

Section 1: 10-Q (FORM 10-Q)

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

- QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED September 30, 2019
- TRANSITION REPORT UNDER SECTION 13 OR 15 (D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM _____ TO _____

COMMISSION FILE NUMBER: 000-49883

PLUMAS BANCORP

(Exact Name of Registrant as Specified in Its Charter)

California

(State or Other Jurisdiction of Incorporation or Organization)

75-2987096

(I.R.S. Employer Identification No.)

35 S. Lindan Avenue, Quincy, California

(Address of Principal Executive Offices)

95971

(Zip Code)

Registrant's Telephone Number, Including Area Code (530) 283-7305

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See definition of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act:

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer Smaller Reporting Company Emerging Growth Company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class:
Common Stock, no par value

Trading Symbol
PLBC

Name of Each Exchange on which Registered:
The NASDAQ Stock Market LLC

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of October 25, 2019. 5,159,560 shares.

PART I – FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

PLUMAS BANCORP AND SUBSIDIARY
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

(In thousands, except share data)

	<u>September 30,</u> <u>2019</u>	<u>December 31,</u> <u>2018</u>
<u>Assets</u>		
Cash and cash equivalents	\$ 77,880	\$ 46,686
Investment securities available for sale	169,516	171,507
Loans, less allowance for loan losses of \$7,226 at September 30, 2019 and \$6,958 at December 31, 2018	598,001	562,498
Real estate acquired through foreclosure	1,094	1,170
Premises and equipment, net	14,554	14,287
Bank owned life insurance	13,102	12,856
Accrued interest receivable and other assets	14,404	15,394
Total assets	<u>\$ 888,551</u>	<u>\$ 824,398</u>
<u>Liabilities and Shareholders' Equity</u>		
Deposits:		
Non-interest bearing	\$ 353,203	\$ 304,039
Interest bearing	422,980	422,526
Total deposits	<u>776,183</u>	<u>726,565</u>
Repurchase agreements	13,389	13,058
Accrued interest payable and other liabilities	6,890	7,533
Junior subordinated deferrable interest debentures	10,310	10,310
Total liabilities	<u>806,772</u>	<u>757,466</u>
Commitments and contingencies (Note 5)		
Shareholders' equity:		
Common stock, no par value; 22,500,000 shares authorized; issued and outstanding – 5,159,560 shares at September 30, 2019 and 5,137,476 at December 31, 2018	7,197	6,944
Retained earnings	72,449	62,005
Accumulated other comprehensive income (loss), net	2,133	(2,017)
Total shareholders' equity	<u>81,779</u>	<u>66,932</u>
Total liabilities and shareholders' equity	<u>\$ 888,551</u>	<u>\$ 824,398</u>

See notes to unaudited condensed consolidated financial statements.

PLUMAS BANCORP AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)
(In thousands, except per share data)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	2018	2019	2018
Interest Income:				
Interest and fees on loans	\$ 8,761	\$ 7,693	\$ 25,655	\$ 21,680
Interest on investment securities	1,075	1,037	3,353	2,873
Other	171	113	445	402
Total interest income	<u>10,007</u>	<u>8,843</u>	<u>29,453</u>	<u>24,955</u>
Interest Expense:				
Interest on deposits	304	159	923	462
Interest on junior subordinated deferrable interest debentures	131	131	406	370
Other	5	2	11	5
Total interest expense	<u>440</u>	<u>292</u>	<u>1,340</u>	<u>837</u>
Net interest income before provision for loan losses	9,567	8,551	28,113	24,118
Provision for Loan Losses				
Provision for loan losses	300	300	900	800
Net interest income after provision for loan losses	<u>9,267</u>	<u>8,251</u>	<u>27,213</u>	<u>23,318</u>
Non-Interest Income:				
Service charges	676	628	1,996	1,919
Interchange revenue	642	572	1,739	1,619
Gain on sale of loans	313	564	788	1,763
Gain on equity securities with no readily determinable fair value	-	-	-	209
Gain (loss) on sale of investments	-	-	20	(8)
Other	515	520	1,578	1,538
Total non-interest income	<u>2,146</u>	<u>2,284</u>	<u>6,121</u>	<u>7,040</u>
Non-Interest Expenses:				
Salaries and employee benefits	3,439	3,049	9,743	9,086
Occupancy and equipment	799	721	2,482	2,127
Other	1,637	1,658	5,077	4,893
Total non-interest expenses	<u>5,875</u>	<u>5,428</u>	<u>17,302</u>	<u>16,106</u>
Income before provision for income taxes	5,538	5,107	16,032	14,252
Provision for Income Taxes				
Provision for income taxes	1,536	1,411	4,402	3,830
Net income	<u>\$ 4,002</u>	<u>\$ 3,696</u>	<u>\$ 11,630</u>	<u>\$ 10,422</u>
Basic earnings per share	<u>\$ 0.78</u>	<u>\$ 0.72</u>	<u>\$ 2.26</u>	<u>\$ 2.04</u>
Diluted earnings per share	<u>\$ 0.77</u>	<u>\$ 0.71</u>	<u>\$ 2.22</u>	<u>\$ 2.00</u>

See notes to unaudited condensed consolidated financial statements.

PLUMAS BANCORP AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)
(In thousands)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	2018	2019	2018
Net income	\$ 4,002	\$ 3,696	\$ 11,630	\$ 10,422
Other comprehensive income:				
Change in net unrealized gain/loss	979	(1,285)	5,912	(4,657)
Reclassification adjustments for net (gains) losses included in net income	-	-	(20)	8
Net unrealized holding gain (loss)	979	(1,285)	5,892	(4,649)
Related tax effect:				
Change in net unrealized gain/loss	(289)	380	(1,748)	1,376
Reclassification of net gains (losses) included in net income	-	-	6	(2)
Income tax effect	(289)	380	(1,742)	1,374
Other comprehensive income (loss)	690	(905)	4,150	(3,275)
Total comprehensive income	\$ 4,692	\$ 2,791	\$ 15,780	\$ 7,147

See notes to unaudited condensed consolidated financial statements.

PLUMAS BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(in thousands, except shares)

	<u>Common Stock</u>		<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income (Loss) (Net of Taxes)</u>	<u>Total Shareholders' Equity</u>
	<u>Shares</u>	<u>Amount</u>			
Balance, December 31, 2017	5,064,972	\$ 6,415	\$ 49,855	\$ (570)	\$ 55,700
Net Income			10,422		10,422
Other comprehensive loss				(3,275)	(3,275)
Cash dividends on common stock			(920)		(920)
Exercise of stock options and tax effect	60,504	291			291
Stock-based compensation expense		148			148
Balance, September 30, 2018	<u>5,125,476</u>	<u>\$ 6,854</u>	<u>\$ 59,357</u>	<u>\$ (3,845)</u>	<u>\$ 62,366</u>
Balance, December 31, 2018	5,137,476	\$ 6,944	\$ 62,005	\$ (2,017)	\$ 66,932
Net Income			11,630		11,630
Other comprehensive income				4,150	4,150
Cash dividends on common stock			(1,186)		(1,186)
Exercise of stock options and tax effect	22,084	103			103
Stock-based compensation expense		150			150
Balance, September 30, 2019	<u>5,159,560</u>	<u>\$ 7,197</u>	<u>\$ 72,449</u>	<u>\$ 2,133</u>	<u>\$ 81,779</u>

See notes to unaudited condensed consolidated financial statements.

PLUMAS BANCORP AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	For the Nine Months Ended September 30,	
	2019	2018
Cash Flows from Operating Activities:		
Net income	\$ 11,630	\$ 10,422
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	900	800
Change in deferred loan origination costs/fees, net	(553)	(1,232)
Depreciation and amortization	1,065	749
Stock-based compensation expense	150	148
(Gain) loss on sale of investments	(20)	8
Amortization of investment security premiums	598	518
Gain on equity securities with no readily determinable fair value	-	(209)
Gain on sale of OREO and other vehicles	(14)	(80)
Gain on sale of loans held for sale	(788)	(1,763)
Loans originated for sale	(16,766)	(34,289)
Proceeds from loan sales	17,887	37,327
Provision from change in OREO valuation	-	38
Earnings on bank-owned life insurance	(246)	(246)
Increase in accrued interest receivable and other assets	(297)	(74)
(Decrease) increase in accrued interest payable and other liabilities	(643)	334
Net cash provided by operating activities	<u>12,903</u>	<u>12,451</u>
Cash Flows from Investing Activities:		
Proceeds from principal repayments from available-for-sale government-sponsored mortgage-backed securities	16,946	11,349
Purchases of available-for-sale securities	(21,471)	(40,286)
Proceeds from sale of available-for-sale securities	11,379	4,157
Net increase in loans	(36,881)	(55,871)
Proceeds from Bank owned life insurance	-	338
Proceeds from sale of OREO	85	568
Proceeds from sale of other vehicles	420	400
Purchase of premises and equipment	(1,053)	(3,079)
Net cash used in investing activities	<u>(30,575)</u>	<u>(82,424)</u>

Continued on next page.

PLUMAS BANCORP AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)
(Continued)

	For the Nine Months Ended September 30,	
	2019	2018
Cash Flows from Financing Activities:		
Net increase in demand, interest bearing and savings deposits	\$ 64,328	\$ 26,307
Net decrease in time deposits	(14,710)	(6,122)
Net increase (decrease) in securities sold under agreements to repurchase	331	(1,864)
Cash dividends paid on common stock	(1,186)	(920)
Proceeds from exercise of stock options	103	291
Net cash provided by financing activities	48,866	17,692
Increase (decrease) in cash and cash equivalents	31,194	(52,281)
Cash and Cash Equivalents at Beginning of Year	46,686	87,537
Cash and Cash Equivalents at End of Period	\$ 77,880	\$ 35,256
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the period for:		
Interest expense	\$ 1,334	\$ 842
Income taxes	\$ 4,409	\$ 3,336
Non-Cash Investing Activities:		
Real estate and vehicles acquired through foreclosure	\$ 409	\$ 646
Non-Cash Financing Activities:		
Common stock retired in connection with the exercise of stock options	\$ 42	\$ 29

See notes to unaudited condensed consolidated financial statements.

PLUMAS BANCORP AND SUBSIDIARY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. THE BUSINESS OF PLUMAS BANCORP

During 2002, Plumas Bancorp (the "Company") was incorporated as a bank holding company for the purpose of acquiring Plumas Bank (the "Bank") in a one bank holding company reorganization. This corporate structure gives the Company and the Bank greater flexibility in terms of operation, expansion and diversification. The Company formed Plumas Statutory Trust I ("Trust I") for the sole purpose of issuing trust preferred securities on September 26, 2002. The Company formed Plumas Statutory Trust II ("Trust II") for the sole purpose of issuing trust preferred securities on September 28, 2005.

The Bank operates eleven branches in California, including branches in Alturas, Chester, Fall River Mills, Greenville, Kings Beach, Portola, Quincy, Redding, Susanville, Tahoe City, and Truckee. In December 2015 the Bank opened a branch in Reno, Nevada; its first branch outside of California and in 2018 the Bank purchased a branch located in Carson City, Nevada. The Bank's administrative headquarters is in Quincy, California. In addition, the Bank operates a lending office specializing in government-guaranteed lending in Auburn, California, and commercial/agricultural lending offices in Chico and Red Bluff, California and Klamath Falls, Oregon. 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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation and Basis of Presentation

The consolidated financial statements include the accounts of the Company and the consolidated accounts of its wholly-owned subsidiary, Plumas Bank. All significant intercompany balances and transactions have been eliminated.

Plumas Statutory Trust I and Trust II are not consolidated into the Company's consolidated financial statements and, accordingly, are accounted for under the equity method. The Company's investment in Trust I of \$347,000 and Trust II of \$178,000 are included in accrued interest receivable and other assets on the consolidated balance sheet. The junior subordinated deferrable interest debentures issued and guaranteed by the Company and held by Trust I and Trust II are reflected as debt on the consolidated balance sheet.

The accounting and reporting policies of Plumas Bancorp and subsidiary conform with accounting principles generally accepted in the United States of America and prevailing practices within the banking industry. In the opinion of management, the unaudited condensed consolidated financial statements contain all adjustments (consisting of only normal recurring adjustments) necessary to present fairly the Company's financial position at September 30, 2019 and the results of its operations and its cash flows for the three-month and nine-month periods ended September 30, 2019 and 2018. Our condensed consolidated balance sheet at December 31, 2018 is derived from audited financial statements.

The unaudited condensed consolidated financial statements of the Company have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") for interim reporting on Form 10-Q. Accordingly, certain disclosures normally presented in the notes to the annual consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") have been omitted. The Company believes that the disclosures are adequate to make the information not misleading. These interim financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's 2018 Annual Report to Shareholders on Form 10-K. The results of operations for the three-month and nine-month periods ended September 30, 2019 may not necessarily be indicative of future operating results. In preparing such financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and revenues and expenses for the periods reported. Actual results could differ significantly from those estimates.

Reclassifications

Certain reclassifications have been made to prior years' balances to conform to the classifications used in 2019. These reclassifications had no impact on the Company's consolidated financial position, results of operations or net change in cash and cash equivalents.

Segment Information

Management has determined that since all of the banking products and services offered by the Company are available in each branch of the Bank, all branches are located within the same economic environment and management does not allocate resources based on the performance of different lending or transaction activities, it is appropriate to aggregate the Bank branches and report them as a single operating segment. No customer accounts for more than 10 percent of revenues for the Company or the Bank.

Revenue from Contracts with Customers

The Company records revenue from contracts with customers in accordance with Accounting Standards Codification Topic 606, "Revenue from Contracts with Customers" ("Topic 606"). Under Topic 606, the Company must identify the contract with a customer, identify the performance obligations in the contract, determine the transaction price, allocate the transaction price to the performance obligations in the contract, and recognize revenue when (or as) the Company satisfies a performance obligation. Significant revenue has not been recognized in the current reporting period that results from performance obligations satisfied in previous periods.

Most of the Company's revenue-generating transactions are not subject to ASC 606, including revenue generated from financial instruments, such as the Company's loans and investment securities. The Company has evaluated the nature of its contracts with customers and determined that further disaggregation of revenue from contracts with customers into more granular categories beyond what is presented in the Condensed Consolidated Statements of Income was not necessary. The Company generally fully satisfies its performance obligations on its contracts with customers as services are rendered and the transaction prices are typically fixed; charged either on a periodic basis or based on activity. Because performance obligations are satisfied as services are rendered and the transaction prices are fixed, there is little judgment involved in applying Topic 606 that significantly affects the determination of the amount and timing of revenue from contracts with customers.

Recently Adopted Accounting Pronouncements

On February 25, 2016, the FASB issued ASU 2016-02, Leases. The most significant change for lessees is the requirement under the new guidance to recognize right-of-use assets and lease liabilities for all leases not considered short-term leases, which is generally defined as a lease term of less than 12 months. This change results in lessees recognizing right-of-use assets and lease liabilities for most leases currently accounted for as operating leases under prior lease accounting guidance. ASU 2016-02 is effective for interim and annual periods beginning after December 15, 2018. The Company has several lease agreements, including two branch locations, which are currently considered operating leases, and therefore, not recognized on the Company's consolidated statements of condition. The Company adopted ASU No. 2016-02 on January 1, 2019 and recorded \$565,000 in right-of-use assets and lease liabilities on adoption.

In July 2018, the FASB issued ASU No. 2018-11, Leases - Targeted Improvements. ASU No. 2018-11 provides entities with relief from the costs of implementing certain aspects of the new leasing standard, ASU No. 2016-02. Specifically, under the amendments in ASU 2018-11: (1) entities may elect not to recast the comparative periods presented when transitioning to the new leasing standard, and (2) lessors may elect not to separate lease and non-lease components when certain conditions are met. The amendments have the same effective date as ASU 2016-02 (January 1, 2019 for the Company). The Company adopted ASU No. 2018-11 on January 1, 2019. The provisions of ASU 2018-11 did not have a material impact on the Company's Consolidated Financial Statements.

On March 30, 2017, the FASB issued ASU 2017-08, Receivables – Non-Refundable Fees and Other Costs: Premium Amortization on Purchased Callable Debt Securities. This ASU amends the amortization period for certain purchased callable debt securities held at a premium, shortening such period to the earliest call date. The amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity. ASU 2017-08 is effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Entities will apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (i.e., modified retrospective approach). The Company adopted ASU No. 2017-08 on January 1, 2019. The provisions of ASU No. 2017-08 did not have a material impact on the Company's Consolidated Financial Statements.

Pending Accounting Pronouncements

In June 2016, the FASB issued ASU No. 2016-13, Measurement of Credit Losses on Financial Instruments. ASU No. 2016-13 significantly changes how entities will measure credit losses for most financial assets and certain other instruments that aren't measured at fair value through net income. The standard will replace today's "incurred loss" approach with an "expected loss" model. The new model, referred to as the current expected credit loss ("CECL") model, will apply to: (1) financial assets subject to credit losses and measured at amortized cost, and (2) certain off-balance sheet credit exposures. This includes, but is not limited to, loans, leases, held-to-maturity securities, loan commitments, and financial guarantees. The CECL model does not apply to available-for-sale ("AFS") debt securities. For AFS debt securities with unrealized losses, entities will measure credit losses in a manner similar to what they do today, except that the losses will be recognized as allowances rather than reductions in the amortized cost of the securities. The ASU also simplifies the accounting model for purchased credit-impaired debt securities and loans. ASU No. 2016-13 also expands the disclosure requirements regarding an entity's assumptions, models, and methods for estimating the allowance for loan and lease losses. ASU No. 2016-13 is effective for interim and annual reporting periods beginning after December 15, 2019; early adoption is permitted for interim and annual reporting periods beginning after December 15, 2018. Entities will apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (i.e., modified retrospective approach). The Company has begun its implementation efforts by establishing an implementation team chaired by the Company's Chief Lending Officer and composed of members of the Company's credit administration and accounting departments. We have purchased software to support the CECL calculation of the allowance for loan losses under ASU No 2016-13 and have engaged the software vendor to assist in the transition to the CECL model. The Company's preliminary evaluation indicates the provisions of ASU No. 2016-13 are expected to impact the Company's Consolidated Financial Statements, in particular the level of the reserve for credit losses. However, the Company continues to evaluate the extent of the potential impact.

On October 16, 2019, the FASB approved a proposal to change the effective date of ASU No. 2016-13 for smaller reporting companies, as defined by the SEC, and other non-SEC reporting entities delaying the effective date to fiscal years beginning after December 31, 2022, including interim periods within those fiscal periods.

As the Company is a smaller reporting company and has not adopted provisions of the standard early, the delay is applicable to the Company.

In August 2018, the FASB issued ASU No. 2018-13, Fair Value Measurement, Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement. The amendments in this update modify the disclosure requirements for fair value measurements by removing, modifying, or adding certain disclosures. The update is effective for interim and annual periods in fiscal years beginning after December 15, 2019, with early adoption permitted. Entities are also allowed to elect early adoption of the eliminated or modified disclosure requirements and delay adoption of the new disclosure requirements until their effective date. As ASU No. 2018-13 only revises disclosure requirements, it will not have a material impact on the Company's Consolidated Financial Statements.

3. INVESTMENT SECURITIES AVAILABLE FOR SALE

The amortized cost and estimated fair value of investment securities at September 30, 2019 and December 31, 2018 consisted of the following, in thousands:

Available-for-Sale	September 30, 2019			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Debt securities:				
U.S. Government-sponsored agencies collateralized by mortgage obligations- residential	\$ 134,990	\$ 1,969	\$ (253)	\$ 136,706
Obligations of states and political subdivisions	31,498	1,331	(19)	32,810
	<u>\$ 166,488</u>	<u>\$ 3,300</u>	<u>\$ (272)</u>	<u>\$ 169,516</u>

Net unrealized gain on available-for-sale investment securities totaling \$3,028,000 were recorded, net of \$895,000 in tax benefits, as accumulated other comprehensive income within shareholders' equity at September 30, 2019. During the nine months ended September 30, 2019 the Company sold forty available-for-sale investment securities for total proceeds of \$11,379,000 recording a \$20,000 gain on sale. The Company realized a gain on sale from twenty-three of these securities totaling \$59,000 and a loss on sale on seventeen securities of \$39,000. No securities were sold during the three months ended September 30, 2019.

Available-for-Sale	December 31, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Debt securities:				
U.S. Government-sponsored agencies collateralized by mortgage obligations- residential	\$ 135,059	\$ 240	\$ (2,621)	\$ 132,678
Obligations of states and political subdivisions	39,311	121	(603)	38,829
	<u>\$ 174,370</u>	<u>\$ 361</u>	<u>\$ (3,224)</u>	<u>\$ 171,507</u>

Unrealized loss on available-for-sale investment securities totaling \$2,863,000 were recorded, net of \$846,000 in tax benefits, as accumulated other comprehensive loss within shareholders' equity at December 31, 2018. During the nine months ended September 30, 2018 the Company sold eighteen available-for-sale investment securities for total proceeds of \$4,157,000 recording a \$8,000 loss on sale. The Company realized a gain on sale from eight of these securities totaling \$4,000 and a loss on sale on ten securities of \$12,000. No securities were sold during the three months ended September 30, 2018.

There were no transfers of available-for-sale investment securities during the nine months ended September 30, 2019 and twelve months ended December 31, 2018. There were no securities classified as held-to-maturity at September 30, 2019 or December 31, 2018.

Investment securities with unrealized losses at September 30, 2019 and December 31, 2018 are summarized and classified according to the duration of the loss period as follows, in thousands:

<u>September 30, 2019</u>	<u>Less than 12 Months</u>		<u>12 Months or More</u>		<u>Total</u>	
	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>
Debt securities:						
U.S. Government-sponsored agencies collateralized by mortgage obligations-residential	\$ 18,348	\$ 45	\$ 20,844	\$ 208	\$ 39,192	\$ 253
Obligations of states and political subdivisions	2,064	19	-	-	2,064	19
	<u>\$ 20,412</u>	<u>\$ 64</u>	<u>\$ 20,844</u>	<u>\$ 208</u>	<u>\$ 41,256</u>	<u>\$ 272</u>
<u>December 31, 2018</u>	<u>Less than 12 Months</u>		<u>12 Months or More</u>		<u>Total</u>	
	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>
Debt securities:						
U.S. Government-sponsored agencies collateralized by mortgage obligations-residential	\$ 26,478	\$ 269	\$ 77,476	\$ 2,352	\$ 103,954	\$ 2,621
Obligations of states and political subdivisions	19,270	284	5,672	319	24,942	603
	<u>\$ 45,748</u>	<u>\$ 553</u>	<u>\$ 83,148</u>	<u>\$ 2,671</u>	<u>\$ 128,896</u>	<u>\$ 3,224</u>

At September 30, 2019, the Company held 191 securities of which 50 were in a loss position. Of the securities in a loss position, 27 were in a loss position for less than twelve months. Of the 191 securities, 104 are U.S. Government-sponsored agencies collateralized by residential mortgage obligations and 87 were obligations of states and political subdivisions. The unrealized losses relate principally to market rate conditions. All of the securities continue to pay as scheduled. When analyzing an issuer's financial condition, management considers the length of time and extent to which the market value has been less than cost; the historical and implied volatility of the security; the financial condition of the issuer of the security; and the Company's intent and ability to hold the security to recovery. As of September 30, 2019, management does not have the intent to sell these securities nor does it believe it is more likely than not that it will be required to sell these securities before the recovery of its amortized cost basis. Based on the Company's evaluation of the above and other relevant factors, the Company does not believe the securities that are in an unrealized loss position as of September 30, 2019 are other than temporarily impaired.

The amortized cost and estimated fair value of investment securities at September 30, 2019 by contractual maturity are shown below, in thousands.

	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>
Within one year	\$ -	\$ -
After one year through five years	3,415	3,504
After five years through ten years	6,228	6,430
After ten years	21,855	22,876
Investment securities not due at a single maturity date:		
Government-sponsored mortgage-backed securities	134,990	136,706
	<u>\$ 166,488</u>	<u>\$ 169,516</u>

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.

Investment securities with amortized costs totaling \$84,586,000 and \$92,166,000 and estimated fair values totaling \$85,280,000 and \$90,122,000 at September 30, 2019 and December 31, 2018, respectively, were pledged to secure deposits and repurchase agreements.

4. LOANS AND THE ALLOWANCE FOR LOAN LOSSES

Outstanding loans are summarized below, in thousands:

	September 30, 2019	December 31, 2018
Commercial	\$ 45,818	\$ 49,563
Agricultural	77,529	69,160
Real estate – residential	14,960	15,900
Real estate – commercial	292,461	271,710
Real estate – construction and land development	42,727	40,161
Equity lines of credit	37,067	38,490
Auto	86,727	77,135
Other	4,467	4,080
Total loans	601,756	566,199
Deferred loan costs, net	3,471	3,257
Allowance for loan losses	(7,226)	(6,958)
Total net loans	\$ 598,001	\$ 562,498

Changes in the allowance for loan losses, in thousands, were as follows:

	September 30, 2019	December 31, 2018
Balance, beginning of period	\$ 6,958	\$ 6,669
Provision charged to operations	900	1,000
Losses charged to allowance	(874)	(1,191)
Recoveries	242	480
Balance, end of period	\$ 7,226	\$ 6,958

The recorded investment in impaired loans totaled \$2,642,000 and \$1,275,000 at September 30, 2019 and December 31, 2018, respectively. The Company had specific allowances for loan losses of \$235,000 on impaired loans of \$633,000 at September 30, 2019 as compared to specific allowances for loan losses of \$181,000 on impaired loans of \$424,000 at December 31, 2018. The balance of impaired loans in which no specific reserves were required totaled \$2,009,000 and \$851,000 at September 30, 2019 and December 31, 2018, respectively. The average recorded investment in impaired loans for the nine months ended September 30, 2019 and September 30, 2018 was \$1,771,000 and \$1,738,000, respectively. The Company recognized \$45,000 and \$56,000 in interest income for impaired loans during the nine months ended September 30, 2019 and 2018, respectively. No interest was recognized on nonaccrual loans accounted for on a cash basis during the nine months ended September 30, 2019 and 2018.

Included in impaired loans are troubled debt restructurings. A troubled debt restructuring is a formal restructure of a loan where the Company for economic or legal reasons related to the borrower's financial difficulties, grants a concession to the borrower. The concessions may be granted in various forms to include one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; or a permanent reduction of the recorded investment in the loan.

To determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Company's internal underwriting policy.

The carrying value of troubled debt restructurings at September 30, 2019 and December 31, 2018 was \$1,046,000 and \$1,080,000, respectively. The Company has allocated \$34,000 and \$53,000 of specific reserves on loans to customers whose loan terms have been modified in troubled debt restructurings as of September 30, 2019 and December 31, 2018, respectively. The Company has not committed to lend additional amounts on loans classified as troubled debt restructurings at September 30, 2019 and December 31, 2018.

There were no troubled debt restructurings that occurred during the nine months ending September 30, 2019 or September 30, 2018.

There were no troubled debt restructurings for which there was a payment default within twelve months following the modification during the nine months ended September 30, 2019 and 2018, respectively.

At September 30, 2019 and December 31, 2018, nonaccrual loans totaled \$2,598,000 and \$1,117,000, respectively. Interest foregone on nonaccrual loans totaled \$116,000 and \$36,000 for the nine months ended September 30, 2019 and 2018, respectively. Interest foregone on nonaccrual loans totaled \$47,000 and \$7,000 for the three months ended September 30, 2019 and 2018, respectively. There were no loans past due 90 days or more and on accrual status at September 30, 2019 and December 31, 2018.

Salaries and employee benefits totaling \$1,716,000 and \$1,937,000 have been deferred as loan origination costs during the nine months ended September 30, 2019 and 2018, respectively. Salaries and employee benefits totaling \$511,000 and \$703,000 have been deferred as loan origination costs during the three months ended September 30, 2019 and 2018, respectively.

The Company assigns a risk rating to all loans and periodically, but not less than annually, performs detailed reviews of all criticized and classified loans over \$100,000 to identify credit risks and to assess the overall collectability of the portfolio. These risk ratings are also subject to examination by independent specialists engaged by the Company and the Company's regulators. During these internal reviews, management monitors and analyzes the financial condition of borrowers and guarantors, trends in the industries in which borrowers operate and the fair values of collateral securing these loans. These credit quality indicators are used to assign a risk rating to each individual loan.

The risk ratings can be grouped into three major categories, defined as follows:

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

Substandard – A substandard loan is not adequately protected by the current sound worth and paying capacity of the borrower or the value of the collateral pledged, if any. Loans classified as substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. Well defined weaknesses include a project's lack of marketability, inadequate cash flow or collateral support, failure to complete construction on time or the project's failure to fulfill economic expectations. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

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

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

The following table shows the loan portfolio allocated by management's internal risk ratings at the dates indicated, in thousands:

September 30, 2019

Commercial Credit Exposure								
Credit Risk Profile by Internally Assigned Grade								
Grade:	Commercial	Agricultural	Real	Real	Real	Equity LOC	Total	
			Estate-Residential	Estate-Commercial	Estate-Construction			
Pass	\$ 45,233	\$ 74,739	\$ 14,649	\$ 286,504	\$ 42,641	\$ 36,111	\$ 499,877	
Special Mention	464	2,790	-	5,078	-	-	8,332	
Substandard	121	-	311	879	86	956	2,353	
Doubtful	-	-	-	-	-	-	-	
Total	\$ 45,818	\$ 77,529	\$ 14,960	\$ 292,461	\$ 42,727	\$ 37,067	\$ 510,562	

December 31, 2018

Commercial Credit Exposure								
Credit Risk Profile by Internally Assigned Grade								
Grade:	Commercial	Agricultural	Real	Real	Real	Equity LOC	Total	
			Estate-Residential	Estate-Commercial	Estate-Construction			
Pass	\$ 48,905	\$ 68,910	\$ 15,621	\$ 268,159	\$ 40,069	\$ 38,304	\$ 479,968	
Special Mention	481	250	124	3,420	-	-	4,275	
Substandard	177	-	155	131	92	186	741	
Doubtful	-	-	-	-	-	-	-	
Total	\$ 49,563	\$ 69,160	\$ 15,900	\$ 271,710	\$ 40,161	\$ 38,490	\$ 484,984	

Grade:	Consumer Credit Exposure			Consumer Credit Exposure		
	Credit Risk Profile			Credit Risk Profile		
	Based on Payment Activity			Based on Payment Activity		
	September 30, 2019			December 31, 2018		
	Auto	Other	Total	Auto	Other	Total
Performing	\$ 86,464	\$ 4,462	\$ 90,926	\$ 76,734	\$ 4,071	\$ 80,805
Non-performing	263	5	268	401	9	410
Total	\$ 86,727	\$ 4,467	\$ 91,194	\$ 77,135	\$ 4,080	\$ 81,215

balance: collectively evaluated for impairment	\$ 45,726	\$ 77,279	\$ 14,318	\$ 291,582	\$ 42,615	\$ 36,400	\$ 86,727	\$ 4,467	\$ 599,114
Ending balance	<u>\$ 45,818</u>	<u>\$ 77,529</u>	<u>\$ 14,960</u>	<u>\$ 292,461</u>	<u>\$ 42,727</u>	<u>\$ 37,067</u>	<u>\$ 86,727</u>	<u>\$ 4,467</u>	<u>\$ 601,756</u>

December 31, 2018:	Commercial	Agricultural	Real Estate- Residential	Real Estate- Commercial	Real Estate- Construction	Equity LOC	Auto	Other	Total
Allowance for Loan Losses									
Ending balance: individually evaluated for impairment	\$ 128	\$ -	41	\$ -	\$ 12	\$ -	\$ -	\$ -	\$ 181
Ending balance: collectively evaluated for impairment	\$ 786	\$ 538	\$ 173	\$ 2,686	\$ 746	\$ 464	\$ 1,289	\$ 95	\$ 6,777
Ending Balance	<u>\$ 914</u>	<u>\$ 538</u>	<u>\$ 214</u>	<u>\$ 2,686</u>	<u>\$ 758</u>	<u>\$ 464</u>	<u>\$ 1,289</u>	<u>\$ 95</u>	<u>\$ 6,958</u>
Loans									
Ending balance: individually evaluated for impairment	\$ 128	\$ 250	\$ 649	\$ 131	\$ 117	\$ -	\$ -	\$ -	\$ 1,275
Ending balance: collectively evaluated for impairment	49,435	68,910	15,251	271,579	40,044	38,490	77,135	4,080	564,924
Ending balance	<u>\$ 49,563</u>	<u>\$ 69,160</u>	<u>\$ 15,900</u>	<u>\$ 271,710</u>	<u>\$ 40,161</u>	<u>\$ 38,490</u>	<u>\$ 77,135</u>	<u>\$ 4,080</u>	<u>\$ 566,199</u>

The following table shows an aging analysis of the loan portfolio by the time past due, in thousands:

<u>September 30, 2019</u>	<u>30-89 Days Past Due</u>	<u>90 Days and Still Accruing</u>	<u>Nonaccrual</u>	<u>Total Past Due and Nonaccrual</u>	<u>Current</u>	<u>Total</u>
Commercial	\$ 142	\$ -	\$ 98	\$ 240	\$ 45,578	\$ 45,818
Agricultural	-	-	-	-	77,529	77,529
Real estate – residential	5	-	311	316	14,644	14,960
Real estate – commercial	63	-	879	942	291,519	292,461
Real estate - construction & land	-	-	86	86	42,641	42,727
Equity Lines of Credit	225	-	956	1,181	35,886	37,067
Auto	1,237	-	263	1,500	85,227	86,727
Other	40	-	5	45	4,422	4,467
Total	\$ 1,712	\$ -	\$ 2,598	\$ 4,310	\$ 597,446	\$ 601,756

<u>December 31, 2018</u>	<u>30-89 Days Past Due</u>	<u>90 Days and Still Accruing</u>	<u>Nonaccrual</u>	<u>Total Past Due and Nonaccrual</u>	<u>Current</u>	<u>Total</u>
Commercial	\$ 11	\$ -	\$ 144	\$ 155	\$ 49,408	\$ 49,563
Agricultural	-	-	-	-	69,160	69,160
Real estate – residential	154	-	155	309	15,591	15,900
Real estate – commercial	-	-	131	131	271,579	271,710
Real estate - construction & land	-	-	92	92	40,069	40,161
Equity Lines of Credit	596	-	186	782	37,708	38,490
Auto	1,725	-	401	2,126	75,009	77,135
Other	85	-	8	93	3,987	4,080
Total	\$ 2,571	\$ -	\$ 1,117	\$ 3,688	\$ 562,511	\$ 566,199

The following tables show information related to impaired loans at September 30, 2019, in thousands:

As of September 30, 2019:	<u>Recorded Investment</u>	<u>Unpaid Principal Balance</u>	<u>Related Allowance</u>	<u>Average Recorded Investment</u>	<u>Interest Income Recognized</u>
With no related allowance recorded:					
Commercial	\$ -	\$ -	\$ -	\$ -	\$ -
Agricultural	250	250	-	250	13
Real estate – residential	464	477	-	375	22
Real estate – commercial	628	641	-	481	-
Real estate – construction & land	-	-	-	-	-
Equity Lines of Credit	667	691	-	272	-
Auto	-	-	-	-	-
Other	-	-	-	-	-
With an allowance recorded:					
Commercial	\$ 92	\$ 92	\$ 83	\$ 2	\$ -
Agricultural	-	-	-	-	-
Real estate – residential	178	178	28	178	5
Real estate – commercial	251	257	118	101	-
Real estate – construction & land	112	112	6	112	5
Equity Lines of Credit	-	-	-	-	-
Auto	-	-	-	-	-
Other	-	-	-	-	-
Total:					
Commercial	\$ 92	\$ 92	\$ 83	\$ 2	\$ -
Agricultural	250	250	-	250	13
Real estate – residential	642	655	28	553	27
Real estate – commercial	879	898	118	582	-
Real estate – construction & land	112	112	6	112	5
Equity Lines of Credit	667	691	-	272	-
Auto	-	-	-	-	-
Other	-	-	-	-	-
Total	<u>\$ 2,642</u>	<u>\$ 2,698</u>	<u>\$ 235</u>	<u>\$ 1,771</u>	<u>\$ 45</u>

The following tables show information related to impaired loans at December 31, 2018, in thousands:

As of December 31, 2018:	<u>Recorded Investment</u>	<u>Unpaid Principal Balance</u>	<u>Related Allowance</u>	<u>Average Recorded Investment</u>	<u>Interest Income Recognized</u>
With no related allowance recorded:					
Commercial	\$ -	\$ -	\$ -	\$ -	\$ -
Agricultural	250	250	-	252	19
Real estate – residential	470	481	-	470	38
Real estate – commercial	131	144	-	136	-
Real estate – construction & land	-	-	-	-	-
Equity Lines of Credit	-	-	-	-	-
Auto	-	-	-	-	-
Other	-	-	-	-	-
With an allowance recorded:					
Commercial	\$ 128	\$ 128	\$ 128	\$ 1	\$ -
Agricultural	-	-	-	-	-
Real estate – residential	179	179	41	181	7
Real estate – commercial	-	-	-	-	-
Real estate – construction & land	117	117	12	120	7
Equity Lines of Credit	-	-	-	-	-
Auto	-	-	-	-	-
Other	-	-	-	-	-
Total:					
Commercial	\$ 128	\$ 128	\$ 128	\$ 1	\$ -
Agricultural	250	250	-	252	19
Real estate – residential	649	660	41	651	45
Real estate – commercial	131	144	-	136	-
Real estate – construction & land	117	117	12	120	7
Equity Lines of Credit	-	-	-	-	-
Auto	-	-	-	-	-
Other	-	-	-	-	-
Total	<u>\$ 1,275</u>	<u>\$ 1,299</u>	<u>\$ 181</u>	<u>\$ 1,160</u>	<u>\$ 71</u>

5. COMMITMENTS AND CONTINGENCIES

The Company is party to claims and legal proceedings arising in the ordinary course of business. In the opinion of the Company's management, the amount of ultimate liability with respect to such proceedings will not have a material adverse effect on the financial condition or result of operations of the Company taken as a whole.

In the normal course of business, there are various outstanding commitments to extend credit, which are not reflected in the financial statements, including loan commitments of \$104.9 million and \$126.9 million and stand-by letters of credit of \$431 thousand and \$417 thousand at September 30, 2019 and December 31, 2018, respectively.

Of the loan commitments outstanding at September 30, 2019, \$8.5 million are real estate construction loan commitments that are expected to fund within the next twelve months. The remaining commitments primarily relate to revolving lines of credit or other commercial loans, and many of these are expected to expire without being drawn upon. Therefore, the total commitments do not necessarily represent future cash requirements. Each loan commitment and the amount and type of collateral obtained, if any, are evaluated on an individual basis. Collateral held varies, but may include real property, bank deposits, debt or equity securities or business assets.

Stand-by letters of credit are conditional commitments written to guarantee the performance of a customer to a third party. These guarantees are primarily related to the purchases of inventory by commercial customers and are typically short-term in nature. Credit risk is similar to that involved in extending loan commitments to customers and accordingly, evaluation and collateral requirements similar to those for loan commitments are used. The deferred liability related to the Company's stand-by letters of credit was not significant at September 30, 2019 or December 31, 2018.

6. LEASES

The Company leases four lending offices, three branch offices, one administrative office and two standalone ATM locations. Two of the branch office leases have options to renew. The exercise of lease renewal options is at our sole discretion; therefore, are not included in our Right of Use (ROU) assets and lease liabilities as they are not reasonably certain of exercise. We regularly evaluate the renewal options and when they are reasonably certain of exercise, we include the renewal period in our lease term. We have elected the practical expedient to exclude short-term leases from our ROU assets and lease liabilities. The three branch leases and two of the lending office leases are classified as operating leases while the remaining leases are all short-term leases. The Company adopted ASU No. 2016-02 on January 1, 2019 and recorded \$565,000 in ROU assets and lease liabilities on adoption.

As our leases do not provide an implicit rate, we use our incremental borrowing rate based on the information available at the lease commencement date in determining the present value of the lease payments. The Company's weighted average incremental borrowing rate used in the calculation of the right-of-use assets and lease liabilities was estimated at 5%. At September 30, 2019 the ROU assets and lease liabilities included on the condensed consolidated balance sheet in other assets and other liabilities, respectively totaled \$328,000 consisting of total undiscounted remaining cash flows of \$347,000 less a present value discount of \$19,000.

The following table presents a maturity analysis of the operating lease liability at September 30, 2019, in thousands:

	Maturities of Lease Liabilities
Three months ended December 31, 2019	\$ 62
Year ended December 31, 2020	163
Year ended December 31, 2021	63
Year ended December 31, 2022	59
	<u>347</u>
Less: Present value discount	(19)
Lease Liability September 30, 2019	<u>\$ 328</u>

The weighted-average remaining lease term is 2.2 years.

Total lease costs for the nine and three months ended September 30, 2019 were as follows, in thousands:

	Nine Months ended September 30, 2019	Three Months ended September 30, 2019
Operating leases	\$ 247	\$ 71
Short-term leases	63	37
Variable lease expense	32	10
Total lease expense	<u>\$ 342</u>	<u>\$ 118</u>

Variable lease expense consists primarily of maintenance expense paid to maintain common areas. Rent expense for the nine and three months ended September 30, 2018, prior to the adoption of ASU 2016-02, was \$275,000 and \$92,000, respectively, which includes \$28,000 and \$10,000, respectively, related to variable lease expense.

Cash paid on operating leases was \$247,000 and \$71,000, respectively for the nine and three months ended September 30, 2019.

The following table presents future minimum rental payments under leases with terms in excess of one year as of December 31, 2018 presented in accordance with ASC Topic 840, "Leases":

Year Ending December 31,	
2019	\$ 248,000
2020	163,000
2021	63,000
2022	59,000
2023	-
	<u>\$ 533,000</u>

7. EARNINGS PER SHARE

Basic earnings per share is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for the period. 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 shares in the earnings of the Company. The treasury stock method has been applied to determine the dilutive effect of stock options in computing diluted earnings per share.

(In thousands, except per share data)	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	2018	2019	2018
Net Income:				
Net income	\$ 4,002	\$ 3,696	\$ 11,630	\$ 10,422
Earnings Per Share:				
Basic earnings per share	\$ 0.78	\$ 0.72	\$ 2.26	\$ 2.04
Diluted earnings per share	\$ 0.77	\$ 0.71	\$ 2.22	\$ 2.00
Weighted Average Number of Shares Outstanding:				
Basic shares	5,160	5,122	5,153	5,100
Diluted shares	5,227	5,225	5,227	5,219

Shares of common stock issuable under stock options for which the exercise prices were greater than the average market prices were not included in the computation of diluted earnings per share due to their antidilutive effect. Stock options not included in the computation of diluted earnings per share, due to shares not being in-the-money and having an antidilutive effect, were approximately 71,000 and 71,000 for the three-month periods ended September 30, 2019 and 2018, respectively. Stock options not included in the computation of diluted earnings per share, due to shares not being in-the-money and having an antidilutive effect, were approximately 71,000 and 71,000 for the nine-month periods ended September 30, 2019 and 2018, respectively.

8. STOCK-BASED COMPENSATION

In 2001, the Company established a Stock Option Plan for which no shares of common stock remain reserved for issuance to employees and directors and no shares are available for future grants as of September 30, 2019.

As of September 30, 2019, all remaining shares in this plan have vested and no compensation cost remains unrecognized.

A summary of the activity within the 2001 Stock Option Plan follows:

	Shares	Weighted Average Exercise Price
Options outstanding at January 1, 2019	6,193	\$ 2.95
Options exercised	(6,193)	2.95
Options outstanding at September 30, 2019	-	\$ -

In May 2013, the Company established the 2013 Stock Option Plan for which 415,085 shares of common stock are reserved and 238,500 shares are available for future grants as of September 30, 2019. The 2013 Plan requires that the option price may not be less than the fair market value of the stock at the date the option is granted, and that the stock must be paid in full at the time the option is exercised. Payment in full for the option price must be made in cash, with Company common stock previously acquired by the optionee and held by the optionee for a period of at least nine months, in options of the Optionee that are fully vested and exercisable or in any combination of the foregoing. The options expire on dates determined by the Board of Directors, but not later than ten years from the date of grant.

No options were granted during the nine months ended September 30, 2019. During the nine months ended September 30, 2018 the Company granted options to purchase 76,000 shares of common stock.

The fair value of each option was estimated on the date of grant using the following assumptions.

	2018
Expected life of stock options (in years)	5.1
Risk free interest rate	2.38%
Volatility	30.4%
Dividend yields	1.39%
Weighted-average fair value of options granted during the three months ended March 31, 2018	\$ 6.54

The Company determines the fair value of options on the date of grant using a Black-Scholes-Merton option pricing model that uses assumptions based on expected option life, expected stock volatility and the risk-free interest rate. The expected volatility assumptions used by the Company are based on the historical volatility of the Company's common stock over the most recent period commensurate with the estimated expected life of the Company's stock options. The Company bases its expected life assumption on its historical experience and on the terms and conditions of the stock options it grants to employees. The risk-free rate is based on the U.S. Treasury yield curve for the periods within the contractual life of the options in effect at the time of the grant.

A summary of the activity within the 2013 Plan follows:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term in Years	Intrinsic Value
Options outstanding at January 1, 2019	196,500	\$ 13.84		
Options cancelled	(2,400)	\$ 8.75		
Options exercised	(17,515)	7.24		
Options outstanding at September 30, 2019	<u>176,585</u>	\$ 14.57	4.8	\$ 1,292,000
Options exercisable at September 30, 2019	102,860	\$ 10.62	4.1	\$ 1,059,000
Expected to vest after September 30, 2019	65,328	\$ 20.07	5.8	\$ 233,000

As of September 30, 2019, there was \$307,000 of total unrecognized compensation cost related to non-vested, share-based compensation. That cost is expected to be recognized over a weighted average period of 2.1 years.

The total fair value of options vested during the nine months ended September 30, 2019 and 2018 was \$197,000 and \$150,000, respectively. The total intrinsic value of options at time of exercise was \$311,000 and \$1,261,000 for the nine months ended September 30, 2019 and 2018, respectively.

Compensation cost related to stock options recognized in operating results under the stock option plans was \$150,000 and \$148,000 for the nine months ended September 30, 2019 and 2018, respectively. The associated income tax benefit recognized was \$10,000 for the nine months ended September 30, 2019 and September 30, 2018. Compensation cost related to stock options recognized in operating results under the stock option plans was \$50,000 for the three months ended September 30, 2019 and 2018. The associated income tax benefit recognized was \$3,000 for the three months ended September 30, 2019 and September 30, 2018.

Cash received from option exercises under the plans for the nine months ended September 30, 2019 and 2018 were \$103,000 and \$291,000, respectively. The tax benefit realized for the tax deductions from option exercise totaled \$24,000 and \$99,000 for the nine months ended September 30, 2019 and 2018, respectively.

9. INCOME TAXES

The Company files its income taxes on a consolidated basis with its subsidiary. Income tax expense is the total of current year income tax due or refundable and the change in deferred tax assets and liabilities.

Deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the reported amount of assets and liabilities and their tax bases. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. A valuation allowance is recognized if, based on the weight of available evidence management believes it is more likely than not that some portion or all of the deferred tax assets will not be realized. On the consolidated balance sheet, net deferred tax assets are included in accrued interest receivable and other assets.

When tax returns are filed, it is highly certain that some positions taken would be sustained upon examination by the taxing authorities, while others are subject to uncertainty about the merits of the position taken or the amount of the position that would be ultimately sustained. The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more likely than not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination.

Interest expense and penalties associated with unrecognized tax benefits, if any, are classified as income tax expense in the consolidated statements of income. There have been no significant changes to unrecognized tax benefits or accrued interest and penalties for the nine months ended September 30, 2019.

10. FAIR VALUE MEASUREMENT

The Company measures fair value under the fair value hierarchy described below.

Level 1: Quoted prices for identical instruments traded in active exchange markets.

Level 2: Quoted prices (unadjusted) 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 or can be corroborated by observable market data.

Level 3: Model based techniques that use one significant assumption not observable in the market. These unobservable assumptions reflect the Company's estimates of assumptions that market participants would use on pricing the asset or liability. Valuation techniques include management judgment and estimation which may be significant.

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 Company'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.

Management monitors the availability of observable market data to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period.

Management evaluates the significance of transfers between levels based upon the nature of the financial instrument and size of the transfer relative to total assets, total liabilities or total earnings.

Fair Value of Financial Instruments

The carrying amounts and estimated fair values of financial instruments, at September 30, 2019 follows, in thousands:

	Carrying Value	Fair Value Measurements at September 30, 2019 Using:			Total Fair Value
		Level 1	Level 2	Level 3	
Financial assets:					
Cash and cash equivalents	\$ 77,880	\$ 77,880	\$ -	\$ -	\$ 77,880
Investment securities	169,516	-	169,516	-	169,516
Loans, net	598,001	-	-	631,755	631,755
FHLB stock	3,517	-	-	-	N/A
Accrued interest receivable	3,205	13	594	2,598	3,205
Financial liabilities:					
Deposits	776,183	733,927	42,266	-	776,193
Repurchase agreements	13,389	-	13,389	-	13,389
Junior subordinated deferrable interest debentures	10,310	-	-	7,473	7,473
Accrued interest payable	94	12	60	22	94

The carrying amounts and estimated fair values of financial instruments, at December 31, 2018 follows, in thousands:

	Carrying Value	Fair Value Measurements at December 31, 2018 Using:			Total Fair Value
		Level 1	Level 2	Level 3	
Financial assets:					
Cash and cash equivalents	\$ 46,686	\$ 46,686	\$ -	\$ -	\$ 46,686
Investment securities	171,507	-	171,507	-	171,507
Loans, net	562,498	-	-	580,396	580,396
FHLB stock	3,027	-	-	-	N/A
Accrued interest receivable	3,345	22	685	2,638	3,345
Financial liabilities:					
Deposits	726,565	669,599	57,050	-	726,649
Repurchase agreements	13,058	-	13,058	-	13,058
Junior subordinated deferrable interest debentures	10,310	-	-	8,092	8,092
Accrued interest payable	88	11	52	25	88

Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding current economic conditions, risk characteristics of various financial instruments and other factors. Those estimates that are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision are included in Level 3. Changes in assumptions could significantly affect the fair values presented.

These estimates do not reflect any premium or discount that could result from offering the Company's entire holdings of a particular financial instrument for sale at one time, nor do they attempt to estimate the value of anticipated future business related to the instruments. In addition, the tax ramifications related to the realization of unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of these estimates.

The following tables present information about the Company's assets and liabilities measured at fair value on a recurring and non-recurring basis as of September 30, 2019 and December 31, 2018, and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value:

Assets and liabilities measured at fair value on a recurring basis at September 30, 2019 are summarized below, in thousands:

	Fair Value Measurements at September 30, 2019 Using			
	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
U.S. Government-sponsored agencies collateralized by mortgage obligations-residential	\$ 136,706	\$ -	\$ 136,706	\$ -
Obligations of states and political subdivisions	32,810		32,810	
	<u>\$ 169,516</u>	<u>\$ -</u>	<u>\$ 169,516</u>	<u>\$ -</u>

Assets and liabilities measured at fair value on a recurring basis at December 31, 2018 are summarized below, in thousands:

	Fair Value Measurements at December 31, 2018 Using			
	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
U.S. Government-sponsored agencies collateralized by mortgage obligations-residential	\$ 132,678	\$ -	\$ 132,678	\$ -
Obligations of states and political subdivisions	38,829		38,829	
	<u>\$ 171,507</u>	<u>\$ -</u>	<u>\$ 171,507</u>	<u>\$ -</u>

The fair value of securities available-for-sale equals quoted market price, if available. If quoted market prices are not available, fair value is determined using quoted market prices for similar securities or matrix pricing. There were no changes in the valuation techniques used during 2019 or 2018. Transfers between hierarchy measurement levels are recognized by the Company as of the beginning of the reporting period. Changes in fair market value are recorded in other comprehensive income.

Assets and liabilities measured at fair value on a non-recurring basis at September 30, 2019 are summarized below, in thousands:

	Fair Value Measurements at September 30, 2019 Using				Total (Losses) Nine Months Ended September 30, 2019
	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets:					
Impaired loans:					
Real estate – commercial	\$ 133	\$ -	\$ -	\$ 133	\$ (118)
Other real estate:					
Real estate – residential	292	-	-	292	-
Real estate – commercial	347	-	-	347	-
Construction and land	455	-	-	455	-
Total other real estate	1,094	-	-	1,094	-
Total	\$ 1,643	\$ -	\$ -	\$ 1,643	\$ (118)

Assets and liabilities measured at fair value on a non-recurring basis at December 31, 2018 are summarized below, in thousands:

	Fair Value Measurements at December 31, 2018 Using				Total (Losses) Nine Months Ended September 30, 2018
	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets:					
Impaired loans:					
Construction and land	\$ -	\$ -	\$ -	\$ -	\$ (25)
Other real estate:					
Real estate – residential	368	-	-	368	(38)
Real estate – commercial	347	-	-	347	-
Construction and land	455	-	-	455	-
Total other real estate	1,170	-	-	1,170	(38)
Total	\$ 1,170	\$ -	\$ -	\$ 1,170	\$ (63)

The Company has no liabilities which are reported at fair value.

The following methods were used to estimate fair value.

Collateral-Dependent Impaired Loans: The Bank does not record loans at fair value on a recurring basis. However, from time to time, fair value adjustments are recorded on these loans to reflect partial write-downs, through charge-offs or specific reserve allowances, that are based on fair value estimates of the underlying collateral. The fair value estimates for collateral-dependent impaired loans are generally based on recent real estate appraisals or broker opinions, obtained from independent third parties, which are frequently adjusted by management to reflect current conditions and estimated selling costs (Level 3). Net losses of (\$118,000) and (\$63,000) represent impairment charges recognized during the nine months ended September 30, 2019 and 2018, respectively, related to the above impaired loans.

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

Appraisals for both collateral-dependent impaired loans and other real estate are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Company. Once received, a member of the Loan Administration Department reviews the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison with independent data sources such as recent market data or industry-wide statistics. On a quarterly basis, the Company compares the actual selling price of similar collateral that has been liquidated to the most recent appraised value for unsold properties to determine what additional adjustment, if any, should be made to the appraisal value to arrive at fair value. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available.

The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at September 30, 2019 and December 31, 2018 (dollars in thousands):

Description	Fair Value 9/30/2019	Fair Value 12/31/2018	Valuation Technique	Significant Unobservable Input	Range (Weighted Average)		Range (Weighted Average)	
					9/30/2019	12/31/2018	9/30/2019	12/31/2018
Impaired Loans:								
RE – Commercial	\$ 133	\$ -	Third Party appraisals	Management Adjustments to Reflect Current Conditions and Selling Costs	10%	(10%)	N/A	
Other Real Estate:								
RE – Residential	\$ 292	\$ 368	Third Party appraisals	Management Adjustments to Reflect Current Conditions and Selling Costs	10%	(10%)	10% - 34%	(16%)
RE – Commercial	\$ 347	\$ 347	Third Party appraisals	Management Adjustments to Reflect Current Conditions and Selling Costs	16% - 17%	(16%)	16% - 17%	(16%)
Construction and Land	\$ 455	\$ 455	Third Party appraisals	Management Adjustments to Reflect Current Conditions and Selling Costs	10% - 51%	(24%)	10% - 51%	(24%)

PART I – FINANCIAL INFORMATION

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Certain matters discussed in this Quarterly Report are forward-looking statements that are subject to risks and uncertainties that could cause actual results to differ materially from those projected in the forward-looking statements. Such risks and uncertainties include, among others, (1) significant increases in competitive pressures in the financial services industry; (2) changes in the interest rate environment resulting in reduced margins; (3) general economic conditions, either nationally or regionally, maybe less favorable than expected, resulting in, among other things, a deterioration in credit quality; (4) changes in regulatory environment; (5) loss of key personnel; (6) fluctuations in the real estate market; (7) changes in business conditions and inflation; (8) operational risks including data processing systems failures or fraud; and (9) changes in securities markets. Therefore, the information set forth herein should be carefully considered when evaluating the business prospects of Plumas Bancorp (the "Company").

When the Company uses in this Quarterly Report the words "anticipate", "estimate", "expect", "project", "intend", "commit", "believe" and similar expressions, the Company intends to identify forward-looking statements. Such statements are not guarantees of performance and are subject to certain risks, uncertainties and assumptions, including those described in this Quarterly Report. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated, expected, projected, intended, committed or believed. The future results and stockholder values of the Company may differ materially from those expressed in these forward-looking statements. Many of the factors that will determine these results and values are beyond the Company's ability to control or predict. For those statements, the Company claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

INTRODUCTION

The following discussion and analysis sets forth certain statistical information relating to the Company as of September 30, 2019 and December 31, 2018 and for the three- and nine-month periods ended September 30, 2019 and 2018. This discussion should be read in conjunction with the condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q and the consolidated financial statements and notes thereto included in Plumas Bancorp's Annual Report filed on Form 10-K for the year ended December 31, 2018.

Plumas Bancorp trades on The NASDAQ Capital Market under the ticker symbol "PLBC".

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

There have been no changes to the Company's critical accounting policies from those disclosed in the Company's 2018 Annual Report to Shareholders on Form 10-K.

This discussion should be read in conjunction with our unaudited condensed consolidated financial statements, including the notes thereto, appearing elsewhere in this report.

OVERVIEW - NINE MONTHS ENDED SEPTEMBER 30, 2019

Net income increased by \$1.2 million from \$10.4 million during the nine months ended September 30, 2018 to \$11.6 million during the current nine-month period. Earnings benefited from an increase of \$4.0 million in net interest income partially offset by a decline in non-interest income of \$919 thousand and increases in the provision for loan losses of \$100 thousand, non-interest expense of \$1.2 million and \$572 thousand in income tax expense. Diluted earnings per share increased to \$2.22 for the nine months ended September 30, 2019 compared to \$2.00 during the nine months ended September 30, 2018.

Total assets at September 30, 2019 were \$888 million, an increase of \$64 million from \$824 million at December 31, 2018. The increase in assets includes increases of \$35.5 million in net loans, \$31.2 million in cash and cash equivalents, and \$2.0 million in investment securities. At September 30, 2019, cash and cash equivalents totaled \$77.9 million, net loans were \$598.0 million and investment securities totaled \$169.5 million.

Total deposits increased by \$49.6 million from \$727 million at December 31, 2018 to \$776 million at September 30, 2019. Shareholders' equity increased by \$14.9 million from \$66.9 million at December 31, 2018 to \$81.8 million at September 30, 2019.

The annualized return on average assets was 1.84% for the nine months ended September 30, 2019 and 1.87% for the nine months ended September 30, 2018. The annualized return on average equity decreased from 23.7% during the first nine months of 2018 to 20.8% during the current nine-month period.

RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2019

Net interest income before provision for loan losses. Net interest income for the nine months ended September 30, 2019 was \$28.1 million, an increase of \$4.0 million from the \$24.1 million earned during the same period in 2018. The increase in net interest income includes an increase of \$4.5 million in interest income partially offset by an increase of \$503 thousand in interest expense. Net interest margin, which benefited from an 18 basis points increase in average yield on interest-earning assets, increased 12 basis points to 4.80%, up from 4.68% for the same period in 2018.

Interest income increased by 18% to \$29.5 million for the nine months ended September 30, 2019, up from \$25.0 million during the same period in 2018. Related to increases in average loan balances and loan yield, interest and fees on loans increased by \$4.0 million to \$25.7 million for the nine months ended September 30, 2019; compared to \$21.7 million during the first nine months of 2018. The Company's average loan balances were \$584 million for the nine months ended September 30, 2019, up \$77 million, or 15%, from \$507 million for the same period in 2018. The average rate earned on the Company's loan balances increased by 16 basis points to 5.88% during the first nine months of 2019 compared to 5.72% during the first nine months of 2018. We attribute this increase in yield primarily to an increase in the average prime interest rate during this period. Loan pricing continues to be extremely competitive in our service area.

The following table compares loan balances by type at September 30, 2019 and 2018.

(dollars in thousands)	Balance at End	Percent of	Balance at End	Percent of
	of Period	Loans in Each	of Period	Loans in Each
	09/30/19	Category to	09/30/18	Category to
		Total Loans		Total Loans
		09/30/19		09/30/18
Commercial	\$ 45,818	7.6%	\$ 46,762	8.7%
Agricultural	77,529	12.9%	70,917	13.1%
Real estate – residential	14,960	2.5%	15,674	2.9%
Real estate – commercial	292,461	48.6%	253,154	46.9%
Real estate – construction & land	42,727	7.1%	38,454	7.1%
Equity Lines of Credit	37,067	6.2%	39,165	7.3%
Auto	86,727	14.4%	71,875	13.3%
Other	4,467	0.7%	3,846	0.7%
Total Gross Loans	\$ 601,756	100%	\$ 539,847	100%

Interest on investment securities increased by \$480 thousand related to an increase in yield of 4 basis points, from 2.56% during the nine months ended September 30, 2018 to 2.60% during the nine months ended September 30, 2019, and an increase in average balance from \$150.3 million during the nine months ended September 30, 2018 to \$172.7 million during the nine months ended September 30, 2019. We attribute the increase in yield during the current period primarily to market conditions. See "Investment Portfolio and Federal Funds Sold" for additional information related to the Company's investment portfolio.

Interest earned on other interest earning assets increased by \$43 thousand to \$445 thousand during the nine months ended September 30, 2019 as an increase in yield of 57 basis points from 1.70% during the nine months ended September 30, 2018 to 2.27% during the current nine-month period was partially offset by a decrease in average balances from \$31.6 million during the nine months ended September 30, 2018 to \$26.2 million during the current nine month period. Other interest earning assets mostly related to balances held at the Federal Reserve Bank of San Francisco.

Interest expense on deposits increased by \$461 thousand from \$462 thousand for the nine months ended September 30, 2018, to \$923 thousand during the current period. This increase mostly relates to an increase in interest expense on money market accounts and time deposits related to the purchase of our Carson City, Nevada branch on October 26, 2018. The average rate paid on the Carson City money market and time deposits exceeds that which Plumas Bank pays in other markets. To date we have maintained the rates on the money market accounts at this branch but have experienced a decrease in deposits mostly related to the maturity of time deposits which were yielding significantly higher rates than our offering rates. In total, time deposits at the Carson City Branch declined by \$12.4 million from \$18.5 million on acquisition to \$6.1 million at September 30, 2019. We expect some additionally runoff on these accounts as they reprice over time. During the nine months ended September 30, 2019 money market accounts housed at our Carson City branch averaged \$15.1 million and time deposits at this branch averaged \$13.4 million. Interest expense on money market accounts increased by \$231 thousand to \$304 thousand related to an increase in average rate paid of 32 basis points and an increase in average balances of \$19.0 million from \$66.6 million during the nine months ended September 30, 2018 to \$85.6 million during the nine-month period. Interest on time deposits increased by \$222 thousand from \$99 thousand during the nine months ended September 30, 2018 to \$321 thousand during the 2019 nine month period. During this same period average time deposits increased by \$9.5 million and the average rate paid on time deposit increased by 52 basis points.

Interest expense on other interest-bearing liabilities increased by \$42 thousand from \$375 thousand during the nine months ended September 30, 2018 to \$417 thousand during the current period mostly related to an increase in rate paid on junior subordinated debentures. Interest on the debentures, which totaled \$406 thousand during the nine months ended September 30, 2019 and \$370 thousand during the nine months ended September 30, 2018, fluctuates with changes in the 3-month London Interbank Offered Rate (LIBOR).

The following table presents for the nine-month periods indicated the distribution of consolidated average assets, liabilities and shareholders' equity. It also presents the amounts of interest income from interest-earning assets and the resultant annualized yields, as well as the amounts of interest expense on interest-bearing liabilities and the resultant cost expressed in both dollars and annualized rate percentages. Average balances are based on daily averages. Nonaccrual loans are included in the calculation of average loans while nonaccrued interest thereon is excluded from the computation of yields earned:

	For the Nine Months Ended September 30, 2019			For the Nine Months Ended September 30, 2018		
	Average Balance (in thousands)	Interest (in thousands)	Yield/ Rate	Average Balance (in thousands)	Interest (in thousands)	Yield/ Rate
Interest-earning assets:						
Loans (1) (2) (3)	\$ 583,792	\$ 25,655	5.88%	\$ 506,592	\$ 21,680	5.72%
Investment securities (1)	172,671	3,353	2.60%	150,285	2,873	2.56%
Interest-bearing deposits	26,223	445	2.27%	31,581	402	1.70%
Total interest-earning assets	782,686	29,453	5.03%	688,458	24,955	4.85%
Cash and due from banks	21,848			21,306		
Other assets	39,878			37,323		
Total assets	\$ 844,412			\$ 747,087		
Interest-bearing liabilities:						
NOW deposits	\$ 105,538	75	0.10%	\$ 102,939	72	0.09%
Money market deposits	85,634	304	0.47%	66,557	73	0.15%
Savings deposits	179,174	223	0.17%	175,739	218	0.17%
Time deposits	51,633	321	0.83%	42,098	99	0.31%
Total deposits	421,979	923	0.29%	387,333	462	0.16%
Junior subordinated debentures	10,310	406	5.26%	10,310	370	4.80%
Other interest-bearing liabilities	10,696	11	0.14%	7,935	5	0.08%
Total interest-bearing liabilities	442,985	1,340	0.40%	405,578	837	0.28%
Non-interest-bearing deposits	319,957			275,953		
Other liabilities	6,878			6,704		
Shareholders' equity	74,592			58,852		
Total liabilities & equity	\$ 844,412			\$ 747,087		
Cost of funding interest-earning assets (4)			0.23%			0.17%
Net interest income and margin (5)		\$ 28,113	4.80%		\$ 24,118	4.68%

(1) Not computed on a tax-equivalent basis.

(2) Average nonaccrual loan balances of \$1.8 million for 2019 and \$1.0 million for 2018 are included in average loan balances for computational purposes.

(3) Net costs included in loan interest income for the nine-month periods ended September 30, 2019 and 2018 were \$491,000 and \$247,000, respectively.

(4) Total annualized interest expense divided by the average balance of total earning assets.

(5) Annualized net interest income divided by the average balance of total earning assets.

The following table sets forth changes in interest income and interest expense for the three-month periods indicated. It includes the amount of change attributable to variances in volume, rates and the combination of volume and rates based on the relative changes of volume and rates:

2019 over 2018 change in net interest income for the nine months ended September 30,				
(in thousands)				
Volume (1)	Rate (2)	Mix (3)	Total	
Interest-earning assets:				
Loans	\$ 3,304	\$ 582	\$ 89	\$ 3,975
Investment securities	428	45	7	480
Interest bearing deposits	(68)	134	(23)	43
Total interest income	3,664	761	73	4,498
Interest-bearing liabilities:				
NOW deposits	2	1	-	3
Money market deposits	21	163	47	231
Savings deposits	4	1	-	5
Time deposits	22	163	37	222
Junior subordinated debentures	-	36	-	36
Other	2	3	1	6
Total interest expense	51	367	85	503
Net interest income	\$ 3,613	\$ 394	\$ (12)	\$ 3,995

- (1) The volume change in net interest income represents the change in average balance multiplied by the previous quarter's rate.
- (2) The rate change in net interest income represents the change in rate multiplied by the previous quarter's average balance.
- (3) The mix change in net interest income represents the change in average balance multiplied by the change in rate.

Provision for loan losses. During the nine months ended September 30, 2019 and 2018 we recorded a provision for loan losses of \$900 thousand and \$800 thousand, respectively. See "Analysis of Asset Quality and Allowance for Loan Losses" for a discussion of loan quality trends and the provision for loan losses.

The allowance for loan losses is maintained at a level that management believes will be appropriate to absorb probable incurred losses on existing loans based on an evaluation of the collectability of the loans and prior loan loss experience. The evaluations take into consideration such factors as changes in the nature and volume of the portfolio, overall portfolio quality, review of specific problem loans, and current economic conditions that may affect the borrower's ability to repay their loan. The allowance for loan losses is based on estimates, and ultimate losses may vary from the current estimates. These estimates are reviewed not less than quarterly and, as adjustments become necessary, they are reported in earnings in the periods in which they become known.

Based on information currently available, management believes that the allowance for loan losses is appropriate to absorb probable incurred losses in the loan portfolio. However, no assurance can be given that the Company may not sustain charge-offs which are in excess of the allowance in any given period.

Non-interest income. During the nine months ended September 30, 2019, non-interest income totaled \$6.1 million, a decrease of \$919 thousand from the nine months ended September 30, 2018. The largest component of this decrease was a decline of \$975 thousand in gains on sale of SBA loans from \$1.8 million during the nine months ended September 30, 2018 to \$788 thousand during the current period. Proceeds from SBA loan sales totaled \$17.9 million during the current nine-month period and \$37.3 million during the nine months ended September 30, 2018. Loans originated for sale totaled \$16.8 million during the nine months ended September 30, 2019 and \$34.3 million during the nine months ended September 30, 2018. We attribute some of the decline in originations to the government shutdown during the first quarter of 2019. During the shutdown we were unable to provide SBA guaranteed loans. In addition, higher market rates have resulted in a decrease in demand; competition in the SBA lending market remains intense. Partially offsetting the decline in gain on sale of SBA loans were increases of \$77 thousand in service charge income, \$120 thousand in interchange income, \$28 thousand in gain on sale of securities and an increase in various other categories of non-interest income totaling \$66 thousand. Non-interest income benefited during the 2018 period from a \$209 thousand gain recorded upon the prospective adoption of a newly effective accounting pronouncement impacting the measurement of equity securities, which in our case consists of stock in our correspondent banks, without a readily determinable fair market value. No gain or loss was recorded on these securities during the current period.

The following table describes the components of non-interest income for the nine-month periods ended September 30, 2019 and 2018 (dollars in thousands):

	For the Nine Months Ended September 30,			
	2019	2018	Dollar Change	Percentage Change
Service charges on deposit accounts	1,996	1,919	77	4.0%
Interchange income	1,739	1,619	120	7.4%
Gain on sale of loans, net	788	1,763	(975)	-55.3%
Loan servicing fees	561	587	(26)	-4.4%
Earnings on life insurance policies	246	246	-	-%
Gain (loss) on sale of investments	20	(8)	28	350.0%
Gain on equity securities ⁽¹⁾	-	209	(209)	-100.0%
Other	771	705	66	9.4%
Total non-interest income	\$ 6,121	\$ 7,040	\$ (919)	-13.1%

(1) With no readily determinable fair market value.

Non-interest expense. During the nine months ended September 30, 2019 non-interest expense increased by \$1.2 million, or 7% to \$17.3 million, up from \$16.1 million during the same period in 2018. Total non-interest expense related to our Carson City, Nevada branch was \$692 thousand for the nine months ended September 30, 2019. Excluding the effect of the Carson City branch, non-interest expense would have increased by 4% for the nine months ended September 30, 2019.

The Company's single largest expense is salary and benefit costs. During the nine months ended September 30, 2019 salary and benefit expense increased by \$657 thousand, or 7%, to \$9.7 million. The increase in salary and benefit costs includes annual merit and promotional increases and an increase in personnel including five FTE at our Carson City, Nevada branch. Other significant increases in non-interest expense include \$355 thousand in occupancy and equipment expense, \$201 thousand in amortization of core deposit intangible, \$135 thousand in director compensation and expense and \$127 thousand in outside service fees. The largest decreases in non-interest expense were reductions in professional fees of \$127 thousand, other non-interest expense of \$122 thousand and deposit insurance expense of \$112 thousand.

Of the \$355 thousand increase in occupancy and equipment costs, \$140 thousand relates to the Carson City, Nevada branch. Of the remaining increase the three largest items were increases of \$60 thousand in equipment depreciation, \$65 thousand in software costs and \$26 thousand in property taxes. The increase in amortization of core deposit intangible is related to the amortization of the core deposit intangible recorded on the acquisition of the Carson City branch. Director compensation and expense was abnormally low during the 2018 period as it included the reversal of accrued retirement costs related to our former director John Flournoy who elected not to run for reelection in 2018 and instead allowed his board term to expire as of May 16, 2018. Mr. Flournoy did not meet the minimum years of service required under his agreement to receive benefits. In addition, during 2019 we have added two new Board members. The increase in outside services primarily relates to growth in the Bank.

Professional fees during the current period benefited from a reduction in consulting costs of \$74 thousand. Consulting costs were somewhat high during the 2018 period as they included an external review of our compliance management system and \$24 thousand related to our acquisition of the Carson City, Nevada branch. In addition, included in professional fees during the 2018 period were \$40 thousand in legal expense related to the Carson City branch acquisition. Other non-interest expense during the 2018 period was also higher than normal as it included a \$50 thousand increase in the reserve for undisbursed loan commitments and costs associated with the pending termination of our lease at our Tahoe City, California branch. During 2018 we purchased a building in Tahoe City which, after remodeling is complete, will become the new home of our Tahoe City branch. Our lease obligation at our current location includes a termination penalty that during 2018 has been accrued into other expense. Deposit insurance costs during the current period benefit from assessment credits we were able to apply to our deposit insurance billings. Plumas Bank was awarded assessment credits totaling \$177 thousand which became available once the Deposit Insurance Fund Reserve Ratio reached at least 1.38. During the third quarter we were notified that the reserve ratio was 1.40 on June 30, 2019 and that our credits would be available to offset insurance assessments beginning with the April 1, 2019 assessment period.

The following table describes the components of non-interest expense for the nine-month periods ended September 30, 2019 and 2018, dollars in thousands:

	For the Nine Months Ended September 30,			
	2019	2018	Dollar Change	Percentage Change
Salaries and employee benefits	\$ 9,743	\$ 9,086	\$ 657	7.2%
Occupancy and equipment	2,482	2,127	355	16.7%
Outside service fees	1,877	1,750	127	7.3%
Professional fees	545	672	(127)	-18.9%
Telephone and data communication	400	397	3	0.8%
Business development	362	296	66	22.3%
Director compensation and expense	318	183	135	73.8%
Armored car and courier	302	245	57	23.3%
Advertising and shareholder relations	295	323	(28)	-8.7%
Amortization of Core Deposit Intangible	206	5	201	4,020.0%
Loan collection expenses	172	200	(28)	-14.0%
Stationery and supplies	87	86	1	1.2%
Deposit insurance	65	177	(112)	-63.3%
OREO expenses	43	47	(4)	-8.5%
Provision from change in OREO valuation	-	38	(38)	-100.0%
Gain on Sale of OREO	(9)	(62)	53	-85.5%
Other	414	536	(122)	-22.8%
Total non-interest expense	<u>\$ 17,302</u>	<u>\$ 16,106</u>	<u>\$ 1,196</u>	7.4%

Provision for income taxes. The Company recorded an income tax provision of \$4.4 million, or 27.5% of pre-tax income for the nine months ended September 30, 2019. This compares to an income tax provision of \$3.8 million or 26.9% of pre-tax income during the first nine months of 2018. The percentages for 2019 and 2018 differ from statutory rates as tax exempt items of income such as earnings on Bank owned life insurance and municipal loan and securities interest decrease taxable income. In addition, the 2019 and 2018 provision include income tax benefits related to the exercise of stock options of \$24 thousand and \$99 thousand, respectively.

Deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the reported amount of assets and liabilities and their tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The determination of the amount of deferred income tax assets which are more likely than not to be realized is primarily dependent on projections of future earnings, which are subject to uncertainty and estimates that may change given economic conditions and other factors. The realization of deferred income tax assets is assessed, and a valuation allowance is recorded if it is "more likely than not" that all or a portion of the deferred tax asset will not be realized. "More likely than not" is defined as greater than a 50% chance. All available evidence, both positive and negative is considered to determine whether, based on the weight of that evidence, a valuation allowance is needed. Based upon the analysis of available evidence, management has determined that it is "more likely than not" that all deferred income tax assets as of September 30, 2019 and December 31, 2018 will be fully realized and therefore no valuation allowance was recorded. On the consolidated balance sheet, net deferred tax assets are included in accrued interest receivable and other assets.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2019

Net Income. The Company recorded net income of \$4.0 million for the three months ended September 30, 2019 up \$306 thousand from net income of \$3.7 million for the three months ended September 30, 2018. An increase of \$1.0 million in net interest income was partially offset by increases of \$447 thousand in non-interest expense and \$125 thousand in income tax expense and a decrease of \$138 thousand in non-interest income.

The following is a detail discussion of each component of the change in net income.

Net interest income before provision for loan losses. Net interest income was \$9.6 million for the three months ended September 30, 2019 an increase of \$1.0 million, or 12%, from \$8.6 million for the same period in 2018. The increase in net interest income includes an increase of \$1.2 million in interest income; the largest component of which was an increase in interest and fees on loans of \$1.1 million. Net interest margin for the three months ended September 30, 2019 decreased by 6 basis points from 4.78% during the third quarter of 2018 to 4.72% during the current quarter.

Interest income increased by 13%, to \$10.0 million for the three months ended September 30, 2019, up from \$8.8 million during the same period in 2018. This was related mostly to an increase in average loan balances interest and fees on loans which increased \$1.1 million to \$8.8 million for the three months ended September 30, 2019 as compared to \$7.7 million during the third quarter of 2018. The Company's average loan balances were \$599 million for the three months ended September 30, 2019, up \$70 million, or 13%, from \$529 million for the same period in 2018. The average yield on loans was 5.80% during the third quarter of 2019, up slightly from 5.77% for same quarter in 2018. Net loan costs increased by \$146 thousand from \$116 thousand during the third quarter of 2018 to \$262 thousand during the current quarter. Net loan costs during the third quarter of 2018 were lower than normal as we benefited from several prepayment penalties.

Interest on investment securities increased by \$38 thousand related to an increase in average balance from \$158.3 million in 2018 to \$172.2 million in 2019. Yield on investment securities was 2.48% during the current quarter and 2.60% during the three months ended September 30, 2018.

Interest expense on deposits increased by \$145 thousand to \$304 thousand for the three months ended September 30, 2019, up from \$159 thousand during the 2018 quarter. This increase mostly relates to an increase in interest expense on money market accounts and time deposits related to the purchase of our Carson City branch on October 26, 2018. Interest on money market accounts increased by \$85 thousand. Average money market accounts increased \$19.6 million from \$68.1 million during the three months ended September 30, 2018 to \$87.7 million during the current quarter. The average rate paid on money market accounts increased by 35 basis points to 0.50% during the three-months ended September 30, 2019 up from 0.15% during the 2018 quarter. Interest on time deposits increased by \$59 thousand from \$34 thousand during the three months ended September 30, 2018 to \$93 thousand during the current quarter. Average time deposits increased by \$6.3 million from \$40.5 million during the three months ended September 30, 2018 to \$46.8 million during the current quarter. The average rate paid on time deposits was 0.33% during the three-months ended September 30, 2018 and 0.79% during the current quarter.

The following table presents for the three-month periods indicated the distribution of consolidated average assets, liabilities and shareholders' equity. It also presents the amounts of interest income from interest earning assets and the resultant annualized yields expressed in both dollars and annualized yield percentages, as well as the amounts of interest expense on interest bearing liabilities and the resultant cost expressed in both dollars and annualized rate percentages. Average balances are based on daily averages. Nonaccrual loans are included in the calculation of average loans while nonaccrued interest thereon is excluded from the computation of yields earned:

	For the Three Months Ended September 30, 2019			For the Three Months Ended September 30, 2018		
	Average Balance (in thousands)	Interest (in thousands)	Yield/ Rate	Average Balance (in thousands)	Interest (in thousands)	Yield/ Rate
Interest-earning assets:						
Loans (1) (2) (3)	\$ 598,899	\$ 8,761	5.80%	\$ 529,100	\$ 7,693	5.77%
Investment securities (1)	172,184	1,075	2.48%	158,316	1,037	2.60%
Interest-bearing deposits	32,355	171	2.10%	22,847	113	1.96%
Total interest-earning assets	803,438	10,007	4.94%	710,263	8,843	4.94%
Cash and due from banks	22,449			21,303		
Other assets	40,100			39,434		
Total assets	<u>\$ 865,987</u>			<u>\$ 771,000</u>		
Interest-bearing liabilities:						
NOW deposits	\$ 106,584	26	0.10%	\$ 104,565	25	0.09%
Money market deposits	87,690	110	0.50%	68,052	25	0.15%
Savings deposits	179,986	75	0.17%	179,224	75	0.17%
Time deposits	46,778	93	0.79%	40,487	34	0.33%
Total deposits	421,038	304	0.29%	392,328	159	0.16%
Junior subordinated debentures	10,310	131	5.04%	10,310	131	5.04%
Other interest-bearing liabilities	11,008	5	0.18%	7,872	2	0.10%
Total interest-bearing liabilities	442,356	440	0.39%	410,510	292	0.28%
Non-interest-bearing deposits	337,023			291,746		
Other liabilities	6,729			7,077		
Shareholders' equity	79,879			61,667		
Total liabilities & equity	<u>\$ 865,987</u>			<u>\$ 771,000</u>		
Cost of funding interest-earning assets (4)			0.22%			0.16%
Net interest income and margin (5)		<u>\$ 9,567</u>	4.72%		<u>\$ 8,551</u>	4.78%

(1) Not computed on a tax-equivalent basis.

(2) Average nonaccrual loan balances of \$2.5 million for 2019 and \$0.9 million for 2018 are included in average loan balances for computational purposes.

(3) Net costs included in loan interest income for the three-month periods ended September 30, 2019 and 2018 were \$262,000 and \$116,000, respectively.

(4) Total annualized interest expense divided by the average balance of total earning assets.

(5) Annualized net interest income divided by the average balance of total earning assets.

The following table sets forth changes in interest income and interest expense for the three-month periods indicated and the amount of change attributable to variances in volume, rates and the combination of volume and rates based on the relative changes of volume and rates:

2019 over 2018 change in net interest income for the three months ended September 30				
(in thousands)				
	Volume (1)	Rate (2)	Mix (3)	Total
Interest-earning assets:				
Loans	\$ 1,015	\$ 47	\$ 6	\$ 1,068
Investment securities	91	(49)	(4)	38
Interest bearing deposits	47	8	3	58
Total interest income	1,153	6	5	1,164
Interest-bearing liabilities:				
NOW deposits	-	1	-	1
Money market deposits	8	60	17	85
Savings deposits	-	-	-	-
Time deposits	5	46	8	59
Junior subordinated debentures	-	-	-	-
Other	1	2	-	3
Total interest expense	14	109	25	148
Net interest income	<u>\$ 1,139</u>	<u>\$ (103)</u>	<u>\$ (20)</u>	<u>\$ 1,016</u>

(1) The volume change in net interest income represents the change in average balance divided by the previous year's rate.

(2) The rate change in net interest income represents the change in rate divided by the previous year's average balance.

(3) The mix change in net interest income represents the change in average balance multiplied by the change in rate.

Provision for loan losses. During the three months ended September 30, 2019 and 2018 we recorded a provision for loan losses of \$300 thousand. See "Analysis of Asset Quality and Allowance for Loan Losses" for a discussion of loan quality trends and the provision for loan losses.

Non-interest income. During the three months ended September 30, 2019, non-interest income totaled \$2.1 million, a decrease of \$138 thousand from the three months ended September 30, 2018. The largest component of this decrease was a \$251 thousand decrease in gains on sale of SBA loans from \$564 thousand during the three months ended September 30, 2018 to \$313 thousand during the current quarter. Proceeds from SBA loan sales totaled \$7.1 million during the current quarter and \$15.1 million during the 2018 quarter. Loans originated for sale totaled \$6.9 million during the three months ended September 30, 2019 and \$11.7 million during the three months ended September 30, 2018. The decline in gain on sale is consistent with the decrease in loans sold during the comparison periods. The decline in gains on sale of SBA loans was partially offset by increases in service charge income of \$48 thousand and interchange income of \$70 thousand.

The following table describes the components of non-interest income for the three-month periods ended September 30, 2019 and 2018, dollars in thousands:

	For the Three Months Ended September 30,			Percentage Change
	2019	2018	Dollar Change	
Service charges on deposit accounts	\$ 676	\$ 628	\$ 48	7.6%
Interchange income	642	572	70	12.2%
Gain on sale of loans, net	313	564	(251)	-44.5%
Loan serving fees	184	200	(16)	-8.0%
Earnings on life insurance policies	82	82	-	-%
Other	249	238	11	4.6%
Total non-interest income	<u>\$ 2,146</u>	<u>\$ 2,284</u>	<u>\$ (138)</u>	-6.0%

Non-interest expense. During the three months ended September 30, 2019, total non-interest expense increased by \$447 thousand, or 8%, to \$5.9 million, up from \$5.4 million for the comparable period in 2018. Total non-interest expense related to our new Carson City, Nevada branch was \$204 thousand for the three months ended September 30, 2019. Excluding the effect of the Carson City branch, non-interest expense would have increased by 6%.

The Company's single largest expense is salary and benefit costs. During the three months ended September 30, 2019 salary and benefits increased by \$390 thousand, or 13%, to \$3.4 million. The increase in salary and benefit costs includes annual merit and promotional increases and an increase in personnel. Additionally, the deferral of loan origination costs declined by \$192 thousand from \$703 thousand during the third quarter of 2018 to \$511 thousand during the current quarter.

Other significant increases in non-interest expense include \$78 thousand in occupancy and equipment expense, \$66 thousand in the amortization of core deposit intangibles and \$52 thousand in outside service fees. The largest single decline in non-interest expense was \$120 thousand in deposit insurance expense. Please see the nine-month discussion for additional information related to these changes.

The following table describes the components of non-interest expense for the three-month periods ended September 30, 2019 and 2018, dollars in thousands:

	For the Three Months Ended September 30,			Percentage Change
	2019	2018	Dollar Change	
Salaries and employee benefits	\$ 3,439	\$ 3,049	\$ 390	12.8%
Occupancy and equipment	799	721	78	10.8%
Outside service fees	646	594	52	8.8%
Professional fees	201	235	(34)	-14.5%
Telephone and data communication	139	131	8	6.1%
Business development	119	100	19	19.0%
Armored car and courier	117	86	31	36.0%
Director compensation and expense	114	98	16	16.3%
Advertising and shareholder relations	89	113	(24)	-21.2%
Amortization of Core Deposit Intangible	68	2	66	3,300%
Loan collection expenses	52	65	(13)	-20.0%
Stationery and supplies	30	34	(4)	-11.8%
OREO expenses	16	9	7	77.8%
Gain on sale of OREO	-	1	(1)	-100%
Deposit insurance	(62)	58	(120)	-206.9%
Other	108	132	(24)	-18.2%
Total non-interest expense	<u>\$ 5,875</u>	<u>\$ 5,428</u>	<u>\$ 447</u>	8.2%

Provision for income taxes. The Company recorded an income tax provision of \$1.5 million, or 27.7% of pre-tax income for the three months ended September 30, 2019. This compares to an income tax provision of \$1.4 million, or 27.6% of pre-tax income for the three months ended September 30, 2018. The percentages for 2019 and 2018 differ from statutory rates as tax exempt items of income such as earnings on Bank owned life insurance and municipal loan and securities interest decrease taxable income.

FINANCIAL CONDITION

Loan Portfolio. Gross loans balances increased by \$35.6 million, or 6%, from \$566 million at December 31, 2018 to \$602 million at September 30, 2019. The increase in loan balances includes increases of \$20.7 million in commercial real estate loans, \$9.6 million in automobile loans, \$8.4 million in agricultural loans, \$2.6 million in construction loans and \$0.4 million in other loans. These increases were partially offset by declines of \$3.8 million in commercial loans, \$1.4 million in equity lines of credit and \$0.9 million in residential real estate loans. The Company continues to manage the mix of its loan portfolio consistent with its identity as a community bank serving the financing needs of all sectors of the area it serves. Although the Company offers a broad array of financing options, it continues to concentrate its focus on small to medium sized commercial businesses. These loans offer diversification as to industries and types of businesses, thus limiting material exposure in any industry concentrations. The Company offers both fixed and floating rate loans and obtains collateral in the form of real property, business assets and deposit accounts, but looks to business and personal cash flows as its primary source of repayment.

As shown in the following table the Company's largest lending categories are commercial real estate loans, auto loans, agricultural loans and commercial loans.

(dollars in thousands)	Balance at	Percent of	Balance at	Percent of
	End of	Loans in	End of	Loans in
	Period	Each	Period	Each
	9/30/19	Category to	12/31/18	Category to
		Total Loans		Total Loans
		9/30/19		12/31/18
Commercial	\$ 45,818	7.6%	\$ 49,563	8.8%
Agricultural	77,529	12.9%	69,160	12.2%
Real estate - residential	14,960	2.5%	15,900	2.8%
Real estate - commercial	292,461	48.6%	271,710	48.0%
Real estate - construction & land	42,727	7.1%	40,161	7.1%
Equity Lines of Credit	37,067	6.2%	38,490	6.8%
Auto	86,727	14.4%	77,135	13.6%
Other	4,467	0.7%	4,080	0.7%
Total Gross Loans	\$ 601,756	100%	\$ 566,199	100%

The Company's real estate related loans, including real estate mortgage loans, real estate construction and land development loans, consumer equity lines of credit, and agricultural loans secured by real estate comprised 71% of the total loan portfolio at September 30, 2019. Moreover, the business activities of the Company currently are focused in the California counties of Plumas, Nevada, Placer, Lassen, Modoc, Shasta, and Sierra and in Washoe and Carson City Counties in Northern Nevada. Consequently, the results of operations and financial condition of the Company are dependent upon the general trends in these economies and, in particular, the residential and commercial real estate markets. In addition, the concentration of the Company's operations in these areas of Northeastern California and Northwestern Nevada exposes it to greater risk than other banking companies with a wider geographic base in the event of catastrophes, such as earthquakes, fires and floods in these regions.

The rates of interest charged on variable rate loans are set at specific increments in relation to the Company's lending rate or other indexes such as the published prime interest rate or U.S. Treasury rates and vary with changes in these indexes. The frequency in which variable rate loans reprice can vary from one day to several years. At September 30, 2019 and December 31, 2018, approximately 74% and 75%, respectively of the Company's loan portfolio was comprised of variable rate loans. Loans indexed to the prime interest rate totaled approximately 26% of the Company's loan portfolio; these loans reprice within one day to three months of a change in the prime rate. At September 30, 2019 and December 31, 2018, 33% of the variable loans were at their respective floor rate. While real estate mortgage, commercial and consumer lending remain the foundation of the Company's historical loan mix, some changes in the mix have occurred due to the changing economic environment and the resulting change in demand for certain loan types. The most significant change has been an increase in indirect auto lending with automobile loans increasing from 2.5% of gross loans at December 31, 2011 to 14.4% of gross loans at September 30, 2019. The automobile portfolio provides diversification to the loan portfolio in terms of rate, term and balance as these loans tend to have a much shorter term and balance than commercial real-estate loans and are fixed rate. In addition, the Company remains committed to the agricultural industry and will continue to pursue high quality agricultural loans. Agricultural loans include both commercial and commercial real estate loans. The Company's agricultural loan balances totaled \$78 million at September 30, 2019 and \$69 million at December 31, 2018.

Analysis of Asset Quality and Allowance for Loan Losses. The Company attempts to minimize credit risk through its underwriting and credit review policies. The Company's credit review process includes internally prepared credit reviews as well as contracting with an outside firm to conduct periodic credit reviews. The Company's management and lending officers evaluate the loss exposure of classified and impaired loans on a quarterly basis, or more frequently as loan conditions change. The Management Asset Resolution Committee (MARC) reviews the asset quality of criticized and past due loans monthly and reports the findings to the full Board of Directors. In management's opinion, this loan review system helps facilitate the early identification of potential criticized loans. MARC also provides guidance for the maintenance and timely disposition of OREO properties including developing financing and marketing programs to incent individuals to purchase OREO. MARC consists of the Bank's Chief Executive Officer, Chief Financial Officer and Chief Credit Officer, and the activities are governed by a formal written charter. The MARC meets monthly and reports to the Board of Directors.

The allowance for loan losses is established through charges to earnings in the form of the provision for loan losses. Loan losses are charged to and recoveries are credited to the allowance for loan losses. The allowance for loan losses is maintained at a level deemed appropriate by management to provide for known and inherent risks in the loan portfolio. The adequacy of the allowance for loan losses is based upon management's continuing assessment of various factors affecting the collectability of loans including current economic conditions, maturity of the portfolio, size of the portfolio, industry concentrations, borrower credit history, collateral, the existing allowance for loan losses, independent credit reviews, current charges and recoveries to the allowance for loan losses and the overall quality of the portfolio as determined by management, regulatory agencies, and independent credit review consultants retained by the Company. There is no precise method of predicting specific losses or amounts which may ultimately be charged off on particular segments of the loan portfolio. The collectability of a loan is subjective to some degree, but must relate to the borrower's financial condition, cash flow, quality of the borrower's management expertise, collateral and guarantees, and state of the local economy.

Formula allocations are calculated by applying loss factors to outstanding loans with similar characteristics. Loss factors are based on the Company's historical loss experience as adjusted for changes in the business cycle and may be adjusted for significant factors that, in management's judgment, affect the collectability of the portfolio as of the evaluation date. Historical loss data from the beginning of the latest business cycle are incorporated in the loss factors.

The discretionary allocation is based upon management's evaluation of various loan segment conditions that are not directly measured in the determination of the formula and specific allowances. The conditions may include, but are not limited to, general economic and business conditions affecting the key lending areas of the Company, credit quality trends, collateral values, loan volumes and concentrations, and other business conditions.

The following table provides certain information for the dates indicated with respect to the Company's allowance for loan losses as well as charge-off and recovery activity.

<i>(dollars in thousands)</i>	For the Nine Months Ended		For the Year Ended		
	September 30,		December 31		
	2019	2018	2018	2017	2016
Balance at beginning of period	\$ 6,958	\$ 6,669	\$ 6,669	\$ 6,549	\$ 6,078
Charge-offs:					
Commercial and agricultural	186	325	325	202	268
Real estate mortgage	-	-	25	48	292
Real estate construction & land	-	-	-	-	5
Consumer (includes equity LOC & Auto)	688	663	841	629	414
Total charge-offs	874	988	1,191	879	979
Recoveries:					
Commercial and agricultural	21	23	83	89	53
Real estate mortgage	4	112	114	118	45
Real estate construction & land	-	3	3	-	389
Consumer (includes equity LOC & Auto)	217	227	280	192	163
Total recoveries	242	365	480	399	650
Net charge-offs	632	623	711	480	329
Provision for loan losses	900	800	1,000	600	800
Balance at end of period	\$ 7,226	\$ 6,846	\$ 6,958	\$ 6,669	\$ 6,549
Net charge-offs during the period to average loans (annualized for the nine-month periods)	0.14%	0.16%	0.14%	0.10%	0.08%
Allowance for loan losses to total loans	1.20%	1.27%	1.23%	1.37%	1.42%

During the nine months ended September 30, 2019 and 2018 we recorded a provision for loan losses of \$900 thousand and \$800 thousand, respectively. Net charge-offs totaled \$632 thousand during the nine months ended September 30, 2019, an increase of \$9 thousand from \$623 thousand during the nine months ended September 30, 2018.

The following table provides a breakdown of the allowance for loan losses at September 30, 2019 and December 31, 2018:

<i>(dollars in thousands)</i>	Balance at	Percent of	Balance at	Percent of
	End of Period	Loans in Each	End of Period	Loans in Each
	2019	Category to	2018	Category to
		Total Loans		Total Loans
		2019		2018
Commercial and agricultural	\$ 1,424	20.5%	\$ 1,452	21.0%
Real estate mortgage	3,261	51.1%	2,900	50.8%
Real estate construction & land	640	7.1%	758	7.1%
Consumer (includes equity LOC & Auto)	1,901	21.3%	1,848	21.1%
Total	\$ 7,226	100.0%	\$ 6,958	100.0%

The allowance for loan losses totaled \$7.2 million at September 30, 2019 and \$7.0 million at December 31, 2018. Specific reserves related to impaired loans increased by \$54 thousand from \$181 thousand at December 31, 2018 to \$235 thousand at September 30, 2019. At least quarterly, the Company evaluates each specific reserve and if it determines that the loss represented by the specific reserve is uncollectable it records a charge-off for the uncollectable portion. General reserves were \$7.0 million at September 30, 2019 and \$6.8 million at December 31, 2018. The allowance for loan losses as a percentage of total loans was 1.20% at September 30, 2019 and 1.23% at December 31, 2018. The percentage of general reserves to unimpaired loans totaled 1.17% at September 30, 2019 and 1.20% at December 31, 2018.

The Company places loans 90 days or more past due on nonaccrual status unless the loan is well secured and in the process of collection. A loan is considered to be in the process of collection if, based on a probable specific event, it is expected that the loan will be repaid or brought current. Generally, this collection period would not exceed 90 days. When a loan is placed on nonaccrual status the Company's general policy is to reverse and charge against current income previously accrued but unpaid interest. Interest income on such loans is subsequently recognized only to the extent that cash is received, and future collection of principal is deemed by management to be probable. Where the collectability of the principal or interest on a loan is considered to be doubtful by management, it is placed on nonaccrual status prior to becoming 90 days delinquent.

Impaired loans are measured based on the present value of the 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 amount of impaired loans is not directly comparable to the amount of nonperforming loans disclosed later in this section. The primary difference between impaired loans and nonperforming loans is that impaired loan recognition considers not only loans 90 days or more past due, restructured loans and nonaccrual loans but also may include identified problem loans other than delinquent loans where it is considered probable that we will not collect all amounts due to us (including both principal and interest) in accordance with the contractual terms of the loan agreement.

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the Company, for economic or legal reasons related to the debtor's financial difficulties, grants a concession to the debtor that it would not otherwise consider. Restructured workout loans typically present an elevated level of credit risk as the borrowers are not able to perform according to the original contractual terms. Loans that are reported as TDRs are considered impaired and measured for impairment as described above.

Loans restructured (TDRs) and not included in nonperforming loans in the following table totaled \$0.9 million, \$1.0 million, \$1.1 million, \$2.6 million and \$2.0 million at September 30, 2019 and December 31, 2018, 2017, 2016, and 2015, respectively. For additional information related to restructured loans see Note 4 to the condensed consolidated financial statements contained within this Form 10-Q.

The following table sets forth the amount of the Company's nonperforming assets as of the dates indicated.

	At September 30,	At December 31,			
	2019	2018	2017	2016	2015
	<i>(dollars in thousands)</i>				
Nonaccrual loans	\$ 2,598	\$ 1,117	\$ 1,226	\$ 2,724	\$ 4,546
Loans past due 90 days or more and still accruing	-	-	1,796	-	-
Total nonperforming loans	2,598	1,117	3,022	2,724	4,546
Other real estate owned	1,094	1,170	1,344	735	1,756
Other vehicles owned	46	53	35	12	30
Total nonperforming assets	\$ 3,738	\$ 2,340	\$ 4,401	\$ 3,471	\$ 6,332
Interest income forgone on nonaccrual loans	\$ 116	\$ 46	\$ 50	\$ 164	\$ 303
Interest income recorded on a cash basis on nonaccrual loans	\$ -	\$ -	\$ -	\$ 29	\$ -
Nonperforming loans to total loans	0.43%	0.20%	0.62%	0.59%	1.13%
Nonperforming assets to total assets	0.42%	0.28%	0.59%	0.53%	1.06%

Nonperforming loans at September 30, 2019 were \$2.6 million, an increase of \$1.5 million from the \$1.1 million balance at December 31, 2018. Specific reserves on nonaccrual loans totaled \$201 thousand at September 30, 2019 and \$128 thousand at December 31, 2018, respectively. Performing loans past due thirty to eighty-nine days were \$1.7 million at September 30, 2019 down from \$2.6 million at December 31, 2018.

A substandard loan is not adequately protected by the current sound worth and paying capacity of the borrower or the value of the collateral pledged, if any. Total substandard loans increased by \$1.6 million from \$741 thousand at December 31, 2018 to \$2.4 million at September 30, 2019. Loans classified as special mention increased by \$4.0 million from \$4.3 million at December 31, 2018 to \$8.3 million at September 30, 2019. At September 30, 2019, \$22 thousand of performing loans were classified as substandard. Further deterioration in the credit quality of individual performing substandard loans or other adverse circumstances could result in the need to place these loans on nonperforming status.

At September 30, 2019 and December 31, 2018, the Company's recorded investment in impaired loans totaled \$2.6 million and \$1.3 million, respectively. The specific allowance for loan losses related to impaired loans totaled \$235 thousand and \$181 thousand at September 30, 2019 and December 31, 2018, respectively. Additionally, \$11 thousand had been charged off against the impaired loans at September 30, 2019 and December 31, 2018.

It is the policy of management to make additions to the allowance for loan losses so that it remains appropriate to absorb the inherent risk of loss in the portfolio. Management believes that the allowance at September 30, 2019 is appropriate. However, the determination of the amount of the allowance is judgmental and subject to economic conditions which cannot be predicted with certainty. Accordingly, the Company cannot predict whether charge-offs of loans in excess of the allowance may occur in future periods.

OREO represents real property acquired by the Bank either through foreclosure or through a deed in lieu thereof from the borrower. Repossessed assets include vehicles and other commercial assets acquired under agreements with delinquent borrowers. OREO holdings represented five properties totaling \$1.1 million at September 30, 2019 and six properties totaling \$1.2 million at December 31, 2018. Nonperforming assets as a percentage of total assets were 0.42% at September 30, 2019 and 0.28% at December 31, 2018.

The following table provides a summary of the change in the number and balance of OREO properties for the nine months ended September 30, 2019 and 2018 (dollars in thousands):

	Nine Months Ended September 30,			
	#	2019	#	2018
Beginning Balance	6	\$ 1,170	6	\$ 1,344
Additions	-	-	2	288
Dispositions	1	76	(2)	(506)
Provision from change in OREO valuation	-	-	-	(38)
Ending Balance	5	\$ 1,094	6	\$ 1,088

The dispositions in 2018 includes \$377 thousand related to the sale of a portion of a property.

Investment Portfolio and Federal Funds Sold. Total investment securities were \$169.5 million as of September 30, 2019 and \$171.5 million as of December 31, 2018. Unrealized gains on available-for-sale investment securities totaling \$3.0 million were recorded, net of \$895 thousand in tax expense, as accumulated other comprehensive income within shareholders' equity at September 30, 2019. Unrealized losses on available-for-sale investment securities totaling \$2.9 million were recorded, net of \$846 thousand in tax benefits, as accumulated other comprehensive income within shareholders' equity at December 31, 2018.

During the three and nine months ended September 30, 2019 the Company sold forty available-for-sale investment securities for total proceeds of \$11.4 million recording a \$20 thousand gain on sale. During the nine months ended September 30, 2018 the Company sold eighteen available-for-sale investment securities for total proceeds of \$4.2 million recording an \$8 thousand loss on sale. No investment securities were sold during the three months ended September 30, 2019 and 2018.

The investment portfolio at September 30, 2019 consisted of \$136.7 million in securities of U.S. Government-sponsored agencies and 87 municipal securities totaling \$32.8 million. The investment portfolio at December 31, 2018 consisted of \$132.7 million in securities of U.S. Government-sponsored agencies and 119 municipal securities totaling \$38.8 million.

There were no Federal funds sold at September 30, 2019 and December 31, 2018; however, the Bank maintained interest earning balances at the Federal Reserve Bank totaling \$50.5 million at September 30, 2019 and \$19.9 million at December 31, 2018. The balance, at September 30, 2019, earns interest at the rate of 1.80%.

The Company classifies its investment securities as available-for-sale or held-to-maturity. Currently all securities are classified as available-for-sale. Securities classified as available-for-sale may be sold to implement the Company's asset/liability management strategies and in response to changes in interest rates, prepayment rates and similar factors.

Deposits. Total deposits increased by \$49.6 million from \$727 million at December 31, 2018 to \$776 million at September 30, 2019. This increase was driven by a \$49.2 million increase in non-interest-bearing demand deposits. Additionally, money market accounts increased by \$6.7 million, savings balances increased by \$4.8 million and interest-bearing demand deposits increased by \$3.6 million. Partially offsetting these increases was a decline in time deposits of \$14.7 million. Much of the decline in time deposits is related to the maturity of higher rate time deposits at the Company's Carson City, Nevada branch. The Company continues to manage the mix of its deposits consistent with its identity as a community bank serving the financial needs of its customers.

The following table shows the distribution of deposits by type at September 30, 2019 and December 31, 2018.

<i>(dollars in thousands)</i>	Balance at	Percent of	Balance at	Percent of
	End of	Deposits in	End of	Deposits in
	Period	Each	Period	Each
	Category to	Total	Category to	Total
	9/30/19	9/30/19	12/31/18	12/31/18
Non-interest bearing	\$ 353,203	45.5%	\$ 304,039	41.8%
NOW	108,708	14.0%	105,107	14.5%
Money Market	89,451	11.5%	82,743	11.4%
Savings	182,565	23.5%	177,710	24.5%
Time	42,256	5.5%	56,966	7.8%
Total Deposits	<u>\$ 776,183</u>	<u>100%</u>	<u>\$ 726,565</u>	<u>100%</u>

Deposits represent the Bank's primary source of funds. Deposits are primarily core deposits in that they are demand, savings and time deposits generated from local businesses and individuals. These sources are considered to be relatively stable, long-term relationships thereby enhancing steady growth of the deposit base without major fluctuations in overall deposit balances. The Company experiences, to a small degree, some seasonality with the slower growth period between November through April, and the higher growth period from May through October. To assist in meeting any funding demands, the Company maintains a secured borrowing arrangement with the Federal Home Loan Bank of San Francisco ("FHLB"). There were no brokered deposits at September 30, 2019 or December 31, 2018.

Short-term Borrowing Arrangements. The Company is a member of the FHLB and can borrow up to \$222 million from the FHLB secured by commercial and residential mortgage loans with carrying values totaling \$359 million. The Company is required to hold FHLB stock as a condition of membership. At September 30, 2019 and December 31, 2018, the Company held \$3.5 million and \$3.0 million, respectively of FHLB stock which is recorded as a component of other assets. Based on this level of stock holdings at September 30, 2019, the Company can borrow up to \$130.2 million. To borrow the \$222 million in available credit the Company would need to purchase \$2.5 million in additional FHLB stock. In addition to its FHLB borrowing line, the Company has unsecured short-term borrowing agreements with three of its correspondent banks in the amounts of \$20 million, \$11 million and \$10 million. There were no outstanding borrowings to the FHLB or the correspondent banks under these agreements at September 30, 2019 and December 31, 2018.

Note Payable. On October 1, 2019 the Company renewed its line of credit, for a one-year term, with the same lender (the "Note"). The maximum amount outstanding at any one time on the Note cannot exceed \$5 million. There were no borrowings on the Note during the nine months ended September 30, 2019 or the year ended December 31, 2018. The Note bears interest at a rate of the U.S. "Prime Rate" plus one-quarter percent per annum and is secured by 100 shares of Plumas Bank stock representing the Company's 100% ownership interest in Plumas Bank. Under the Note, the Bank is subject to several negative and affirmative covenants including, but not limited to providing timely financial information, maintaining specified levels of capital, restrictions on additional borrowings, and meeting or exceeding certain capital and asset quality ratios. The Bank was in compliance with all such covenants related to the Note at September 30, 2019 and December 31, 2018.

Repurchase Agreements. In 2011 the Bank introduced a new product for its larger business customers which use securities sold under agreements to repurchase as an alternative to interest-bearing deposits. Securities sold under agreements to repurchase totaling \$13.4 million and \$13.1 million at September 30, 2019 and December 31, 2018, respectively are secured by U.S. Government agency securities with a carrying amount of \$19.6 million and \$21.8 million at September 30, 2019 and December 31, 2018, respectively. Interest paid on this product is similar to that which is paid on the Bank's premium interest-bearing transaction accounts; however, these are not deposits and are not FDIC insured.

Junior Subordinated Deferrable Interest Debentures. Plumas Statutory Trust I and II are business trust subsidiaries formed by the Company with capital of \$347,000 and \$178,000, respectively, for the sole purpose of issuing trust preferred securities fully and unconditionally guaranteed by the Company.

During 2002, Trust I issued 6,000 Floating Rate Capital Trust Pass-Through Securities ("Trust Preferred Securities"), with a liquidation value of \$1,000 per security, for gross proceeds of \$6,000,000. During 2005, Trust II issued 4,000 Trust Preferred Securities with a liquidation value of \$1,000 per security, for gross proceeds of \$4,000,000. The entire proceeds were invested by Trust I in the amount of \$6,186,000 and Trust II in the amount of \$4,124,000 in Floating Rate Junior Subordinated Deferrable Interest Debentures (the "Subordinated Debentures") issued by the Company, with identical maturity, repricing and payment terms as the Trust Preferred Securities. The Subordinated Debentures represent the sole assets of Trusts I and II.

Trust I's Subordinated Debentures mature on September 26, 2032, bear a current interest rate of 5.51% (based on 3-month LIBOR plus 3.40%), with repricing and payments due quarterly. Trust II's Subordinated Debentures mature on September 28, 2035, bear a current interest rate of 3.60% (based on 3-month LIBOR plus 1.48%), with repricing and payments due quarterly. The interest rate of the Trust Preferred Securities issued by Trust I adjust on each quarterly anniversary date to equal the 3-month LIBOR plus 3.40%. The Trust Preferred Securities issued by Trust II adjust on each quarterly anniversary date to equal the 3-month LIBOR plus 1.48%. Both Trusts I and II have the option to defer payment of the distributions for a period of up to five years, as long as the Company is not in default on the payment of interest on the Subordinated Debentures.

Interest expense recognized by the Company for the nine months ended September 30, 2019 and 2018 related to the subordinated debentures was \$406 thousand and \$370 thousand, respectively.

Capital Resources

Shareholders' equity increased by \$14.9 million from \$66.9 million at December 31, 2018 to \$81.8 million at September 30, 2019. The \$14.9 million increase was related to earnings during the first nine months of 2019 of \$11.6 million, an increase in unrealized gain on investment securities of \$4.2 million and \$0.3 million representing stock option activity. These items were partially offset by a semi-annual dividend which totaled \$1.2 million.

It is the policy of the Company to periodically distribute excess retained earnings to the shareholders through the payment of cash dividends. Such dividends help promote shareholder value and capital adequacy by enhancing the marketability of the Company's stock. All authority to provide a return to the shareholders in the form of a cash or stock dividend or split rests with the Board of Directors. The Board will periodically, but on no regular schedule, reviews the appropriateness of a cash dividend payment. Banking regulations limit the amount of dividends that may be paid without prior approval of regulatory agencies. The Company is subject to various restrictions on the payment of dividends.

On October 20, 2016 the Company announced that its Board of Directors approved the reinstatement of a semi-annual cash dividend. The dividend in the amount of \$0.10 per share was paid on November 21, 2016. On May 15, 2017 and November 15, 2017, the Company paid semi-annual cash dividends each of which totaled \$0.14 per share. On May 15, 2018 and November 15, 2018, the Company paid semi-annual cash dividends each of which totaled \$0.18 per share. On May 15, 2019 the Company paid a semi-annual cash dividend of \$0.23 per share.

Capital Standards. In July 2013, the federal bank regulatory agencies approved the final rules implementing the Basel Committee on Banking Supervision's capital guidelines for U.S. banks, sometimes called "Basel III". The phase-in period for the final rules began in 2015, with certain of the rules' requirements phased in over a multi-year schedule. Under the final rules minimum requirements increased for both the quantity and quality of capital held by the Company and the Bank. The new capital rules include a new minimum "common equity Tier 1" ratio of 4.5%, a Tier 1 capital ratio of 6.0% (increased from 4.0%), a total risk-based capital ratio of 8.0%, and a minimum leverage ratio of 4.0% (calculated as Tier 1 capital to average consolidated assets). The effective date of these requirements was January 1, 2015. In addition, the new capital rules include a capital conservation buffer of 2.5% above each of these levels (to be phased in over three years beginning at 0.625% on January 1, 2016 and increasing by that amount on each subsequent January 1, until reaching 2.5% on January 1, 2019) required for banking institutions to avoid restrictions on their ability to pay dividends, repurchase stock or pay discretionary bonuses. Including the capital conservation buffer of 2.5%, the new capital rules would result in the following minimum ratios to be considered well capitalized: (i) a Tier 1 capital ratio of 8.5%, (ii) a common equity Tier 1 capital ratio of 7.0%, and (iii) a total capital ratio of 10.5%. The final rules also implement strict eligibility criteria for regulatory capital instruments.

Plumas Bancorp qualifies for treatment under the Small Bank Holding Company Policy Statement (Regulation Y, Appendix C) (the "Policy Statement") and is thereby not subject to consolidated capital rules at the bank holding company level. On May 24, 2018, the Economic Growth, Regulatory Relief and Consumer Protection Act (the "Relief Act") was signed into law. The Relief Act included a provision to increase the threshold for qualifying for the Policy Statement from \$1 billion to \$3 billion in total assets.

On September 17, 2019 the FDIC approved a final rule allowing community banks with a leverage capital ratio of at least 9% to be considered in compliance with Basel III capital requirements and exempt from the complex Basel calculation.

Under the final rule, banks with less than \$10 billion in assets may elect the community bank leverage ratio framework (“CBLR”) if they meet the 9 percent ratio and if they hold 25 or less percent of assets in off-balance sheet exposures, and 5 percent or less of assets in trading assets and liabilities. For institutions that fall below the 9% capital requirement but remain above 8%, the final rule establishes a 2 quarter grace period to either meet the qualifying criteria again or comply with the generally applicable capital rule.

Eligible banks may opt-in to the CBLR beginning in the first quarter of 2020. Plumas Bank believes it meets all eligibility criteria required under the CBLR, but has not yet determined if it will opt-in.

The following table sets forth the Bank's actual capital amounts and ratios (dollar amounts in thousands):

	Minimum Amount of Capital Required					
	Actual		For Capital Adequacy Purposes ⁽¹⁾		To be Well-Capitalized Under Prompt Corrective Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
September 30, 2019						
Common Equity Tier 1 Ratio	\$ 87,570	13.0%	\$ 30,383	4.5%	\$ 43,887	6.5%
Tier 1 Leverage Ratio	87,570	10.2%	34,453	4.0%	43,066	5.0%
Tier 1 Risk-Based Capital Ratio	87,570	13.0%	40,511	6.0%	54,015	8.0%
Total Risk-Based Capital Ratio	95,046	14.1%	54,015	8.0%	67,519	10.0%
December 31, 2018						
Common Equity Tier 1 Ratio	\$ 76,545	11.8%	\$ 29,071	4.5%	\$ 41,991	6.5%
Tier 1 Leverage Ratio	76,545	9.3%	32,765	4.0%	40,956	5.0%
Tier 1 Risk-Based Capital Ratio	76,545	11.8%	38,761	6.0%	51,681	8.0%
Total Risk-Based Capital Ratio	83,753	13.0%	51,681	8.0%	64,602	10.0%

(1) Does not include amounts required to maintain the capital conservation buffer under the new capital rules

Management believes that Plumas Bank currently meets all its capital adequacy requirements.

The current and projected capital positions of the Bank and the impact of capital plans and long-term strategies are reviewed regularly by management. The Company policy is to maintain the Bank’s ratios above the prescribed well-capitalized ratios at all times.

Off-Balance Sheet Arrangements

Loan Commitments. In the normal course of business, there are various commitments outstanding to extend credits that are not reflected in the financial statements. Commitments to extend credit and letters of credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Annual review of commercial credit lines, letters of credit and ongoing monitoring of outstanding balances reduces the risk of loss associated with these commitments. As of September 30, 2019, the Company had \$104.9 million in unfunded loan commitments and \$431 thousand in letters of credit. This compares to \$126.9 million in unfunded loan commitments and \$417 thousand in letters of credit at December 31, 2018. Of the \$104.9 million in unfunded loan commitments, \$58.0 million and \$46.9 million represented commitments to commercial and consumer customers, respectively. Of the total unfunded commitments at September 30, 2019, \$57.3 million were secured by real estate, of which \$20.4 million was secured by commercial real estate and \$36.9 million was secured by residential real estate in the form of equity lines of credit. The commercial loan commitments not secured by real estate primarily represent business lines of credit, while the consumer loan commitments not secured by real estate primarily represent revolving credit card lines and overdraft protection lines. Since some of the commitments are expected to expire without being drawn upon the total commitment amounts do not necessarily represent future cash requirements.

Leases. The Company leases three depository branches, four lending offices and two non-branch automated teller machine locations. Total rental expenses under all leases were \$342 thousand and \$275 thousand during the nine months ended September 30, 2019 and 2018, respectively. The expiration dates of the leases vary, with the first such lease expiring during 2019 and the last such lease expiring during 2022.

Liquidity

The Company manages its liquidity to provide the ability to generate funds to support asset growth, meet deposit withdrawals (both anticipated and unanticipated), fund customers' borrowing needs, satisfy maturity of short-term borrowings and maintain reserve requirements. The Company's liquidity needs are managed using assets or liabilities, or both. On the asset side, in addition to cash and due from banks, the Company maintains an investment portfolio which includes unpledged U.S. Government-sponsored agency securities that are classified as available-for-sale. On the liability side, liquidity needs are managed by charging competitive offering rates on deposit products and the use of established lines of credit.

The Company is a member of the FHLB and can borrow up to \$222 million from the FHLB secured by commercial and residential mortgage loans with carrying values totaling \$359 million. See "Short-term Borrowing Arrangements" for additional information on our FHLB borrowing capacity. In addition to its FHLB borrowing line, the Company has unsecured short-term borrowing agreements with three of its correspondent banks in the amounts of \$20 million, \$11 million and \$10 million. There were no outstanding borrowings under the FHLB or the correspondent bank borrowing lines at September 30, 2019 or December 31, 2018.

Customer deposits are the Company's primary source of funds. Total deposits increased by \$49.6 million from \$727 million at December 31, 2018 to \$776 million at September 30, 2019. Deposits are held in various forms with varying maturities. The Company's securities portfolio, Federal funds sold, FHLB advances, and cash and due from banks serve as the primary sources of liquidity, providing adequate funding for loans during periods of high loan demand. During periods of decreased lending, funds obtained from the maturing or sale of investments, loan payments, and new deposits are invested in short-term earning assets, such as cash held at the FRB, Federal funds sold and investment securities, to serve as a source of funding for future loan growth. Management believes that the Company's available sources of funds, including borrowings, will provide adequate liquidity for its operations in the foreseeable future.

Recent Developments. On October 16, 2019 the Company declared a semi-annual cash dividend totaling \$0.23 per share, or approximately \$1.2 million. The dividend is payable on November 15, 2019 to shareholders of record at the close of business day on November 1, 2019.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not required.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Company's management, including the Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of September 30, 2019. The Company's disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the U.S. Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of September 30, 2019.

Changes in Internal Control over Financial Reporting

There were no changes in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the quarter ended September 30, 2019 that have materially affected or are reasonably likely to materially affect the Company's internal control over financial reporting.

PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, the Company and/or its subsidiary are a party to claims and legal proceedings arising in the ordinary course of business. In the opinion of the Company's management, the amount of ultimate liability with respect to such proceedings will not have a material adverse effect on the financial condition or results of operations of the Company taken as a whole.

ITEM 1A RISK FACTORS

There have been no material changes to the principal risks that we believe are material to our business, results of operations and financial condition, from the risk factors previously disclosed in the 2018 Annual Report on Form 10-K. For a discussion on these risk factors, please see "Item 1A. Risk Factors" contained in the 2018 Annual Report on Form 10-K.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) None.

(b) None.

(c) None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

The following documents are included or incorporated by reference in this Quarterly Report on Form 10Q:

- 3.1 [Articles of Incorporation as amended of Registrant included as exhibit 3.1 to the Registrant's Form S-4, File No. 333-84534, which is incorporated by reference herein.](#)
- 3.2 [Bylaws of Registrant as amended on March 16, 2011 included as exhibit 3.2 to the Registrant's Form 10-K for December 31, 2010, which is incorporated by this reference herein.](#)
- 3.3 [Amendment of the Articles of Incorporation of Registrant dated November 1, 2002, is included as exhibit 3.3 to the Registrant's 10-Q for September 30, 2005, which is incorporated by this reference herein.](#)
- 3.4 [Amendment of the Articles of Incorporation of Registrant dated August 17, 2005, is included as exhibit 3.4 to the Registrant's 10-Q for September 30, 2005, which is incorporated by this reference herein.](#)
- 4 [Specimen form of certificate for Plumas Bancorp included as exhibit 4 to the Registrant's Form S-4, File No. 333-84534, which is incorporated by reference herein.](#)
- 10.1 [Executive Salary Continuation Agreement of Andrew J. Ryback dated December 17, 2008, is included as exhibit 10.1 to the Registrant's 10-K for December 31, 2008, which is incorporated by this reference herein.](#)
- 10.2 [Split Dollar Agreement of Andrew J. Ryback dated August 23, 2005, is included as Exhibit 10.2 to the Registrant's 8-K filed on October 17, 2005, which is incorporated by this reference herein.](#)
- 10.3 [Amendment to Salary Continuation Agreement of Andrew J. Ryback dated April 1, 2019, is included as Exhibit 10.1 to the Registrant's 8-K filed on April 2, 2019, which is incorporated by this reference herein.](#)
- 10.4 [Amendment to Salary Continuation Agreement of Richard L. Belstock dated April 1, 2019, is included as Exhibit 10.2 to the Registrant's 8-K filed on April 2, 2019, which is incorporated by this reference herein.](#)
- 10.5 [Amendment to Salary Continuation Agreement of BJ North dated April 1, 2019, is included as Exhibit 10.3 to the Registrant's 8-K filed on April 2, 2019, which is incorporated by this reference herein.](#)
- 10.6 [Salary Continuation Agreement of Aaron Boigon dated April 1, 2019, is included as Exhibit 10.4 to the Registrant's 8-K filed on April 2, 2019, which is incorporated by this reference herein.](#)
- 10.7 [Promissory Note Dated October 24, 2013, is included as Exhibit 10.6 to the Registrant's 10-Q filed on November 7, 2013, which is incorporated by this reference herein.](#)
- 10.9 [Amendment to Salary Continuation Agreement of Andrew J. Ryback dated April 1, 2016, is included as Exhibit 10.1 to the Registrant's 8-K filed on April 4, 2016, which is incorporated by this reference herein.](#)
- 10.10 [Salary Continuation Agreement of Richard L. Belstock dated April 1, 2016, is included as Exhibit 10.2 to the Registrant's 8-K filed on April 4, 2016, which is incorporated by this reference herein.](#)
- 10.11 [Salary Continuation Agreement of Kerry D. Wilson dated April 1, 2016, is included as Exhibit 10.3 to the Registrant's 8-K filed on April 4, 2016, which is incorporated by this reference herein.](#)
- 10.12 [Salary Continuation Agreement of BJ North dated April 1, 2016, is included as Exhibit 10.4 to the Registrant's 8-K filed on April 4, 2016, which is incorporated by this reference herein.](#)
- 10.13 [Director Retirement Agreement of Steven M. Coldani dated December 21, 2016, is included as Exhibit 10.13 to the Registrant's 10-K filed on March 17, 2017, which is incorporated by this reference herein.](#)
- 10.18 [Amended and Restated Director Retirement Agreement of Daniel E. West dated May 10, 2000, is included as Exhibit 10.18 to the Registrant's 10-QSB for June 30, 2002, which is incorporated by this reference herein.](#)

- 10.19 [Consulting Agreement of Daniel E. West dated May 10, 2000, is included as Exhibit 10.19 to the Registrant's 10-QSB for June 30, 2002, which is incorporated by this reference herein.](#)
- 10.24 [Amended and Restated Director Retirement Agreement of Gerald W. Fletcher dated May 10, 2000, is included as Exhibit 10.24 to the Registrant's 10-QSB for June 30, 2002, which is incorporated by this reference herein.](#)
- 10.25 [Consulting Agreement of Gerald W. Fletcher dated May 10, 2000, is included as Exhibit 10.25 to the Registrant's 10-QSB for June 30, 2002, which is incorporated by this reference herein.](#)
- 10.33 [Amended and Restated Director Retirement Agreement of Terrance J. Reeson dated April 19, 2000, is included as Exhibit 10.33 to the Registrant's 10-QSB for June 30, 2002, which is incorporated by this reference herein.](#)
- 10.34 [Consulting Agreement of Terrance J. Reeson dated May 10, 2000, is included as Exhibit 10.34 to the Registrant's 10-QSB for June 30, 2002, which is incorporated by this reference herein.](#)
- 10.41 [Form of Indemnification Agreement \(Plumas Bancorp\) is included as Exhibit 10.41 to the Registrant's 10-Q for March 31, 2009, which is incorporated by this reference herein.](#)
- 10.42 [Form of Indemnification Agreement \(Plumas Bank\) is included as Exhibit 10.42 to the Registrant's 10-Q for March 31, 2009, which is incorporated by this reference herein.](#)
- 10.47 [2013 Stock Option Plan is included as exhibit 99.1 of the Form S-8 filed September 12, 2013, which is incorporated by this reference herein.](#)
- 10.48 [Specimen Form of Incentive Stock Option Agreement under the 2013 Stock Option Plan is included as exhibit 99.2 of the Form S-8 filed September 12, 2013, which is incorporated by this reference herein.](#)
- 10.49 [Specimen Form of Nonqualified Stock Option Agreement under the 2013 Stock Option Plan is included as exhibit 99.3 of the Form S-8 filed September 12, 2013, which is incorporated by this reference herein.](#)
- 10.51 [First Amendment to Split Dollar Agreement of Andrew J. Ryback, is included as exhibit 10.51 to the Registrant's 10-K for December 31, 2008, which is incorporated by this reference herein.](#)
- 10.66 [Director Retirement Agreement of Robert McClintock, is included as Exhibit 10.66 to the Registrant's 10-K filed on March 23, 2012, which is incorporated by this reference herein.](#)
- 10.67 [First Amendment to the Plumas Bank Amended and Restated Director Retirement Agreement for Terrance J. Reeson adopted on September 19, 2007, is included as Exhibit 10.67 to the Registrant's 8-K filed on September 25, 2007, which is incorporated by this reference herein.](#)
- 10.69 [First Amendment to the Plumas Bank Amended and Restated Director Retirement Agreement for Daniel E. West adopted on September 19, 2007, is included as Exhibit 10.69 to the Registrant's 8-K filed on September 25, 2007, which is incorporated by this reference herein.](#)
- 10.70 [First Amendment to the Plumas Bank Amended and Restated Director Retirement Agreement for Gerald W. Fletcher adopted on October 9, 2007, is included as Exhibit 10.70 to the Registrant's 10-Q for September 30, 2007, which is incorporated by this reference herein.](#)
- 31.1* [Rule 13a-14\(a\) \[Section 302\] Certification of Principal Financial Officer dated October 30, 2019.](#)
- 31.2* [Rule 13a-14\(a\) \[Section 302\] Certification of Principal Executive Officer dated October 30, 2019.](#)
- 32.1* [Certification of Principal Financial Officer pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 dated October 30, 2019.](#)
- 32.2* [Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 dated October 30, 2019.](#)

101.INS* XBRL Instance Document.

101.SCH* XBRL Taxonomy Schema.

101.CAL* XBRL Taxonomy Calculation Linkbase.

101.DEF* XBRL Taxonomy Definition Linkbase.

101.LAB* XBRL Taxonomy Label Linkbase.

101.PRE* XBRL Taxonomy Presentation Linkbase.

* Filed herewith

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

PLUMAS BANCORP

(Registrant)

Date: October 30, 2019

/s/ Richard L. Belstock

Richard L. Belstock
Chief Financial Officer

/s/ Andrew J. Ryback

Andrew J. Ryback
Director, President and Chief Executive Officer

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Section 2: EX-31.1 (EXHIBIT 31.1)

Exhibit 31.1

CERTIFICATION UNDER SECTION 302 OF THE SARBANES OXLEY ACT OF 2002

I, Richard L. Belstock, Chief Financial Officer, certify that:

1. I have reviewed this report on Form 10-Q of Plumas Bancorp;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

- a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
- b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 30, 2019

/s/ Richard L. Belstock
Richard L. Belstock, Chief Financial Officer

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Section 3: EX-31.2 (EXHIBIT 31.2)

Exhibit 31.2

CERTIFICATION UNDER SECTION 302 OF THE SARBANES OXLEY ACT OF 2002

I, Andrew J. Ryback, Chief Executive Officer, certify that:

1. I have reviewed this report on Form 10-Q of Plumas Bancorp;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 30, 2019

/s/ Andrew J. Ryback
Andrew J. Ryback, Chief Executive Officer

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Section 4: EX-32.1 (EXHIBIT 32.1)

Exhibit 32.1

CERTIFICATION OF CHIEF FINANCIAL OFFICER Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of Plumas Bancorp (the "Company") hereby certifies, to such officer's knowledge, that:

- (i) the accompanying Quarterly Report on Form 10-Q of the Company for the quarterly period ended September 30, 2019 (the “Report”) fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: October 30, 2019

/s/ Richard L. Belstock
Richard L. Belstock, Chief Financial Officer

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Section 5: EX-32.2 (EXHIBIT 32.2)

Exhibit 32.2

Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of Plumas Bancorp (the “Company”) hereby certifies, to such officer’s knowledge, that:

- (i) the accompanying Quarterly Report on Form 10-Q of the Company for the quarterly period ended September 30, 2019 (the “Report”) fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: October 30, 2019

/s/ Andrew J. Ryback
Andrew J. Ryback, Chief Executive Officer

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