses relating to specifically identified loans. Management's periodic evaluation of the adequacy of the allowance is based on the Company's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay (including the timing of payments), the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions, and other relevant factors. This evaluation is inherently subjective as it requires material estimates that are susceptible to significant change including the amounts and timing of future cash flows expected to be received on impaired loans.

While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in local economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for losses on loans. Such agencies may require the Company to recognize additions to the allowance based on their judgment about information available to them at the time of their examination. Because of these factors, it is reasonably possible that the allowance for losses on loans may change materially in the near term. However, the amount of the change that is reasonably possible cannot be estimated.

The allowance for loan losses may consist of specific, general, and unallocated components. The specific component relates to loans that are classified as impaired. For loans that are classified as impaired, an allowance is established when the collateral value less selling costs, present value of expected cash flows, or the observable market price of the impaired loan is lower than the carrying value of the loan.

A loan is considered impaired when, based on current information and events, it is probable the Company will be unable to collect the scheduled payments of principal and interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. The amount of impairment, if any, and any subsequent changes are included in the allowance for loan losses or charged-off if determined to be uncollectible. By the time a loan becomes probable for foreclosure it has been charged down to fair value, less estimated costs to sell.

General allowances are established for non-impaired loans. These loans are assigned a loan category, and the allocated allowance for loan losses is determined based upon the loss percentage factors that correspond to each loan category.

Loss percentage factors are based on historical loss experience adjusted for qualitative factors. The qualitative factors consider, among other things, credit concentrations, recent levels and trends in delinquencies and nonaccrual loans, and growth in the loan portfolio. The occurrence of certain events could result in changes to the loss factors. Accordingly, these loss factors are reviewed periodically and modified as necessary.

(1) **Summary of Significant Accounting Policies, continued**  
**Allowance for Loan Losses, continued**

The general reserves are determined based on consideration of historic loss data, the various risk characteristics of each loan segment, and whether the loans are within or outside the Company's general market area. Risk characteristics relevant to each portfolio segment are as follows:

Construction, development and land loans — Loans in this segment primarily include real estate development loans for which payment is derived from sale of the property as well as construction projects in which the property will ultimately be used by the borrower. Credit risk is affected by cost overruns, time to sell at an adequate price, and market conditions.

Real estate - mortgage — Loans in this segment are dependent on the credit quality of the individual borrower. The overall health of the economy, including unemployment rates, will have an effect on the credit quality in the segment. The Company generally does not originate loans with a loan-to-value ratio greater than 85% and does not grant subprime loans.

Commercial real estate — Loans in this segment are owner occupied business properties and non-owner occupied business income-producing properties. The underlying cash flows generated by the properties and the businesses occupying the properties are adversely impacted by a downturn in the economy as evidenced by increased vacancy rates and decreased owner cash flows, which in turn, will have an effect on the credit quality in this segment. Management monitors the cash flows of these borrowers.

Commercial and industrial loans — Loans in this segment are made to businesses and are generally secured by assets of the business. Repayment is expected from the cash flows of the business. A weakened economy, and resultant decreased consumer spending, will have an effect on the credit quality in this segment.

Other loans – Loans in the segment are made to individuals and are generally secured by personal property and/or personal guaranties. Repayment is expected from the cash flows of the individual which is affected by the overall economy with specific regards to the unemployment rate.

Unallocated allowances relate to inherent losses that are not otherwise evaluated in the specific and general allowances. The qualitative factors associated with unallocated allowances are subjective and require a high degree of management judgment. These factors include the inherent imprecision in mathematical models and credit quality statistics, recent economic uncertainty, losses incurred from recent events, lagging or incomplete data and the significant factors affecting the real estate market.

**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 Company - put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

**Premises and Equipment**

Premises and equipment are stated at cost less accumulated depreciation, computed principally on the straight- line method over the estimated useful lives of the assets.

Maintenance and repairs that do not extend the useful life of the premises and equipment are charged to expense. The useful lives of premises and equipment are as follows:

Building	40 years
Furniture, fixtures and equipment	3-9 years

(1) **Summary of Significant Accounting Policies, continued**  
**Other Real Estate**

Real estate properties acquired through, or in lieu of, loan foreclosure are to be sold and are initially recorded at fair value less selling costs at the date of foreclosure establishing a new cost basis. Any write down to fair value at the time of foreclosure is charged to the allowance for loan losses. After foreclosure, valuations are periodically performed by management and the real estate is carried at the lower of carrying amount or fair value less cost to sell. Costs of improvements are capitalized, whereas costs relating to holding other real estate and subsequent adjustment to the value are expensed.

**Income Taxes**

Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the differences between the book and tax bases of the various balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws and considers any uncertain tax positions.

A valuation allowance for deferred tax assets is required when it is more likely than not that some portion or all of the deferred tax asset will not be realized. In assessing the realization of the deferred tax assets, management considers the scheduled reversals of deferred tax liabilities, projected future taxable income (in the near-term based on current projections), and tax planning strategies.

The Company recognizes accrued interest associated with uncertain tax positions as part of interest expense and penalties associated with uncertain tax positions as part of other expenses. As of December 31, 2018 and 2017, there were no accrued interest and penalties associated with uncertain tax positions.

The operating results of the Company and its subsidiary are included in consolidated income tax returns.

**Loss Contingencies**

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. The Company has a liability recorded as described more fully in Note 10 related to a pending claim that originated in 2017.

**Comprehensive Income**

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net earnings. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with our net earnings, are components of comprehensive income.

**Stock Based Compensation**

The Company maintains a share-based employee compensation plan for grants of equity based compensation to key personnel. The Company accounts for such share-based payment based on the fair value of such as of the date of grant. Upon issuance of share based payment awards, compensation cost is recognized in the consolidated financial statements of the Company for all share-based payments granted, based on the grant date fair value over the requisite service period of the awards. The stock based compensation plan is described more fully in Note 12.

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(2) Securities Available-for-Sale**

Investment securities available-for-sale at December 31, 2018 and 2017 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
<u>December 31, 2018:</u>				
U.S. Government sponsored enterprises	\$ 904,916	1,050	23,920	882,046
State and municipal securities	2,040,003	2,780	5,700	2,037,083
Mortgage-backed securities	16,460,592	1,167	519,819	15,941,940
Total	<u>\$ 19,405,511</u>	<u>4,997</u>	<u>549,439</u>	<u>18,861,069</u>
<u>December 31, 2017:</u>				
U.S. Government sponsored enterprises	\$ 1,133,153	581	21,723	1,112,011
State and municipal securities	2,082,609	10,333	3,131	2,089,811
Mortgage-backed securities	18,573,048	7,231	255,514	18,324,765
Total	<u>\$ 21,788,810</u>	<u>18,145</u>	<u>280,368</u>	<u>21,526,587</u>

The following table outlines the unrealized losses and fair value by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2018 and 2017.

	<u>2018</u>		<u>2017</u>	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
Unrealized loss for less than 12 months:				
U.S. Government sponsored enterprises	\$ -	-	-	-
State and municipal securities	1,034,302	5,700	1,033,510	3,131
Mortgage backed securities	-	-	7,322,384	38,462
Less than 12 months	<u>1,034,302</u>	<u>5,700</u>	<u>8,355,894</u>	<u>41,593</u>
Unrealized loss for greater than 12 months:				
U.S. Government sponsored enterprises	629,426	23,920	762,946	21,723
State and municipal securities	-	-	-	-
Mortgage backed securities	15,890,775	519,819	9,840,536	217,052
Total more than 12 months	<u>16,520,201</u>	<u>543,739</u>	<u>10,603,482</u>	<u>238,775</u>
Total	<u>\$ 17,554,503</u>	<u>549,439</u>	<u>18,959,376</u>	<u>280,368</u>

At December 31, 2018, securities in an unrealized loss position for greater than twelve months consist of one security sponsored by a U.S. Government enterprise and 26 mortgage-backed securities. At December 31, 2017, securities in an unrealized loss position for greater than twelve months consist of one security sponsored by a U.S. Government enterprise and 13 mortgage-backed securities. At December 31, 2018, securities in an unrealized loss position for less than twelve months consist of two state and municipal securities. At December 31, 2017, securities in an unrealized loss position for less than twelve months consist of one state and municipal security and 14 mortgage-backed 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 industry analysts' reports. As management has the ability to hold debt securities until maturity, or for the foreseeable future, no declines are deemed to be other than temporary.

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(2) Securities Available-for-Sale, continued**

The amortized cost and estimated fair value of securities available-for-sale at December 31, 2018, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
U.S Government sponsored enterprises & state and municipal securities:		
Five to ten years	\$ 2,040,003	2,037,083
Over ten years	904,916	882,046
Mortgage-backed securities	<u>16,460,592</u>	<u>15,941,940</u>
	<u>\$ 19,405,511</u>	<u>18,861,069</u>

The Company had no sales of investment securities during 2018 and 2017.

Securities with a carrying value of \$1,961,100 and \$1,441,143 at December 31, 2018 and 2017, respectively, were pledged to secure certain deposits.

**(3) Loans and Allowance for Loan Losses**

Major classifications of loans at December 31, 2018 and 2017 are summarized as follows:

	2018	2017
Construction, development and land	\$ 44,947,201	32,811,635
Real estate – mortgage	12,588,505	16,090,352
Commercial real estate	250,804,357	250,945,601
Commercial and industrial	48,912,682	50,231,985
Other	<u>2,670,639</u>	<u>2,701,730</u>
	359,923,384	352,781,303
Less: Allowance for loan losses	5,137,531	5,030,037
Unearned deferred fees	<u>831,513</u>	<u>1,004,731</u>
Loans, net	<u>\$ 353,954,340</u>	<u>346,746,535</u>

The loan classifications above include unamortized net premiums on purchased loans totaling \$10,268,996 and \$11,869,576 as of December 31, 2018 and 2017, respectively.

The Bank grants loans and extensions of credit to individuals and a variety of businesses operating in the north-metro Atlanta area. Although the Bank has a diversified loan portfolio, a substantial portion of the portfolio is collateralized by improved and unimproved real estate and is dependent upon the real estate market. In addition, the Bank makes loans nationally through government guaranteed lending programs.

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(3) Loans and Allowance for Loan Losses, continued**

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of December 31, 2018 and 2017:

December 31, 2018:	Construction, Development and Land	Real Estate - Mortgage	Commercial Real Estate	Commercial and Industrial	Other	Unallocated	Total
Allowance for loan losses:							
Balance at beginning of the period	\$ 139,013	58,755	4,078,791	114,726	9,553	629,199	5,030,037
Charge-offs	-	-	-	-	-	-	-
Recoveries	-	-	1,069	6,425	-	-	7,494
Provision for loan losses	152,256	(4,111)	(40,837)	6,740	4,044	(18,092)	100,000
Ending balance	<u>\$ 291,269</u>	<u>54,644</u>	<u>4,039,023</u>	<u>127,891</u>	<u>13,597</u>	<u>611,107</u>	<u>5,137,531</u>
Ending balance individually evaluated for impairment	\$ -	-	1,488,776	-	-	-	1,488,776
Ending balance collectively evaluated for impairment	291,269	54,644	2,550,247	127,891	13,597	611,107	3,648,755
	<u>\$ 291,269</u>	<u>54,644</u>	<u>4,039,023</u>	<u>127,891</u>	<u>13,597</u>	<u>611,107</u>	<u>5,137,531</u>
Loans:							
Individually evaluated for impairment	\$ -	-	2,977,553	-	-	-	2,977,553
Collectively evaluated for impairment	44,947,201	12,588,505	247,826,804	48,912,682	2,670,639	-	356,945,831
	<u>\$ 44,947,201</u>	<u>12,588,505</u>	<u>250,804,357</u>	<u>48,912,682</u>	<u>2,670,639</u>	<u>-</u>	<u>359,923,384</u>
December 31, 2017:							
Allowance for loan losses:							
Balance at beginning of the period	\$ 141,653	73,131	2,576,628	173,693	9,620	209,005	3,183,730
Charge-offs	-	-	-	-	-	-	-
Recoveries	-	20,047	-	1,260	-	-	21,307
Provision for loan losses	(2,640)	(34,423)	1,502,163	(60,227)	(67)	420,194	1,825,000
Ending balance	<u>\$ 139,013</u>	<u>58,755</u>	<u>4,078,791</u>	<u>114,726</u>	<u>9,553</u>	<u>629,199</u>	<u>5,030,037</u>
Ending balance individually evaluated for impairment	\$ -	-	1,578,695	-	-	-	1,578,695
Ending balance collectively evaluated for impairment	139,013	58,755	2,500,096	114,726	9,553	629,199	3,451,342
	<u>\$ 139,013</u>	<u>58,755</u>	<u>4,078,791</u>	<u>114,726</u>	<u>9,553</u>	<u>629,199</u>	<u>5,030,037</u>
Loans:							
Individually evaluated for impairment	\$ -	-	3,157,390	-	-	-	3,157,390
Collectively evaluated for impairment	32,811,635	16,090,352	247,788,211	50,231,985	2,701,730	-	349,623,913
	<u>\$ 32,811,635</u>	<u>16,090,352</u>	<u>250,945,601</u>	<u>50,231,985</u>	<u>2,701,730</u>	<u>-</u>	<u>352,781,303</u>

The following table presents the aging of the recorded investment in past due loans and non-accrual loan balances as of December 31, 2018 and 2017, respectively, by class of loans:

December 31, 2018:	30-59 Days Past Due	60-89 Days Past Due	>90 Days Past Due	Total Past Due	Current	Total	Non- Accrual
Construction, Development and Land	\$ 500,433	-	-	500,433	44,446,768	44,947,201	-
Real Estate – Mortgage	-	-	-	-	12,588,505	12,588,505	-
Commercial Real Estate	2,219,291	1,081,673	2,977,553	6,278,517	244,525,840	250,804,357	2,977,553
Commercial and Industrial	-	-	-	-	48,912,682	48,912,682	-
Other	-	-	-	-	2,670,639	2,670,639	-
Total	<u>\$ 2,719,724</u>	<u>1,081,673</u>	<u>2,977,553</u>	<u>6,778,950</u>	<u>353,144,434</u>	<u>359,923,384</u>	<u>2,977,553</u>

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(3) Loans and Allowance for Loan Losses, continued**

December 31, 2017:	30-59 Days Past Due	60-89 Days Past Due	>90 Days Past Due	Total Past Due	Current	Total	Non- Accrual
Construction, Development and Land	\$ -	-	-	-	32,811,635	32,811,635	-
Real Estate – Mortgage	-	-	-	-	16,090,352	16,090,352	-
Commercial Real Estate	5,970,150	547,750	-	6,517,900	244,427,701	250,945,601	3,157,390
Commercial and Industrial	-	-	-	-	50,231,985	50,231,985	-
Other	-	-	-	-	2,701,730	2,701,730	-
<b>Total</b>	<b>\$ 5,970,150</b>	<b>547,750</b>	<b>-</b>	<b>6,517,900</b>	<b>346,263,403</b>	<b>352,781,303</b>	<b>3,157,390</b>

As of December 31, 2018, the Company had an unpaid principal balance and recorded investment in impaired commercial real estate loans of \$2,977,553. The average recorded investment of these loans was \$3,059,889. There was no interest income recognized on these loans since deemed impaired. As of December 31, 2017, the Company had an unpaid principal balance and recorded investment in impaired commercial real estate loans of \$3,157,390. The average recorded investment of these loans was \$4,820,696. There was no interest income recognized on these loans since deemed impaired.

During 2018 and 2017, the Bank did not modify any loans that would be considered troubled debt restructurings. At December 31, 2018 and 2017, the Bank did not have any outstanding recorded investment in troubled debt restructurings.

The Company utilizes a nine grade internal loan rating system for its loan portfolio as follows:

- Loans rated 1-4 (Pass) - Loans in these categories have low to average risk.
- Loans rated 5 (Internal Watch List) - These assets raise some concern due to either prior financial or collateral problems, or recent developing conditions, and thus warrant closer monitoring and review than “pass” assets.
- Loans rated 6 (Special Mention) - These assets constitute an undue and unwarranted credit risk but not to the point of justifying a substandard classification.
- Loans rated 7 (Substandard) - A substandard asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any.
- Loans rated 8 (Doubtful) - An asset classified as doubtful has all the weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.
- Loans rated 9 (Loss) - Assets classified loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted.

As of December 31, 2018 and 2017, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

December 31, 2018:	Pass	Internal Watch List	Special Mention	Substandard	Doubtful/ Loss	Total
Construction, Development and Land	\$ 42,711,004	1,651,217	584,980	-	-	44,947,201
Real Estate – Mortgage	12,588,505	-	-	-	-	12,588,505
Commercial Real Estate	222,995,898	2,674,922	22,155,984	-	2,977,553	250,804,357
Commercial and Industrial	48,452,618	328,645	131,419	-	-	48,912,682
Other	2,670,639	-	-	-	-	2,670,639
	<b>\$ 329,418,664</b>	<b>4,654,784</b>	<b>22,872,383</b>	<b>-</b>	<b>2,977,553</b>	<b>359,923,384</b>



TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(3) Loans and Allowance for Loan Losses, continued**

December 31, 2017:	Pass	Internal Watch List	Special Mention	Substandard	Doubtful/ Loss	Total
Construction, Development and Land	\$ 32,811,635	-	-	-	-	32,811,635
Real Estate – Mortgage	16,090,352	-	-	-	-	16,090,352
Commercial Real Estate	241,384,260	5,191,656	880,554	331,741	3,157,390	250,945,601
Commercial and Industrial	50,089,845	-	142,140	-	-	50,231,985
Other	2,701,730	-	-	-	-	2,701,730
	<u>\$ 343,077,822</u>	<u>5,191,656</u>	<u>1,022,694</u>	<u>331,741</u>	<u>3,157,390</u>	<u>352,781,303</u>

The Company purchases loans and amortizes the premium over the estimated life of the portfolio on a level yield basis as a yield adjustment. During 2018, the Company purchased loans for a total purchase price of \$4,106,637. The loans had a carrying value of \$3,613,098. During 2017, the Company purchased loans for a total purchase price of \$110,307,900. The loans had a carrying value of \$97,614,957. The outstanding balances of purchased loans as of December 31, 2018 and 2017 was approximately \$103,014,000 and \$105,078,000, respectively. These loans are included in the loan disclosures above.

**(4) Premises and Equipment**

Premises and equipment at December 31, 2018 and 2017, are summarized as follows:

	2018	2017
Land	\$ 400,000	400,000
Building	1,154,606	1,154,606
Furniture, fixtures and equipment	305,685	217,804
	<u>1,860,291</u>	<u>1,772,410</u>
Less: Accumulated depreciation	386,233	291,293
	<u>\$ 1,474,058</u>	<u>1,481,117</u>

Depreciation expense was approximately \$95,000 and \$81,000 for the years ended December 31, 2018 and 2017, respectively.

**(5) Deposits**

The aggregate amount of time deposit accounts with a minimum denomination of \$250,000 was approximately \$81,105,000 and \$50,578,000 at December 31, 2018 and 2017, respectively.

At December 31, 2018, the scheduled maturities of time deposits were as follows:

2019	\$ 196,177,101
2020	34,376,407
2021	4,313,266
2022	161,030
2023	1,042,808
	<u>\$ 236,070,612</u>

Time deposits listed above includes approximately \$49,018,000 and \$33,143,000 in brokered certificates of deposit at December 31, 2018 and 2017, respectively.

**(6) Federal Funds Purchased**

As of December 31, 2018 and 2017, the Company has lines of credit with correspondent banks for overnight borrowings of \$35,500,000. The Company had no borrowings outstanding on these lines at December 31, 2018 and 2017.

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(7) Federal Home Loan Bank Advances**

At December 31, 2018 and 2017, the Company had advances of \$20,500,000 and \$27,500,000, respectively, outstanding from the FHLB.

The following advances, which required monthly or quarterly interest payments, were outstanding at December 31, 2018:

Advance Date	Advance	Interest Rate	Maturity	Rate Type
12/12/2018	\$ 2,500,000	2.84%	12/11/2020	Fixed
11/07/2018	5,000,000	3.08%	02/08/2021	Fixed
10/05/2018	4,000,000	3.03%	04/05/2021	Fixed
09/20/2018	4,000,000	2.92%	09/18/2020	Fixed
09/18/2018	<u>5,000,000</u>	2.65%	09/18/2019	Daily Rate Credit
	<u>\$ 20,500,000</u>			

The following advances, which required monthly or quarterly interest payments, were outstanding at December 31, 2017:

Advance Date	Advance	Interest Rate	Maturity	Rate Type
12/21/2017	\$ 5,000,000	1.55%	04/20/2018	Fixed
12/20/2017	5,000,000	1.50%	03/20/2018	Fixed
11/28/2017	2,000,000	1.43%	02/28/2018	Fixed
09/13/2017	10,000,000	1.59%	09/13/2018	Daily Rate Credit
09/04/2008	3,000,000	3.60%	09/04/2018	Convertible
09/08/2008	<u>2,500,000</u>	3.25%	09/10/2018	Convertible
	<u>\$ 27,500,000</u>			

The aggregate of the advances is collateralized by the Company's FHLB stock, the Company's deposits with the FHLB, certain securities and a blanket floating lien on a portion of the Company's loan portfolio, portions of which can be used to cover any defaults on repayments of advances. The total amount of loans pledged as of December 31, 2018 and 2017 was approximately \$53,295,000 and \$54,449,000, respectively.

**(8) Income Taxes**

On December 22, 2017, the Tax Cuts and Jobs Act ("Tax Reform") was signed into law and impacts individuals, pass through entities and corporations. The Company was impacted by the corporation changes. The new federal corporate tax rate fell from a maximum 35% rate to 21% beginning in 2018. For the year ended December 31, 2017, current income tax was based on a tax rate of 34%. GAAP requires the deferred tax components to be recorded at the rate in which the differences are expected to reverse which impacts tax expense for the year ended December 31, 2017. Based on the new corporate tax rate of 21% for 2018 and forward, the deferred tax assets and liabilities were revalued at the new rate and the adjustment of approximately \$464,000 was recorded directly to income tax expense in 2017, including any impact associated with the deferred tax component of unrealized losses on available-for-sale securities.

Additionally, the Company recorded a reclassification entry of approximately \$23,000 between accumulated other comprehensive loss and accumulated deficit in order to correct the stranded amount associated with the true up of the net deferred asset on available-for-sale securities. The reclassification entry is disclosed within the Statements of Changes in Stockholders' Equity.

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(8) Income Taxes, continued**

The components of income tax expense for the years ended December 31, 2018 and 2017 consisted of the following:

	<u>2018</u>	<u>2017</u>
Current	\$ 1,750,436	1,785,356
Deferred	40,314	259,279
Change in valuation allowance	-	(203,185)
Rate reduction adjustment	-	464,120
	<u>\$ 1,790,750</u>	<u>2,305,570</u>

The Company's income tax expense differs from the amounts computed by applying the federal income tax statutory rates to earnings before income taxes. A reconciliation of the differences is as follows:

	<u>2018</u>	<u>2017</u>
Tax provision at federal statutory rate (21% and 34%)	\$ 1,502,057	1,420,010
State income tax	230,167	95,048
Other	58,526	(16,563)
Change in valuation allowance	-	(203,185)
Write down of deferred tax asset related to stock warrants	-	546,140
Rate reduction adjustment	-	464,120
	<u>\$ 1,790,750</u>	<u>2,305,570</u>

The following summarizes the components of the net deferred tax asset, which is included in other assets at December 31, 2018 and 2017.

	<u>2018</u>	<u>2017</u>
Deferred income tax assets:		
Pre-opening expense	\$ 94,370	118,279
Allowance for loan losses	894,491	875,093
Stock-based compensation	83,538	39,527
Deferred loan fees	30,847	31,056
Securities available-for-sale	116,369	63,168
Premises and equipment	51,513	36,471
State income tax credits	-	15,781
Other	11,723	11,803
Gross deferred income tax assets	1,282,851	1,191,178
Deferred income tax liability consisting of government guaranteed loans servicing asset	<u>270,267</u>	<u>191,481</u>
Net deferred income tax asset	<u>\$ 1,012,584</u>	<u>999,697</u>

**(9) Related Party Transactions**

The Bank conducts transactions with its directors and officers, including companies in which they have beneficial interest, in the normal course of business. It is the policy of the Bank that loan transactions with directors and officers be made on substantially the same terms as those prevailing at the time for comparable loans to other persons. There was no related party loan activity for 2018.

Deposits from related parties totaled approximately \$20,622,000 and \$17,505,000 at December 31, 2018 and 2017, respectively.

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(10) Commitments and Contingencies**

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheet. The contract amounts of those instruments reflect the extent of involvement the Bank has in particular classes of financial instruments.

The Bank's exposure to credit loss in the event of nonperformance by the other party 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 conditional obligations as it does for on-balance-sheet instruments.

The Bank generally requires collateral or other security to support financial instruments with off-balance sheet risk.

	Approximate Contractual Amount	
	2018	2017
Financial instruments whose contract amounts represent credit risk:		
Commitments to extend credit	\$ 33,134,624	24,784,631
Standby letters of credit	\$ 228,050	242,295

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 many of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank, upon extension of credit is based on management's credit evaluation. Collateral held varies but may include unimproved and improved real estate, certificates of deposit, or personal property.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance 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 loan facilities to customers.

The Company entered into a lease agreement to lease an office location in Alpharetta, Georgia for a term of fifty-four months, with the lease commencing in February 2015 and ending in July 2019. The Company expects to renew the lease and is currently in lease negotiations.

The minimum lease payments not including common area cost allocation under these leases are as follows:

Year ending December 31,	Minimum Lease Payments
2019	\$ 45,381

Total rental expense was \$66,784 for the years ended December 31, 2018 and 2017.

There is pending litigation against the Company as of December 31, 2018. The litigation relates to two loans which are claimed to have been fraudulently executed by an individual who was not authorized to do so by the borrowing company. The Company has moved these loans to an impaired loan classification and established a specific reserve of approximately \$1,489,000 related to its estimate for potential losses regarding this matter as of December 31, 2018.

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(11) Employee Benefits**

The Company has a 401(k) plan covering all employees. There was approximately \$3,000 and \$5,000 in expenses related to this plan charged to operations for 2018 and 2017, respectively.

**(12) Stock-based Compensation**  
**Stock Options**

During 2008, the Company adopted an Employee Incentive Stock Plan (the "Stock Plan"). The Stock Plan offers stock awards to key employees to encourage continued employment by facilitating their purchase of an equity interest in the Company. These awards are granted at the discretion of the Board of Directors at an exercise price determined by the Board at the grant date. Options awarded under the Stock Plan have a term of ten years from the date of grant and vest ratably over three years, unless otherwise stated in the award agreement. A total of 191,000 shares have been reserved under the Stock Plan.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. Expected volatility for the period has been determined by the expected volatility of similar entities. The expected term of options granted represents the period of time that the options are expected to be outstanding. Expected dividends are based on dividend trends of the Company's stock at grant. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

Option related compensation cost recorded during the years ended December 31, 2018 and 2017 was approximately \$175,000 and \$146,000, respectively. At December 31, 2018, there was approximately \$205,000 of total unrecognized compensation cost related to options outstanding. The cost is expected to be recognized over a weighted average period of approximately 1.17 years.

There were no stock options granted during 2018. Assumptions used in calculating the fair value of options granted during 2017 were as follows:

	2017
Dividend yield	0.56%
Volatility	30%
Risk-free interest rate	2.46%
Term	9 years

A summary of activity for all stock options for the years ended December 31, 2018 and 2017 is presented below:

	Shares	Weighted Avg. Exercise Price	Weighted Avg. Remaining Contractual Term (Years)
Outstanding at December 31, 2016	36,418	\$ 8.59	4.70
Granted during the year	154,582	8.85	9.17
Outstanding at December 31, 2017	191,000	8.80	7.94
Forfeited during the year	18,000	7.84	2.77
Expired during the year	13,418	10.00	-
Outstanding, December 31, 2018	159,582	7.36	6.71
Exercisable at December 31, 2018	99,467	\$ 8.78	7.95

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(13) Stockholders' Equity**

On September 1, 2017, the Company initiated a private offering to accredited investors of up to 35,000,000 shares of its common stock at a price of \$10.05 per share. During 2017, the Company issued a total of 1,003,000 shares of common stock for total proceeds of \$10,029,665, net of offering costs of \$50,485 related to this offering. During 2018, the Company issued a total of 7,500 shares of common stock for total proceeds of \$75,375. The offering expired on January 31, 2018.

**(14) Regulatory Matters**

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

In July 2013, the Federal bank regulatory agencies issued a final rule that revised their risk-based capital requirements and the method for calculating components of capital and of computing risk-weighted assets to make them consistent with agreements that were reached by the Basel Committee on Banking Supervision and certain provisions of the Dodd-Frank Act. The final rule applies to all depository institutions, top-tier bank holding companies with total consolidated assets of \$500 million or more and top-tier savings and loan holding companies. The rule established a new common equity Tier 1 minimum capital requirement, increased the minimum capital ratios and assigned a higher risk weight to certain assets based on the risk associated with these assets. The final rule includes a transition period that implements the new regulations over a five year period. These changes were phased in beginning in January 2015. Management continues to evaluate this final rule and its potential impact on the Bank. Preliminary assessments indicate that the Bank will continue to exceed all regulatory capital requirements under the phased in requirements of the new rule.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios of total common equity Tier 1, total and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets. Management believes, as of December 31, 2018, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2018 and 2017, the most recent notification from the FDIC categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum common equity Tier 1 risk-based, total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth below. There are no conditions or events since that notification that management believes have changed the Bank's category.

The Bank's actual capital amounts and ratios as of December 31, 2018 and 2017 are also presented below.

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2018:						
(Dollars in Thousands)						
Common Equity Tier 1 Capital to Risk-Weighted Assets	\$ 47,144	18.14%	\$ 11,693	4.50%	\$ 16,889	6.50%
Total Capital to Risk-Weighted Assets	\$ 50,415	19.40%	\$ 20,787	8.00%	\$ 25,983	10.00%
Tier I Capital to Risk-Weighted Assets	\$ 47,144	18.14%	\$ 15,590	6.00%	\$ 20,787	8.00%
Tier I Capital to Average Assets	\$ 47,144	12.03%	\$ 15,670	4.00%	\$ 19,587	5.00%

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
Notes to Consolidated Financial Statements, continued

**(14) Regulatory Matters, continued**

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2017:	(Dollars in Thousands)					
Common Equity Tier 1 Capital to Risk-Weighted Assets	\$ 43,642	17.91%	\$ 10,964	4.50%	\$ 15,837	6.50%
Total Capital to Risk-Weighted Assets	\$ 46,714	19.17%	\$ 19,492	8.00%	\$ 24,365	10.00%
Tier I Capital to Risk-Weighted Assets	\$ 43,642	17.91%	\$ 14,619	6.00%	\$ 19,492	8.00%
Tier I Capital to Average Assets	\$ 43,642	11.48%	\$ 15,204	4.00%	\$ 19,004	5.00%

**(15) Limitation on Distributions**

Dividends paid by the Bank are the primary source of funds available to the Company. Banking regulations limit the amount of dividends that may be paid to the Company without prior approval of the regulatory authorities. These restrictions are based on the level of regulatory classified assets, the prior years' net earnings, and the ratio of equity capital to total assets. The Company declared a dividend of \$1,342,767 on November 14, 2018 for shareholders of record as of December 31, 2018. The dividend was paid on January 31, 2019.

**(16) Fair Value Measurements**

The Company utilizes fair value measurements to record fair value adjustments to certain assets. Investment securities available-for-sale are recorded at fair value on a recurring basis.

Fair Value Hierarchy

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

- Level 1 – Valuation is based upon quoted prices for identical instruments traded in active markets.
- Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 – Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

Following is a description of valuation methodologies used for assets which are recorded at fair value:

Investment Securities Available-for-Sale

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

TOUCHMARK BANCSHARES, INC. AND SUBSIDIARY  
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**(16) Fair Value Measurements, continued**

Loans

The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and a specific allocation is established within the allowance for loan losses. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment using one of three methods, including collateral value, market value of similar debt, and discounted cash flows.

Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. Impaired loans in which an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price, the Company records the impaired loan as nonrecurring Level 2. When an appraised value is utilized or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3.

Other Real Estate

Other real estate properties are adjusted to fair value less estimated selling costs upon transfer of the loans to other real estate. Subsequently, other real estate assets are carried at the lower of carrying value or fair value. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. When the fair value is based on an observable market price, the Company records the other real estate as nonrecurring Level 2. When the fair value is based on an appraised value, or when an appraised value is not available, the Company records the other real estate asset as nonrecurring Level 3. There were no other real estate properties as of December 31, 2018 and 2017.

Assets Recorded at Fair Value on a Recurring Basis

The table below presents the recorded amount of assets measured at fair value on a recurring basis as of December 31, 2018 and 2017.

<u>December 31, 2018:</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
U.S. government sponsored enterprises	\$ -	882,046	-	882,046
State and municipal securities	-	2,037,083	-	2,037,083
Mortgage-backed securities	-	15,941,940	-	15,941,940
	<u>\$ -</u>	<u>18,861,069</u>	<u>-</u>	<u>18,861,069</u>
<u>December 31, 2017:</u>				
U.S. government sponsored enterprises	\$ -	1,112,011	-	1,112,011
Mortgage-backed securities	-	2,089,811	-	2,089,811
Corporate securities	-	18,324,765	-	18,324,765
	<u>\$ -</u>	<u>21,526,587</u>	<u>-</u>	<u>21,526,587</u>

Assets Recorded at Fair Value on a Nonrecurring Basis

The Company may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with U.S. generally accepted accounting principles. These include assets that are measured at the lower of cost or market that were recognized at fair value below cost at the end of the period. Assets measured at fair value on a nonrecurring basis as of December 31, 2018 and 2017 are included in the table below.

<u>December 31, 2018:</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Impaired loans, net	\$ -	-	1,488,776	1,488,776
<u>December 31, 2017:</u>				
Impaired loans, net	\$ -	-	1,578,695	1,578,695