

**AVIDBANK HOLDINGS, INC.**

**ISSUER INFORMATION AND DISCLOSURE STATEMENT  
PURSUANT TO RULE 15c2-11(a)(5)**

For the Period ended September 30, 2019

**This statement has not been filed with the Securities and Exchange Commission or any other regulatory agency**

The following information is compiled, maintained and made available pursuant to Rule 144(c)(2) of the Securities Act of 1933, as amended, and Rule 15c2-11(a)(5)(i) - (xiv) and (a)(5)(xvi) of the Securities Exchange Act of 1934, as amended (“Securities Exchange Act”). Avidbank Holdings, Inc. (the “Company”) is not subject to Section 13 or 15(d) of the Securities Exchange Act and does not file periodic reports with the Securities and Exchange Commission (“SEC”). In the absence of such filings, this information is intended to satisfy the requirement that adequate current public information with respect to an issuer be available as a condition to the resale of certain securities of the issuer under Rule 144.

**i. the exact name of the issuer and its predecessor (if any);**

The name of the Company is Avidbank Holdings, Inc. The Company’s predecessor and current subsidiary is Avidbank. The Company was formerly Peninsula Bank Holding Co., which was organized in 2007 to be the holding company for The Private Bank of the Peninsula which was incorporated on April 8, 2003 and commenced operations on October 1, 2003. The Private Bank of the Peninsula changed its name to Avidbank on April 1, 2011, and Peninsula Bank Holding Co. changed its name to Avidbank Holdings, Inc. on August 1, 2011.

**ii. the address of its principal executive offices;**

1732 North First Street, 6<sup>th</sup> Floor  
San Jose, California 95112  
telephone: (408) 200-7390  
website: www.avidbank.com

for investor relations issues, contact:

Mark D. Mordell, Chairman and CEO  
1732 North First Street, 6<sup>th</sup> Floor  
San Jose, California 95112  
telephone: (408) 200-7390

**iii. the state of incorporation, if it is a corporation;**

California; incorporated in 2007 to act as the holding company for Avidbank

**iv. the exact title and class of the security; and**

**v. the par or stated value of the security;**

a. 6,079,160 shares of Avidbank Holdings, Inc. Common Stock, no par value,

issued and outstanding as of [September 30, 2019](#); Stock Ticker Symbol – AVBH or AVBH.OB; CUSIP # 05368J103; approximately 475 shareholders of record.

**vi. the number of shares or total amount of the securities outstanding as of the end of the issuer's most recent fiscal year;**

As of December 31, 2018, there were [5,968,148](#) shares of Avidbank Holdings, Inc. Common Stock, no par value, issued and outstanding

As of December 31, 2018, there were [10,000](#) options to purchase the Company's Common Stock issued and outstanding under the Company's equity incentive plan.

**vii. the name and address of the transfer agent;**

**American Stock Transfer & Trust Company, LLC**

6201 15<sup>th</sup> Avenue  
Brooklyn, NY 11219  
Bus: 718.921.8337  
eFax: 718.765.8795

Attention: Craig Colosso

**viii. the nature of the issuer's business;**

Avidbank Holdings, Inc. is a bank holding company registered under the Bank Holding Company Act of 1956, as amended. The Company was incorporated under the laws of the State of California in 2007 for the principal purpose of engaging in activities permitted for a bank holding company. As a bank holding company, the Company is authorized to engage in the activities permitted under the Bank Holding Company Act of 1956, as amended, and the regulations thereunder. Its principal office is located at 1732 North First Street, 6<sup>th</sup> Floor, San Jose, California 95112 and its telephone number is 408 (200)-7390.

The Company owns 100% of the issued and outstanding common shares of its banking subsidiary, Avidbank.

The Bank was incorporated under the laws of the State of California on April 8, 2003, and with the approval of the Department of Financial Institutions and the Federal Deposit Insurance Corporation (the "FDIC"), opened for business on October 1, 2003. In doing so, the Bank became the first locally owned commercial bank to start business in Palo Alto in many years. Avidbank operates in Santa Clara, San Mateo and San Francisco Counties including a head office and branch office in San Jose located at 1732 North First Street, 6<sup>th</sup> floor, San Jose, CA and a full service branch at 437 Lytton Avenue, Suite 100, Palo Alto, CA. The Bank has loan production offices in Redwood City located at 999 Main Street, Suite 100 and in San Francisco located at 135 Main Street, Suite 1130.

Avidbank's deposits are insured by the FDIC up to applicable legal limits. Avidbank's primary business is providing a wide array of financial products with an exemplary level of personal service to small and medium sized businesses, professionals and individuals preferring quality personal attention. The Bank's principal service area is Santa Clara, San Francisco and San Mateo counties, and the Bank utilizes electronic banking systems and an extensive courier service to provide personalized banking services throughout its service area. Avidbank accepts checking

and savings deposits, offers unsecured commercial loans, secured real estate loans, and other installment or term loans and offers other customary banking services. The Bank is a California state-chartered banking institution.

The mission of Avidbank is to provide customized financial services to the San Francisco Bay Area's businesses, professionals, and individuals who desire a high degree of personalized attention.

The Company's Primary SIC Code is 6022, state commercial bank.

For discussion of Supervision and Regulation of the Company and the Bank, see Appendix A.

At [September 30, 2019](#), the company had [107](#) full-time employees and equivalents.

**ix. the nature of products or services offered;**

Avidbank is a full service community bank that specializes in providing financial services to small and medium sized businesses, professionals and individuals in the San Francisco Bay Area. Avidbank's Specialty Finance and Venture Lending Divisions work with companies throughout the country. The products and the marketing focus of the Bank are designed to meet the demands of the Bank's target market. In addition to providing products and services, the Bank emphasizes the establishment of long standing relationships with its customers, and regularly modifies the products and services it offers to meet the unique demands of its customers. The following discussion is a review of the base or core products and services that Avidbank offers and is prepared to structure to meet customer needs.

*Commercial Lending*

The Bank provides a full array of commercial credit products:

- Lines of Credit to finance seasonal cash flow fluctuation.
- Term Loans to finance equipment purchases, business acquisitions and other growth needs.
- Venture Term Loans to bridge companies to their next equity round and provide ongoing working capital.
- Account Receivables / Inventory Lines to finance business with ongoing working capital requirements.
- Invoice Financing Lines to provide ongoing working capital.
- Standby Letters of Credit in lieu of performance bonds or guarantees.

The Bank's commercial and industrial loans have a high degree of industry diversification. A substantial portion of commercial and industrial loans that are not secured by real estate are secured by accounts receivables, inventory, equipment or other collateral. The remainder of the Bank's commercial and industrial loans are unsecured. Both secured and unsecured loans are underwritten based on the underlying historic and projected cash flow of the borrower.

*Commercial Real Estate and Construction Lending*

The Bank provides commercial real estate financing for both construction and mortgage

purposes as well as construction lending on residential properties. Although many real estate borrowers are owners / users of the property constructed and / or permanently financed, the Bank also provides real estate financing for developers. The products offered by the bank include:

- Construction Loans for both residential and commercial projects.
- Commercial Mortgage financing (“Mini Perms”) with maturities up to ten years with longer amortizations.
- Acquisition financing for “build ready” lots that are already zoned and approved for the proposed project.
- Business lines of credit secured on residential or commercial property which provide secured working capital lines to developers.

Real estate mortgage loans are secured by deeds of trust on commercial property with repayment from the cash flow of the borrower.

Real estate construction loans consist of loans to individuals and developers that are secured by single-family and multi-family residential properties and to owner-users and developers that are secured by commercial properties. Repayment of construction loans is generally from long-term mortgages.

#### *Personal Loan Products*

For individuals, Avidbank offers lines of credit on an unsecured basis to qualified borrowers.

#### *Cash Management Services*

For business customers, Avidbank offers an extensive array of cash management products, which can be customized to meet specific customer requirements. Products on the accounts payable side include ACH payments, Bill Pay, Positive Pay, Wire Transfers and Zero Balance Accounts. Products on the accounts receivable side include ACH Collections, Lockbox, Merchant Services, Remote Deposit Capture and Incoming Wire Transfers.

#### *Deposit Products*

Avidbank offers a wide variety of both interest bearing and non-interest bearing transactional accounts for both businesses and individuals. In addition to providing access to deposit accounts via Online (Internet) Banking, the Bank also provides extensive courier service throughout the San Francisco Bay Area so that customers’ deposit and other banking needs may be served without the customer having to make a trip to the Bank. The Bank also offers savings accounts, money market deposit accounts and certificates of deposits for businesses and individuals.

#### *Other Services*

Avidbank offers notary services and medallion guarantee stamps for stock transfers.

It is Avidbank’s intent to provide our customers with easy access to solutions for all their financing needs.

## *Competition*

The Bank's primary market area consists of the San Francisco Bay Area peninsula and nearby communities of adjacent counties. In California generally, and in the Bank's service area specifically, major banks and local regional banks dominate the commercial banking industry. By virtue of their larger capital bases, such institutions have substantially greater lending limits than those of the Bank, as well as more locations, more products and services, greater economies of scale and greater ability to make investments in technology for the delivery of financial services.

As an independent bank, the Bank's principal competitors for deposits and loans are other banks (particularly major banks), savings and loan associations, credit unions, thrift and loans, mortgage brokerage companies and insurance companies. Other institutions, such as mutual funds, brokerage houses, credit card companies and even retail establishments have offered new investment vehicles, such as money-market funds, that also compete with banks. The direction of federal legislation in recent years' favors competition between different types of financial institutions and encourages new entrants into the financial services market, and it is anticipated that this trend will continue.

To compete with larger financial institutions in its service area, the Bank relies upon specialized services, responsive handling of customer needs, local promotional activity, and personal contacts by its officers, directors and staff, compared to large multi-branch banks that compete primarily on interest rates and location of branches. The Bank also assists customers requiring services not offered by the Bank to obtain such services from its correspondent banks. For customers whose loan demands exceed the Bank's lending limits, the Bank seeks to arrange funding for such loans on a participation basis with its correspondent banks or other independent commercial banks. No assurance can be given that the Bank will be able to compete successfully for such loans. Even if the Bank is successful in making such larger loans, larger and stronger borrowers may be more creditworthy and therefore may be able to negotiate for lower interest rates on their loans, which in turn may reduce the net interest margin in the Bank's portfolio.

### **x. the nature and extent of the issuer's facilities;**

The Company and Avidbank lease all four of their current premises.

The Company's headquarters and branch office are located at 1732 North First Street, 6th Floor, San Jose, CA 95112. The landlord is RNM First Street Center, L.P., 135 Main Street, Suite 1140, San Francisco, CA 94105. The premises consist of approximately 28,404 square feet on the sixth floor of the office building. The Bank leased the property for ten years commencing in October 23, 2017 and contains one five-year renewal option.

Avidbank's branch office is located at 437 Lytton Avenue, Suite 100, Palo Alto, CA 94301. The landlord is Manhattan Associates, LP, 3105 Woodside Road, Woodside, CA, 94062. The branch office consists of approximately 2,986 square feet situated on the first floor of the building. The office was leased for a ten-year term commencing on November 13, 2017 and contains one five-year renewal option.

The Bank's Redwood City loan production office opened October 1, 2012 and is located at 999 Main Street, Redwood City, California. The premises consist of approximately 3,575 square feet on the first floor of a two story commercial office building. The office space is leased from Premia 9M, LLC. This lease has a schedule of fixed annual rent increases with the initial term expiring in 2019. The lease contains one five-year renewal option.

The Bank's San Francisco loan production office opened March 30, 2015 and is located at 135 Main Street, Suite 1130, San Francisco, California. The premises consist of approximately 4,375 square feet on the eleventh floor of a twenty-two story commercial office building. The office space is leased from RNM 135 Main, LP. This lease has a schedule of fixed annual rent increases with the term expiring in 2022.

**xi. the name of the chief executive officer and members of the board of directors;**

Name	Age	Position With Company	Director Since	Principal Occupation, Business Experience During Past Five Years and Other Information
Mark D. Mordell	59	Chairman of the Board and CEO	2006	Chairman of the Board and Chief Executive Officer of the Bank and the Company. Mr. Mordell joined the board in January of 2006 and was appointed Chairman in February of 2007. He was named Chief Executive Officer in March of 2012 and brings over 30 years of financial services, real estate and diverse business experience to the bank. He is founder and former board member of CBC Properties, LLC, a full service real estate investment and management organization based in Palo Alto. Mr. Mordell also serves as an advisor to MMM Management, Inc., the strategic advisor to a family office based in San Francisco. He also serves on the board of Seven Peaks Ventures, a Bend, Oregon based venture capital firm.
Kristofer W. Biorn	54	Director	2009	Attorney with the Palo Alto law firm of Crist, Biorn, Shepherd & Roskoph, APC. He has served on the Silicon Valley Bar Association Executive Committee and the Palo Alto Family YMCA Board of Directors.
Kenneth D. Brenner	73	Director and Head Of Strategic Relationships	2007	Mr. Brenner served as Chief Executive Officer of the Bank and the Company from August 2007 until March 2012. From 2001 to 2006, Mr. Brenner was Executive Vice President of Bridge Bank, and President and Manager of their Palo Alto region. He was President and Managing Director of the Venture Banking Group of Cupertino National Bank from 1992 through 2001, and for the seven years prior to that was Senior Vice President at Silicon Valley Bank.

Name	Age	Position With Company	Director Since	Principal Occupation, Business Experience During Past Five Years and Other Information
Lisa B. Hendrickson	67	Director	2006	Former President and CEO of Avenidas, a Palo Alto based not-for-profit senior services agency. Previously she had twenty years of commercial banking experience culminating as Senior Vice President and Manager, Regional Commercial Banking, Wells Fargo Bank, Palo Alto.
Bryan C. Polster	66	Lead Independent Director	2007	Chairman of the Board of Partners and former Managing Partner of Frank, Rimerman & Co. LLP and its subsidiaries. He is a practicing Certified Public Accountant and has served on several committees of the American Institute of Certified Public Accountants. He is a member of the California Society of Certified Public Accountants and previously served on its Board of Directors.
Roxy H. Rapp	81	Director	2007	Founder of Rapp Development, a commercial real estate development company focused on the San Francisco Bay Area. He has served on the Board of Trustees of Menlo College, the Palo Alto Junior Museum & Zoo, the Museum of American Heritage and the Palo Alto Chamber of Commerce.
Michael F. Rosinus	61	Director	2014	Private investor and the founder of TRF Partners, LLC, a consulting firm focusing on investments in community banks and other financial services companies. Mr. Rosinus is a director of Bridgeview Bancorp Inc. and Bridgeview Bank Group. He previously served as a director of Cordia Bancorp and Bank of Virginia, Home Bancorp Inc. and Homebank and NewDominionBank. Before founding TRF Partners, Mr. Rosinus was employed in the banking industry for 18 years, serving as the Chief Lending Officer for M&T Bank in New York City and subsequently the Chief Executive Officer of the Commercial Banking Division for Citibank in Chicago.
Robert H. Scott	64	Director	2017	CEO of Cygilant, Inc., a software as a service network security company. Previously, Rob served as CEO of Bradford Networks, a prominent network security company that was acquired by Fortinet. Prior to that Rob was CEO of Clique Intelligence a software platform for data sharing and collaboration. In 2008 he was appointed, Vice President of Worldwide Sales and Marketing at HP ProCurve Networking. During his career, Rob has steered the helm of several technology companies as president and CEO, including Colubris Networks, a wireless LAN provider, Xelor Software, an IP telephony company, and IPeria, a provider of network-based voice messaging applications.

Name	Age	Position With Company	Director Since	Principal Occupation, Business Experience During Past Five Years and Other Information
Marc Verissimo	63	Director	2017	After stints with Bank of America, First Interstate Bank, and Comerica Bank, Mr. Verissimo joined Silicon Valley Bank in 1993. Over the next 24 years he served on the executive committee and worked in multiple roles including Head of California Banking, Chief Strategy Officer, Chief Risk Officer, and twice held the office as interim Chief Financial Officer. In these positions, he led the California banking team that comprised two thirds of the bank's revenues, oversaw the bank's international expansion into the United Kingdom, China, Israel and India, oversaw IT, HR, Legal, Operations, Finance, Audit, BSA/AML at various times, and finally led credit, enterprise Risk Management, cyber security, compliance, credit review, and regulatory relations among other responsibilities. Mr. Verissimo serves on the board of Pollen VC, a private equity backed FinTech company, and Lighter Capital, a venture capital firm backed FinTech company providing growth capital to companies across the United States.

### *Principal Shareholders*

Principal shareholders owning five percent or more of the Company's issued and outstanding shares of common stock are listed in the table below.

### *Security Ownership of Management, Directors and Principal Shareholders*

The following table sets forth information as of [September 30, 2019](#) pertaining to beneficial ownership of the Company's common stock. The information in the following table has been obtained from the Company's records, or from information furnished directly by the individual or entity to the Company.

For purposes of the following table, shares issuable pursuant to stock options which may be exercised within 60 days of the above date are deemed to be issued and outstanding and have been treated as outstanding in determining the amount and nature of beneficial ownership and in calculating the percentage of ownership of those individuals possessing such interest, but not for any other individuals.



9/30/19

Name and Address of Beneficial Owner (A)	Relationship with Company	Amount and Nature of Beneficial Ownership (B)	Unvested Restricted Stock (C)	Vested Options (D)	% Shares Owned, Restricted Stock and Vested Options
Mark D. Mordell	<i>CEO and Chairman</i>	96,268	35,015	0	2.16%
Kristofer W. Biorn	<i>Director</i>	45,765	3,000	0	0.80%
Lisa B. Hendrickson	<i>Director</i>	31,010	3,000	0	0.56%
Bryan C. Polster	<i>Lead Independent Director</i>	149,353	3,000	0	2.51%
Roxy H. Rapp	<i>Director</i>	100,599	3,000	0	1.70%
Michael F. Rosinus (E)	<i>Director</i>	205,080	3,000	0	3.42%
Robert H. Scott	<i>Director</i>	264	3,000	0	0.05%
Marc Verissimo	<i>Director</i>	0	3,000	0	0.05%
Kenneth D. Brenner	<i>Director and Head of Strategic Relationships</i>	47,803	5,830	0	0.88%
Dori K. Hamilton	<i>Executive Vice President and Chief Banking Officer</i>	34,653	8,925	0	0.22%
Steven J. Leen	<i>Executive Vice President and Chief Financial Officer</i>	25,927	7,310	0	0.55%
Geoffrey E. Butner	<i>Executive Vice President and Chief Credit Officer</i>	2,632	10,950	0	0.72%
All directors and executive officers as a group (12 in number)		739,354	89,030	0	13.63%
Patriot Financial Partners, L.P.	<i>5% or more ownership</i>	548,848	0	0	9.03%

(A) The address for all persons is c/o Avidbank Holdings, Inc., 1732 North First Street, 6th Floor, San Jose, CA 95112.

(B) Includes all shares owned, whether directly or indirectly, individually or together with associates.

(C) Includes all shares of unvested restricted stock issued.

(D) Includes any shares of which beneficial ownership may be acquired within 60 days by exercise of stock options.

(E) Mr. Rosinus has a 50% ownership in PTMR Capital Partners LP which owns 200,000 shares of the company's stock.

## xii. the issuer's \$20 million private offering

On July 13, 2017, Avidbank Holdings, Inc. completed a \$20 million private offering of common shares at a purchase price of \$19.00 per share. Sandler O'Neill + Partners, L.P. acted as the sole placement agent for Avidbank Holdings in connection with the offering. Manatt, Phelps & Phillips, LLP, San Francisco, CA acted as legal counsel to Avidbank Holdings. Sheppard, Mullin, Richter & Hampton LLP acted as legal counsel to the placement agent

**xiii. the issuer's private placement of subordinated notes;**

On November 12, 2015, Avidbank Holdings, Inc. completed a private placement of \$12 million in ten-year, fixed-to-floating rate subordinated notes to certain qualified institutional buyers. The subordinated notes have a maturity date of November 15, 2025 and bear interest at the rate of 6.875% per annum, payable semiannually, for the first five years of the term, and then at a variable rate that will reset quarterly to a level equal to the then current 3-month LIBOR plus 536.7 basis points over the remainder of the term. The notes are redeemable after five years, subject to satisfaction of certain conditions. The indebtedness evidenced by the subordinated notes, including principal and interest, is unsecured and subordinate and junior to general and secured creditors and depositors.

The subordinated notes were issued at the holding company level, and have been structured to qualify as Tier 2 capital for regulatory purposes. The Company plans to use the proceeds from the placement of the subordinated notes for general corporate purposes including, but not limited to, contributing capital to the Bank to fund future growth. Sandler O'Neill + Partners, L.P. acted as placement agent for the private placement of the subordinated notes. The Company was advised by Manatt, Phelps & Phillips, LLP.

**xiv. the issuer's most recent balance sheet and profit and loss and retained earnings statements;**

Please refer to the financial tables below. The balance sheet includes a statement of retained earnings.

**AVIDBANK HOLDINGS, INC. AND SUBSIDIARY**

Unaudited Consolidated Statement of Condition

(In thousands, except number of shares)

<u>Assets</u>	<u>9/30/19</u>	<u>6/30/19</u>	<u>3/31/19</u>	<u>12/31/18</u>	<u>9/30/18</u>
Cash and due from banks	\$24,649	\$12,887	\$12,204	\$19,252	\$13,256
Due from Federal Reserve Bank	90,180	57,530	76,295	8,400	79,670
Total cash and cash equivalents	114,829	70,417	88,499	27,652	92,926
Investment securities - available for sale	53,571	55,002	55,654	56,491	57,401
Loans, net of deferred loan fees	909,312	857,831	831,772	807,339	757,115
Allowance for loan losses	(11,087)	(11,155)	(10,368)	(9,758)	(8,811)
Loans, net of allowance for loan losses	898,225	846,676	821,404	797,581	748,304
Bank owned life insurance	11,088	11,019	10,953	10,890	10,822
Premises and equipment, net	5,238	5,296	5,507	5,723	5,951
Other real estate owned	-	-	-	-	2,094
Accrued interest receivable & other assets	31,751	33,031	31,736	18,568	17,776
Total assets	\$1,114,702	\$1,021,441	\$1,013,753	\$916,905	\$935,274
<u>Liabilities</u>					
Non-interest-bearing demand deposits	\$401,360	\$374,407	\$376,976	\$366,851	\$384,731
Interest bearing transaction accounts	20,114	21,076	28,045	25,378	22,793
Money market and savings accounts	287,082	283,734	297,941	267,185	249,580
Time deposits	179,645	150,952	143,834	137,183	132,439
Total deposits	888,201	830,169	846,796	796,597	789,543
FHLB advances	80,000	50,000	30,000	-	30,000
Subordinated debt, net	11,908	11,887	11,866	11,845	11,824
Other liabilities	21,897	20,750	20,607	7,947	7,286
Total liabilities	1,002,006	912,806	909,269	816,389	838,653
<u>Shareholders' equity</u>					
Common stock/additional paid-in capital	68,851	68,583	68,157	68,012	67,891
Retained earnings	43,861	40,408	37,226	34,053	30,581
Accumulated other comprehensive income (loss)	(16)	(356)	(899)	(1,549)	(1,851)
Total shareholders' equity	112,696	108,635	104,484	100,516	96,621
Total liabilities and shareholders' equity	\$1,114,702	\$1,021,441	\$1,013,753	\$916,905	\$935,274
<u>Capital ratios</u>					
Tier 1 leverage ratio	10.84%	10.69%	10.86%	10.82%	11.07%
Common equity tier 1 capital ratio	10.16%	10.28%	10.22%	10.38%	10.39%
Tier 1 risk-based capital ratio	10.16%	10.28%	10.22%	10.38%	10.39%
Total risk-based capital ratio	12.26%	12.49%	12.41%	12.62%	12.61%
Book value per common share	\$18.54	\$17.88	\$17.28	\$16.84	\$16.17
Total common shares outstanding	6,079,160	6,075,429	6,047,136	5,968,148	5,974,645
<u>Other Ratios</u>					
Non-interest bearing deposits to total deposits	45.2%	45.1%	44.5%	46.1%	48.7%
Core deposits to total deposits	82.5%	84.7%	85.8%	85.4%	85.9%
Loan to deposit ratio	102.4%	103.3%	98.2%	101.3%	95.9%
Allowance for loan losses to total loans	1.22%	1.30%	1.25%	1.21%	1.16%

**AVIDBANK HOLDINGS, INC. AND SUBSIDIARY**

Unaudited Consolidated Statements of Income

(In thousands, except per share data)

	Quarter Ended			Year to Date	
	9/30/19	6/30/19	9/30/18	9/30/19	9/30/18
Interest and fees on loans and leases	\$12,465	\$12,307	\$10,176	\$36,601	\$28,553
Interest on investment securities	328	359	350	1,062	1,209
Other interest income	300	418	349	1,001	730
Total interest income	<u>13,093</u>	<u>13,084</u>	<u>10,875</u>	<u>38,664</u>	<u>30,492</u>
Deposit interest expense	1,381	1,234	800	3,752	1,990
Other interest expense	548	425	479	1,280	1,370
Total interest expense	<u>1,929</u>	<u>1,659</u>	<u>1,279</u>	<u>5,032</u>	<u>3,360</u>
Net interest income	11,164	11,425	9,596	33,632	27,132
Provision for loan losses	39	787	665	1,285	665
Net interest income after provision for loan losses	11,125	10,638	8,931	32,347	26,467
Service charges, fees and other income	615	555	453	1,648	1,576
Income from bank owned life insurance	69	66	68	198	203
Gain on sale of assets	2	0	0	351	17
Total non-interest income	<u>686</u>	<u>621</u>	<u>521</u>	<u>2,197</u>	<u>1,796</u>
Compensation and benefit expenses	4,972	4,605	3,619	14,375	11,258
Occupancy and equipment expenses	881	863	842	2,687	2,638
Other operating expenses	1,140	1,202	1,201	3,668	3,757
Total non-interest expense	<u>6,993</u>	<u>6,670</u>	<u>5,662</u>	<u>20,730</u>	<u>17,653</u>
Income before income taxes	4,818	4,589	3,790	13,814	10,610
Provision for income taxes	1,366	1,406	925	4,006	2,971
Net income	<u>\$3,452</u>	<u>\$3,183</u>	<u>\$2,865</u>	<u>\$9,808</u>	<u>\$7,639</u>
Basic earnings per common share	\$0.59	\$0.55	\$0.50	\$1.69	\$1.33
Diluted earnings per common share	\$0.58	\$0.54	\$0.49	\$1.66	\$1.30
Average common shares outstanding	5,807,384	5,799,847	5,767,950	5,796,782	5,751,400
Average common fully diluted shares	5,919,698	5,907,107	5,879,337	5,904,960	5,865,859
Annualized returns:					
Return on average assets	1.32%	1.25%	1.28%	1.30%	1.22%
Return on average common equity	12.31%	11.90%	11.82%	12.22%	10.95%
Net interest margin	4.49%	4.74%	4.47%	4.70%	4.53%
Cost of funds	0.84%	0.75%	0.65%	0.76%	0.61%
Efficiency ratio	59.01%	55.37%	55.97%	57.86%	61.02%

**xv. similar financial information for such part of the two preceding fiscal years as the issuer or its predecessor has been in existence;**

Please refer to the Company's audited balance sheets as of December 31, 2018 and December 31, 2017 and related consolidated statements of income, statements of shareholders' equity and comprehensive income cash flows for each of the years in the three-year period ending December 31, 2018 in conformity with generally accepted accounting principles together with the report of independent certified public accountants included in Avidbank Holdings, Inc.'s 2018 Annual Report.

A copy of the Company's 2018 Annual Report can be found on the home page of the company's web site [www.avidbank.com](http://www.avidbank.com) under the title Investor Relations followed by the subtitle Financial Documents.

**xvi. whether a broker or dealer or any associated person is affiliated, directly or indirectly with the issuer;**

No broker or dealer or any associated person is affiliated, directly or indirectly, with the Company in connection with any shares of the Company's common stock that may be resold under Rule 144. One or more brokers or dealers facilitate trades in the Company's common stock and may act as informal market makers. However, no broker or dealer has any obligation to purchase or sell any of the Company's shares of common stock at any time and may discontinue any market making activities at any time.

**xvii. [omitted]**

**xviii. whether the quotation is being submitted or published directly or indirectly on behalf of the issuer, or any director, officer or any person, directly or indirectly the beneficial owner of more than 10 percent of the outstanding units or shares of any equity security of the issuer, and, if so, the name of such person, and the basis for any exemption under the federal securities laws for any sales of such securities on behalf of such person.**

To the best knowledge of the Company, there is no quotation being submitted or published directly or indirectly on behalf of the Company, or any director, officer or any person directly or indirectly the beneficial owner of more than 10 percent of the outstanding units or shares of any equity security of the Company, or at the request of any promoter for the Company.

As of the date of this disclosure, officers or directors of the Company for whose account a broker or dealer is offering to sell shares of the Company's common stock include the following:

**NONE as of September 30, 2019**

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The Company's regular outside counsel is Manatt, Phelps & Phillips, LLP, San Francisco, California. The Company's independent public accounting firm is Crowe LLP. The services provided by Crowe LLP include the auditing and reporting of the financial status of the

Company.

This information has been prepared by the Company. If this information is made available by a broker or dealer to other persons pursuant to a request under Rule 15c2-11, delivery of this information to other persons shall not constitute a representation by the broker or dealer that the information is accurate.

Date on which this information was last revised: **September 30, 2019**

No dealer, salesman or any other person has been authorized to give any information, or to make any representations, not contained herein in connection with the issuer. Such information or representations, if made, must not be relied upon as having been authorized by the issuer.

Delivery of this information file does not at any time imply that the information contained herein is correct as of any time subsequent to the date above.

## Appendix A

### SUPERVISION AND REGULATION

#### General

Avidbank Holdings, Inc. (the “Company”) is a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended (the “Bank Holding Company Act”), and is registered as such with, and subject to the supervision of, the Board of Governors. The Company is required to obtain the approval of the Board of Governors before it may acquire all or substantially all of the assets of any bank, or ownership or control of the voting shares of any bank if, after giving effect to such acquisition of shares, the Company would own or control more than 5% of the voting shares of such bank. The Bank Holding Company Act prohibits the Company from acquiring any voting shares of, or interest in, all or substantially all of the assets of, a bank located outside the State of California unless such an acquisition is specifically authorized by the laws of the state in which such bank is located. Any such interstate acquisition is also subject to applicable California and federal law.

The common stock of the Company is subject to the registration requirements of the Securities Act of 1933, as amended, and the qualification requirements of the California Corporate Securities Law of 1968, as amended.

The Company, and any subsidiaries which it may acquire or organize, are deemed to be “affiliates” within the meaning of that term as defined in the Federal Reserve Act. This means, for example, that there are limitations (a) on loans by Avidbank to affiliates, (b) on investments by Avidbank in affiliates’ stock as collateral for loans to any borrower, and (c) other transactions between any bank subsidiary and the Company. The Company and its subsidiaries are also subject to certain restrictions with respect to engaging in the underwriting, public sale and distribution of securities.

Avidbank is licensed by the California Commissioner (the “Commissioner”) of the Department of Business Oversight (the “DBO”), and its deposits are insured by the FDIC up to the applicable legal limits. Avidbank shares and Avidbank are required to file reports with the Board of Governors, the Commissioner, and the FDIC and provide any additional information that the Board of Governors, the Commissioner, and the FDIC may require.

#### Capital Standards

Federal regulations require FDIC insured depository institutions, including state-chartered banks, to meet several minimum capital standards: a common equity Tier 1 capital to risk-based assets ratio, a Tier 1 capital to risk-based assets ratio, a total capital to risk-based assets and a Tier 1 capital to total assets leverage ratio. The existing capital requirements were effective January 1, 2015 and are the result of a final rule implementing regulatory amendments based on recommendations of the Basel Committee on Banking Supervision and certain requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”).

The capital standards require the maintenance of common equity Tier 1 capital, Tier 1 capital and total capital to risk-weighted assets of at least 4.5%, 6% and 8%, respectively, and a leverage ratio of at least 4% Tier 1 capital. Common equity Tier 1 capital is generally defined as common stockholders’ equity and retained earnings. Tier 1 capital is generally defined as common equity Tier 1 and Additional Tier 1 capital. Additional Tier 1 capital generally includes certain noncumulative

perpetual preferred stock and related surplus and minority interests in equity accounts of consolidated subsidiaries. Total capital includes Tier 1 capital (common equity Tier 1 capital plus Additional Tier 1 capital) and Tier 2 capital. Tier 2 capital is comprised of capital instruments and related surplus meeting specified requirements, and may include cumulative preferred stock and long-term perpetual preferred stock, mandatory convertible securities, intermediate preferred stock and subordinated debt. Also included in Tier 2 capital is the allowance for loan and lease losses limited to a maximum of 1.25% of risk-weighted assets and, for institutions that have exercised an opt-out election regarding the treatment of Accumulated Other Comprehensive Income (“AOCI”), up to 45% of net unrealized gains on available-for-sale equity securities with readily determinable fair market values. Institutions that have not exercised the AOCI opt-out have AOCI incorporated into common equity Tier 1 capital (including unrealized gains and losses on available-for-sale securities). We exercised the opt-out election regarding the treatment of AOCI. Calculation of all types of regulatory capital is subject to deductions and adjustments specified in the regulations.

In determining the amount of risk-weighted assets for purposes of calculating risk-based capital ratios, a bank’s assets, including certain off-balance sheet assets (e.g., recourse obligations, direct credit substitutes, residual interests), are multiplied by a risk weight factor assigned by the regulations based on perceived risks inherent in the type of asset. Higher levels of capital are required for asset categories believed to present greater risk. For example, a risk weight of 0% is assigned to cash and U.S. government securities, a risk weight of 50% is generally assigned to prudently underwritten first lien 1 – 4 family residential mortgages, a risk weight of 100% is assigned to commercial and consumer loans, a risk weight of 150% is assigned to certain past due loans and a risk weight of between 0% to 600% is assigned to permissible equity interests, depending on certain specified factors.

In addition to establishing the minimum regulatory capital requirements, the regulations limit capital distributions and certain discretionary bonus payments to management if the institution does not hold a “capital conservation buffer” consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets above the amount necessary to meet its minimum risk-based capital requirements. The capital conservation buffer requirement was phased in beginning January 1, 2016 at 0.625% of risk-weighted assets and increasing each year until now fully implemented at 2.5% as of January 1, 2019.

Management believes that Avidbank is in compliance with the minimum capital requirements, including the fully phased-in capital conservation buffer requirement based upon its capital position at March 31, 2019.

In accordance with the Dodd-Frank Act and long-standing Federal Reserve policy, the Company must act as a source of financial and managerial strength to Avidbank. Under this policy, the Company must commit resources to support the Bank, including at times when the Company may not be in a financial position to provide it. The Company could be required to guarantee the capital plan of Avidbank if it becomes undercapitalized for purposes of banking regulations, as described below. Any capital loans by a bank holding company to its subsidiary bank are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary bank. The Bank Holding Company Act of 1956, as amended (the “BHC Act”) provides that, in the event of a bank holding company’s bankruptcy, any commitment by the bank holding company to a federal bank regulatory agency to maintain the capital of a bank subsidiary will be assumed by the bankruptcy trustee and entitled to priority of payment.

In February, 2019, the Office of the Comptroller of the Currency, the FRB and the FDIC (collectively, the agencies) issued a notice of proposed rulemaking that would provide a simplified



measure of capital adequacy for qualifying community banking organizations (including institutions who have less than \$10 billion in assets (such as Avidbank) and meet certain other criteria) consistent with section 201 of the Economic Growth, Regulatory Relief, and Consumer Protection Act. Qualifying community banking organizations that comply with and elect to use the community bank leverage ratio (CBLR) framework and that maintain a CBLR greater than 9 percent would be considered to have met the capital requirements for the “well-capitalized” capital category under the agencies’ prompt corrective action (PCA) frameworks and would no longer be subject to the generally applicable capital rule.

### **Safety and Soundness Standards**

Each federal banking agency, including the FDIC, has adopted guidelines establishing general standards relating to internal controls, information and internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, asset quality, earnings, compensation, fees and benefits and information security standards. In general, the guidelines require appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines. The guidelines prohibit excessive compensation as an unsafe and unsound practice and describe compensation as excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director, or principal stockholder. The FDIC also has issued guidance on risks banks may face from third party relationships (e.g. relationships under which the third party provides services to the bank). The guidance generally requires the bank to perform adequate due diligence on the third party, appropriately document the relationship, and perform adequate oversight and auditing, in order to the limit the risks to the bank.

### **Prompt Corrective Regulatory Action**

Federal law requires that federal bank regulatory authorities take “prompt corrective action” with respect to institutions that do not meet minimum capital requirements. For these purposes, the statute establishes five capital tiers: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized.

State banks that have insufficient capital are subject to certain mandatory and discretionary supervisory measures. For example, a bank that is “undercapitalized” (i.e. fails to comply with any regulatory capital requirement) is subject to growth limitations and is required to submit a capital restoration plan; a holding company that controls such a bank is required to guarantee that the bank complies with the restoration plan. A “significantly undercapitalized” bank is subject to additional restrictions. State banks deemed by the FDIC to be “critically undercapitalized” are subject to the appointment of a receiver or conservator.

The final rule that increased regulatory capital standards also adjusted the prompt corrective action tiers as of January 1, 2015 to conform to the new capital standards. The various categories now incorporate the newly adopted common equity Tier 1 capital requirement, an increase in the Tier 1 to risk-based assets requirement and other changes. Under the revised prompt corrective action requirements, insured depository institutions are required to meet the following in order to qualify as “well capitalized:” (1) a common equity Tier 1 risk-based capital ratio of 6.5% (new standard); (2) a Tier 1 risk-based capital ratio of 8% (increased from 6%); (3) a total risk-based capital ratio of 10% (unchanged) and (4) a Tier 1 leverage ratio of 5% (unchanged). Avidbank’s capital ratios are set forth above in the income statement section at the bottom of page 11.

## **Additional Regulations**

Under the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), the federal financial institution agencies have adopted regulations which require institutions to establish and maintain comprehensive written real estate policies which address certain lending considerations, including loan-to-value limits, loan administrative policies, portfolio diversification standards, and documentation, approval and reporting requirements. The FDICIA further generally prohibits an insured state bank from engaging as a principal in any activity that is impermissible for a national bank, absent FDIC determination that the activity would not pose a significant risk to the Bank Insurance Fund, and that the bank is, and will continue to be, within applicable capital standards.

The Federal Financial Institution Examination Counsel (“FFIEC”) utilizes the Uniform Financial Institutions Rating System (“UFIRS”) commonly referred to as “CAMELS” to classify and evaluate the soundness of financial institutions. Bank examiners use the CAMELS measurements to evaluate capital adequacy, asset quality, management, earnings, liquidity and sensitivity to market risk. Effective January 1, 2005, bank holding companies such as the Company, were subject to evaluation and examination under a revised bank holding company rating system. The so-called BOPEC rating system implemented in 1979 was primarily focused on financial condition, consolidated capital and consolidated earnings. The rating system reflects the change toward analysis of risk management (as reflected in bank examination under the CAMELS measurements), in addition to financial factors and the potential impact of non-depository subsidiaries upon depository institution subsidiaries.

The federal financial institution agencies have established bases for analysis and standards for assessing a financial institution’s capital adequacy in conjunction with the risk-based and Basel III capital guidelines including analysis of interest rate risk, concentrations of credit risk, risk posed by non-traditional activities, and factors affecting overall safety and soundness. The safety and soundness standards for insured financial institutions include analysis of (1) internal controls, information systems and internal audit systems; (2) loan documentation; (3) credit underwriting; (4) interest rate exposure; (5) asset growth; (6) compensation, fees and benefits; and (7) excessive compensation for executive officers, directors or principal shareholders which could lead to material financial loss. If an agency determines that an institution fails to meet any standard, the agency may require the financial institution to submit to the agency an acceptable plan to achieve compliance with the standard. If the agency requires submission of a compliance plan and the institution fails to timely submit an acceptable plan or to implement an accepted plan, the agency must require the institution to correct the deficiency. The agencies may elect to initiate enforcement action in certain cases rather than rely on an existing plan particularly where failure to meet one or more of the standards could threaten the safe and sound operation of the institution.

Community Reinvestment Act (“CRA”) regulations evaluate banks’ lending to low and moderate income individuals and businesses across a four-point scale from “outstanding” to “substantial noncompliance,” and are a factor in regulatory review of applications to merge, establish new branches or form bank holding companies. In addition, any bank rated in “substantial noncompliance” with the CRA regulations may be subject to enforcement proceedings. In its most recent exam for CRA compliance, Avidbank has a rating of “satisfactory.”

## **Limitations on Dividends, Repurchases and Redemptions**

The Company’s ability to pay cash dividends is subject to restrictions set forth in the California General Corporation Law. Funds for payment of any cash dividends by the Company would be obtained from its investments as well as dividends and/or management fees from its subsidiaries, including Avidbank. The payment of cash dividends and/or management fees by

Avidbank is subject to restrictions set forth in the California Financial Code, as well as restrictions established by the FDIC. Under the California Financial Code, funds available for cash dividend payments by a bank are restricted to the lesser of: (i) retained earnings; or (ii) Avidbank's net income for its last three fiscal years (less any distributions to shareholders made during such period). However, under the California Financial Code, with the prior approval of the Commissioner, a bank may pay cash dividends in an amount not to exceed the greater of the: (1) retained earnings of the bank; (2) net income of the bank for its last fiscal year; or (3) net income of the bank for its current fiscal year. However, if the state finds that the shareholders' equity of the bank is not adequate or that the payment of a dividend would be unsafe or unsound, the Commissioner may order such bank not to pay a dividend to shareholders. The Company does not currently pay any cash dividends and we cannot provide any assurance that we will pay dividends in the future.

It is an essential principle of safety and soundness that a banking organization's redemption and repurchases of regulatory capital instruments, including common stock, from investors be consistent with the organization's current and prospective capital needs. Consultation with the Federal Reserve before redeeming any equity or other capital instrument included in Tier 1 or Tier 2 capital is generally advisable in all circumstances and is required if such redemption could have a material effect on the level or composition of the organization's capital base. Bank holding companies that are experiencing financial weaknesses, or that are at significant risk of developing financial weaknesses, must consult with the appropriate Federal Reserve supervisory staff before redeeming or repurchasing common stock or other regulatory capital instruments for cash or other valuable consideration. Similarly, any bank holding company considering expansion, whether through acquisitions or through organic growth and new activities, generally also must consult with the appropriate Federal Reserve supervisory staff before redeeming or repurchasing common stock or other regulatory capital instruments for cash or other valuable consideration. In evaluating the appropriateness of a bank holding company's proposed redemption or repurchase of capital instruments, the Federal Reserve will consider the potential losses that the holding company may suffer from the prospective need to increase reserves and write down assets from continued asset deterioration and the holding company's ability to raise additional common stock and other Tier 1 capital to replace capital instruments that are redeemed or repurchased. A bank holding company must inform the Federal Reserve of a redemption or repurchase of common stock or perpetual preferred stock for cash or other value resulting in a net reduction of the bank holding company's outstanding amount of common stock or perpetual preferred stock below the amount of such capital instrument outstanding at the beginning of the quarter in which the redemption or repurchase occurs. In addition, a bank holding company must advise the Federal Reserve sufficiently in advance of such redemptions and repurchases to provide reasonable opportunity for supervisory review and possible objection should the Federal Reserve determine a transaction raises safety and soundness concerns.

Bank holding company that are not well capitalized or well managed, or that are subject to any unresolved supervisory issues, must provide prior notice to the Federal Reserve for any repurchase or redemption of its equity securities for cash or other value that would reduce by 10% or more the holding company's consolidated net worth aggregated over the preceding 12-month period.

### **FDIC Insurance**

On October 3, 2008, the Emergency Economic Stabilization Act of 2008 (the "EESA") was signed into law. The EESA temporarily raised the limit on federal deposit insurance coverage provided by the FDIC from \$100,000 to \$250,000 per depositor. On July 21, 2010, President Obama signed the Dodd-Frank Act into law. On November 9, 2010, the FDIC issued a final rule implementing section 343 of the Dodd-Frank Act that permanently raised the current standard maximum deposit insurance amount per depositor to \$250,000. In addition, the Dodd-Frank Act also

made other deposit insurance changes which may affect our insurance premium assessments to include (i) amendment of the assessment base used to calculate an insured depository institution's deposit insurance premiums paid to the DIF by elimination of deposits and substitution of average consolidated total assets less average tangible equity during the assessment period as the revised assessment base; (ii) increasing the minimum designated reserve ratio of the DIF from 1.15 percent to 1.35 percent of the estimated amount of total insured deposits; (iii) eliminating the requirement that the FDIC pay dividends to depository institutions when the reserve ratio exceeds certain thresholds; and (iv) repeal of the prohibition upon the payment of interest on demand deposits to be effective one year after the date of enactment of the Dodd-Frank Act.

On November 18, 2014, the FDIC adopted the Assessments Final Rule which revises the FDIC's risk-based deposit insurance assessment system to reflect changes in the regulatory capital rules adopted by the federal banking agencies as part of the so-called Basel III capital regulations to conform the prompt corrective action capital ratios and ratio thresholds for "well capitalized" and "adequately capitalized" evaluations.

On June 16, 2015, the FDIC proposed changes to the deposit insurance assessments for small insured banks having total assets less than \$10 Billion which have been insured for at least five years, based upon experience with bank failures. The changes, among other matters, revise the financial ratios method of determining assessments to reflect a statistical model estimating the probability of failure over three years and updating the financial measures used in the financial ratios method consistent with the statistical model. The FDIC proposed additional changes on October 22, 2015 to require banks with over \$10 Billion in assets to be responsible for the recapitalization of the DIF to 1.35 percent of insured deposits after achieving a 1.15 percent reserve ratio. On January 21, 2016, the FDIC proposed further revisions to the small insured bank assessments as the result of comments and recommendations received in response to its earlier proposal. The FDIC proposed that a final rule would go into effect the quarter after adoption, but the amendments would not become operative until the quarter after the DIF reserve ratio reached 1.15 percent. The DIF achieved a reserve ratio of 1.17 as of June 30, 2016. Among the effects of the amendments was a reduction in the initial assessment rates for all banks. On September 30, 2018, the DIF reached 1.36%. Because the reserve ratio has exceeded 1.35%, two deposit insurance assessment changes occurred under the FDIC regulations: 1) surcharges on large banks (total consolidated assets of \$10 billion or more) ended; the last surcharge on large banks was collected on December 28, 2018 and 2) small banks (total consolidated assets of less than \$10 billion) were awarded assessment credits for the portion of their assessments that contributed to the growth in the reserve ratio from 1.15% to 1.35%, to be applied when the reserve ratio is at least 1.38%.

Although Avidbank's recent assessments have declined as a result of the change to the deposit assessment system, it is uncertain what effect the implementation of the changes to the insurance assessments will have upon the Company's cost of operations in the future, but a deterioration in the economic conditions impacting financial institutions or a significant number of failed institutions might necessitate increases in premium assessments to maintain the DIF which could adversely impact the Company's earnings.

### **Impact of Certain Legislation and Regulation**

*Interstate Banking.* The Dodd-Frank Act signed into law by President Obama on July 21, 2010, includes provisions authorizing national and state banks to establish branch offices in other states to the same extent as a bank chartered by that state would be permitted to branch. Previously, banks could only establish branch offices in other states if the host state expressly permitted out-of-

state banks to establish branch offices in that state. Accordingly, banks may be able to enter new markets more freely.

*Gramm-Leach-Bliley Act.* In 1999, the Gramm-Leach-Bliley Act (the “GLB Act”) was signed into law. The GLB Act eliminated most of the remaining depression-era “firewalls” between banks, securities firms and insurance companies which were established by The Banking Act of 1933, also known as the Glass-Steagall Act (“Glass-Steagall”). Glass-Steagall sought to insulate banks as depository institutions from the perceived risks of securities dealing and underwriting, and related activities. The GLB Act permitted bank holding companies that could qualify as “financial holding companies” to acquire securities firms or create them as subsidiaries, and securities firms could acquire banks or start banking activities through a financial holding company. Prior to the GLB Act, banks were also (with minor exceptions) prohibited from engaging in insurance activities or affiliating with insurers. The GLB Act removed these restrictions and substantially eliminated the prohibitions under the Bank Holding Company Act on affiliations between banks and insurance companies. Consequently, the common ownership of banks, securities firms and insurance firms was possible, in addition to the conduct of commercial banking, merchant banking, investment management, securities underwriting and insurance within a single financial institution using a “financial holding company” structure authorized by the GLB Act.

A bank holding company could qualify as a financial holding company if (i) its banking subsidiaries are “well capitalized” and “well managed” and (ii) it files with the Board of Governors a certification to such effect and a declaration that it elects to become a financial holding company. The Bank Holding Company Act was amended to permit financial holding companies to engage in activities, and acquire companies engaged in activities, that are financial in nature or incidental to such financial activities. Financial holding companies were also permitted to engage in activities that were complementary to financial activities if the Board of Governors determined that the activity did not pose a substantial risk to the safety or soundness of depository institutions or the financial system in general. These standards expanded upon the list of activities “closely related to banking” which have defined the permissible activities of bank holding companies under the Bank Holding Company Act. Neither the Company nor Avidbank has determined whether or when to seek to acquire and exercise powers or activities under the GLB Act.

*Volcker Rule.* On December 10, 2013, the federal banking agencies jointly issued a final rule implementing the so-called “Volcker Rule” (set forth in Section 619 of the Dodd-Frank Act). The Volcker Rule prohibits depository institutions, companies that control such institutions, bank holding companies, and the affiliates and subsidiaries of such banking entities, from engaging as principal for the trading account of the banking entity in any purchase or sale of one or more covered financial instruments (so-called “proprietary trading”) and imposes limitations upon retaining ownership interests in, sponsoring, investing in and transacting with certain investment funds, including hedge funds and private equity funds. Management believes the investment portfolio and activities of Avidbank and the Company are in compliance with the Volcker Rule and its implementing regulations.

*Change in Bank Control Act.* Subject to various exceptions, the BHC Act and the Change in Bank Control Act, together with related regulations, require Federal Reserve approval prior to any person’s or company’s acquiring “control” of a bank holding company. Under a rebuttable presumption established by the Federal Reserve pursuant to the Change in Bank Control Act, the acquisition of 10% or more of a class of voting stock of a bank holding company would constitute acquisition of control of the bank holding company if no other person will own, control, or hold the power to vote a greater percentage of that class of voting stock immediately after the transaction or the bank holding company has registered securities under the Exchange Act. In addition, any person or

group of persons acting in concert must obtain the approval of the Federal Reserve under the BHC Act before acquiring 25% (5% in the case of an acquirer that is already a bank holding company) or more of the outstanding voting stock of a bank holding company, the right to control in any manner the election of a majority of the company's directors, or otherwise obtaining control or a "controlling influence" over the bank holding company. The California Financial Code has similar regulations applicable to acquisition of securities of a California-chartered bank holding company and bank, such as the Company and Avidbank.

*Patriot Act.* On October 26, 2001, President Bush signed the USA Patriot Act (the "Patriot Act"), which includes provisions pertaining to domestic security, surveillance procedures, border protection, and terrorism laws to be administered by the Secretary of the Treasury. Title III of the Patriot Act entitled, "International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001" includes amendments to the Bank Secrecy Act which expand the responsibilities of financial institutions in regard to anti-money laundering activities with particular emphasis upon international money laundering and terrorism financing activities through designated correspondent and private banking accounts.

The Patriot Act contains various provisions that affect the operations of financial institutions by encouraging cooperation among financial institutions, regulatory authorities and law enforcement authorities with respect to individuals, entities and organizations engaged in, or reasonably suspected of engaging in, terrorist acts or money laundering activities. The Company and Avidbank are not currently aware of any account relationships between Avidbank and any foreign bank or other person or entity which would not be in compliance with the Patriot Act.

The effects which the Patriot Act and any amendments to the Patriot Act or additional legislation enacted by Congress may have upon financial institutions is uncertain; however, such legislation could increase compliance costs and thereby potentially may have an adverse effect upon the Company's results of operations.

*Sarbanes-Oxley Act.* On July 30, 2002, President Bush signed into law the Sarbanes-Oxley Act of 2002 (the "Act") which responded to issues in corporate governance and accountability. Among other matters, key provisions of the Act and rules promulgated by the SEC pursuant to the Act include enhancement of financial disclosures and related certification requirements, rules related to audit committees, auditor independence, ethics requirements, securities trading prohibitions, securities reporting requirements, and securities listing requirements.

*Fair and Accurate Credit Transactions Act.* The Board of Governors, the FDIC, the other federal financial institution regulatory agencies, and the Federal Trade Commission issued final rules and guidelines effective January 1, 2008, subject to mandatory compliance as of November 1, 2008, implementing sections 114 and 315 of the Fair and Accurate Credit Transactions Act of 2003 to require financial institutions and other creditors to develop and implement a written identity theft prevention program. The program must include reasonable policies and procedures for detecting, preventing, and mitigating identity theft in connection with certain new and existing covered accounts. Covered accounts are defined as (i) an account primarily for personal, family, or household purposes (i.e., consumer accounts), or (ii) any other account for which there is a reasonably foreseeable risk to customers or the safety and soundness of the financial institution or creditor from identity theft. The program must be appropriate to the size and complexity of the financial institution or creditor and the nature and scope of its activities and should be designed to:

- identify relevant patterns, practices, and specific forms of activity that are "red flags" of possible identity theft and incorporate those red flags into the program;
- detect the occurrence of red flags incorporated into the program;

- respond appropriately to any red flags that are detected to prevent and mitigate identity theft; and
- ensure that the program is updated periodically to reflect changes in risks to customers or to the safety and soundness of the financial institution or creditor from identity theft.

The regulations include guidelines that each financial institution must consider and, to the extent appropriate, include in its program and steps that must be taken to administer the program including (i) obtaining approval of the program by the board of directors or a committee of the board, (ii) ensuring oversight of the development, implementation and administration of the program, (iii) training staff, and (iv) overseeing service provider arrangements. The guidelines contemplate that existing fraud prevention procedures may be incorporated into the program.

*Office of Foreign Assets Control Regulation.* The United States has imposed economic sanctions that affect transactions with designated foreign countries, foreign nationals and others. These are typically known as the “OFAC” rules based on their administration by the U.S. Department of the Treasury Office of Foreign Assets Control (“OFAC”). The OFAC-administered sanctions targeting countries take many different forms. Generally, however, they contain one or more of the following elements: (i) restrictions on trade with or investment in a sanctioned country, including prohibitions against direct or indirect imports from and exports to a sanctioned country and prohibitions on “U.S. persons” engaging in financial transactions relating to making investments in, or providing investment-related advice or assistance to, a sanctioned country; and (ii) a blocking of assets in which the government or specially designated nationals of the sanctioned country have an interest, by prohibiting transfers of property subject to U.S. jurisdiction (including property in the possession or control of U.S. persons). Blocked assets (e.g., property and bank deposits) cannot be paid out, withdrawn, set off or transferred in any manner without a license from OFAC. Avidbank is responsible for, among other things, blocking accounts of, and transactions with, such targets and countries, prohibiting unlicensed trade and financial transactions with them and reporting blocked transactions after their occurrence. Failure to comply with these sanctions could have serious legal and reputational consequences.

*The Dodd-Frank Act.* On July 21, 2010, President Obama signed into law the Dodd-Frank Act. The Dodd-Frank Act is intended to restructure the regulation of the financial services sector by, among other things, (i) establishing a framework to identify systemic risks in the financial system implemented by a newly created Financial Stability Oversight Council and other federal banking agencies; (ii) expanding the resolution authority of the federal banking agencies over troubled financial institutions; (iii) authorizing changes to capital and liquidity requirements; (iv) changing deposit insurance assessments; and (v) enhancing regulatory supervision to improve the safety and soundness of the financial services sector. Below is a summary of certain provisions of the Dodd-Frank Act which, directly or indirectly, may affect us.

- *Changes to Capital Requirements.* The federal banking agencies are required to establish revised minimum leverage and risk-based capital requirements for banks and bank holding companies. The Dodd-Frank Act requires capital requirements to be counter cyclical so that the required amount of capital increases in times of economic expansion and decreases in times of economic contraction consistent with safety and soundness.
- *Enhanced Regulatory Supervision.* The Dodd-Frank Act increases regulatory oversight, supervision and examination of banks, bank holding companies and their respective subsidiaries by the appropriate regulatory agency.

- *Consumer Protection.* The Dodd-Frank Act created the Consumer Financial Protection Bureau (“7”) within the Federal Reserve System. The CFPB is responsible for establishing and implementing rules and regulations under various federal consumer protection laws governing certain consumer products and services. The CFPB has primary enforcement authority over large financial institutions with assets of \$10 Billion or more, while smaller institutions will be subject to the CFPB’s rules and regulations through the enforcement authority of the federal banking agencies. States are permitted to adopt consumer protection laws and regulations that are more stringent than those laws and regulations adopted by the CFPB and state attorneys general are permitted to enforce consumer protection laws and regulations adopted by the CFPB.
- *Deposit Insurance.* The Dodd-Frank Act permanently increased the deposit insurance limit for insured deposits to \$250,000 per depositor. Other deposit insurance changes under the Dodd-Frank Act include (i) amendment of the assessment base used to calculate an insured depository institution’s deposit insurance premiums paid to the Deposit Insurance Fund (“DIF”) by elimination of deposits and substitution of average consolidated total assets less average tangible equity during the assessment period as the revised assessment base; (ii) increasing the minimum designated reserve ratio of the DIF from 1.15 percent to 1.35 percent of the estimated amount of total insured deposits; (iii) eliminating the requirement that the FDIC pay dividends to depository institutions when the reserve ratio exceeds certain thresholds; and (iv) repeal of the prohibition upon the payment of interest on demand deposits to be effective one year after the date of enactment of the Dodd-Frank Act. The FDIC has proposed further changes to the deposit insurance assessments applicable to small insured depository institutions with assets less than \$10 Billion and additional DIF recapitalization obligations for insured depository institutions with more than \$10 Billion in assets. See the discussion of these changes in “Supervision and Regulation - FDIC Insurance.”
- *Transactions with Affiliates.* The Dodd-Frank Act enhances the requirements for certain transactions with affiliates under Section 23A and 23B of the Federal Reserve Act, including an expansion of the definition of “covered transactions” and increasing the amount of time for which collateral requirements regarding covered transactions must be maintained.
- *Transactions with Insiders.* Insider transaction limitations are expanded through the strengthening of loan restrictions to insiders and the expansion of the types of transactions subject to the various limits, including derivative transactions, repurchase agreements, reverse repurchase agreements and securities lending or borrowing transactions. Restrictions are also placed on certain asset sales to and from an insider to an institution, including requirements that such sales be on market terms and, in certain circumstances, approved by the institution’s board of directors.
- *Enhanced Lending Limitations.* The Dodd-Frank Act strengthens the existing limits on a depository institution’s credit exposure to include credit exposure arising from derivative transactions, repurchase agreements, and securities lending and borrowing transactions.
- *Debit Card Interchange Fees.* The Dodd-Frank Act requires that the amount of any interchange fee charged by a debit card issuer with respect to a debit card transaction must be reasonable and proportional to the cost incurred by the issuer. The Federal Reserve Board was required to establish standards for reasonable and proportional fees which may take into account the costs of preventing fraud. The restrictions on



interchange fees, however, do not apply to banks that, together with their affiliates, have assets of less than \$10 Billion.

- *Interstate Branching.* The Dodd-Frank Act authorizes national and state banks to establish branch offices in other states to the same extent as a bank chartered by that state would be permitted to branch. Previously, banks could only establish branch offices in other states if the host state expressly permitted out-of-state banks to establish branch offices in that state. Accordingly, banks may be able to enter new markets more freely.

*Compensation Practices.* The Dodd-Frank Act provides that the appropriate federal banking regulators must establish standards prohibiting as an unsafe and unsound practice any compensation plan of a bank holding company or other “covered financial institution” that provides an insider or other employee with “excessive compensation” or could lead to a material financial loss to such firm. In June 2016, several federal financial agencies (including the Federal Reserve and FDIC) re-proposed restrictions on incentive-based compensation pursuant to Section 956 of the Dodd-Frank Act for financial institutions with \$1 billion or more in total consolidated assets. For institutions with at least \$1 billion but less than \$50 billion in total consolidated assets, the proposal would impose principles-based restrictions that are broadly consistent with existing interagency guidance on incentive-based compensation. Such institutions would be prohibited from entering into incentive compensation arrangements that encourage inappropriate risks by the institution (i) by providing an executive officer, employee, director, principal shareholder or individuals who are “significant risk takers” with excessive compensation, fees or benefits, or (ii) that could lead to material financial loss to the institution. Depending upon the outcome of the rule making process, the application of this rule to us if we were to cross the \$1 billion threshold could require us to revise our compensation strategy, increase our administrative costs and adversely affect our ability to recruit and retain qualified associates.

In June 2010, prior to the enactment of the Dodd-Frank Act, the federal bank regulatory agencies jointly issued the *Interagency Guidance on Sound Incentive Compensation Policies* (“Guidance”), which requires that financial institutions establish metrics for measuring the risk to the financial institution of such loss from incentive compensation arrangements and implement policies to prohibit inappropriate risk taking that may lead to material financial loss to the institution. Together, the Dodd-Frank Act and the Guidance may impact our compensation policies and arrangements.

Requirements under the Dodd-Frank Act are anticipated to be implemented over an extended period of time, unless the implementation is changed as the result of additional legislation promulgated by Congress or as a result of actions taken by the administration of President Trump. Therefore, the nature and extent of regulations that will be issued by various regulatory agencies and the impact such regulations will have on the operations of financial institutions such as ours is unclear. Such regulations resulting from the Dodd-Frank Act may impact the profitability of our business activities, require changes to certain of our business practices, impose upon us more stringent capital, liquidity and leverage ratio requirements or otherwise adversely affect our business. These changes may also require us to invest significant management attention and resources to evaluate and make necessary changes in order to comply with new statutory and regulatory requirements.

#### *Customer Information Privacy and Cybersecurity*

The FRB and other bank regulatory agencies have adopted guidelines for safeguarding confidential, personal, non-public customer information. These guidelines require each financial institution, under the supervision and ongoing oversight of its board of directors or an appropriate

committee thereof, to create, implement, and maintain a comprehensive written information security program designed to ensure the security and confidentiality of customer information, protect against any anticipated threats or hazard to the security or integrity of such information, and protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer. We have adopted a customer information security program to comply with these requirements.

In March 2015, federal regulators issued two related statements regarding cybersecurity. One statement indicates that financial institutions should design multiple layers of security controls to establish lines of defense and to ensure that their risk management processes also address the risk posed by compromised customer credentials, including security measures to reliably authenticate customers accessing Internet-based services of the financial institution. The other statement indicates that a financial institution's management is expected to maintain sufficient business continuity planning processes to ensure the rapid recovery, resumption and maintenance of the institution's operations after a cyber-attack involving destructive malware. A financial institution is also expected to develop appropriate processes to enable recovery of data and business operations and address rebuilding network capabilities and restoring data if the institution or its critical service providers fall victim to this type of cyber-attack. If we fail to observe the regulatory guidance, we could be subject to various regulatory sanctions, including financial penalties.

The GLB Act requires financial institutions to implement policies and procedures regarding the disclosure of non-public personal information about consumers to non-affiliated third parties. The GLB Act requires disclosures to consumers on policies and procedures regarding the disclosure of such non-public personal information and, except as otherwise required by law, prohibit disclosing such information except as provided in the Avidbank's policies and procedures. We have implemented privacy policies addressing these restrictions that are distributed regularly to all existing and new customers of Avidbank.

State regulators have been increasingly active in implementing privacy and cybersecurity standards and regulations. Recently, several states have adopted regulations requiring certain financial institutions to implement cybersecurity programs and providing detailed requirements with respect to these programs, including data encryption requirements. Many states have also recently implemented or modified their data breach notification and data privacy requirements. In June 2018, the California legislature passed the California Consumer Privacy Act of 2018 (the "California Privacy Act"), which is scheduled to take effect on January 1, 2020. The California Privacy Act, which covers businesses that obtain or access personal information on California resident consumers, grants consumers enhanced privacy rights and control over their personal information and imposes significant requirements on covered companies with respect to consumer data privacy rights. We expect this trend of state-level activity to continue, and are continually monitoring developments in the states in which we operate.

### **2017 Tax Reform Law**

On December 22, 2017, President Trump signed into law "H.R.1" commonly referred to as the Tax Cuts and Jobs Act, which among other matters reduced the federal corporate income tax rate to 21%, effective January 1, 2018. The lowering of the tax rate caused banks that carry net deferred tax assets on their balance-sheets (i.e., tax positions carried forward to offset against future taxes) to take charges against the valuation of their net deferred tax assets because the higher the tax rate, the more these net deferred tax assets are worth. Hence, the reduction of the federal corporate-tax rate from the Company's 2017 rate of 34% to the projected future rate of 21%, reduced the value of these net

deferred tax assets. Charges of \$1,101,218 against the Company's net deferred tax assets were recorded as additional income tax expense in the fourth quarter of 2017.

### **Future Legislation and Regulation**

In addition to legislative changes, the various federal and state financial institution regulatory agencies frequently propose rules and regulations to implement and enforce already existing legislation. It cannot be predicted whether or in what form any such rules or regulations will be enacted or the effect that such regulations may have on Avidbank shares or Avidbank. The Company anticipates that additional regulations would likely increase the Company's expenses, which may adversely impact the Company's results of operations, financial condition, future prospects, profitability, and stock price.

### **Conclusions**

It is impossible for the Company to predict with any degree of accuracy the competitive impact the laws and regulations described above will have on commercial banking in general and on the business of the Company and Avidbank in particular, or to predict whether or when any of the proposed legislation and regulations described above will be adopted. The Company anticipates that banking will continue to be a highly regulated industry. Additionally, there has been a continued lessening of the historical distinction between the services offered by financial institutions and other businesses offering financial services. Also, the trend toward nationwide interstate banking is expected to continue. As a result of these factors, the Company anticipates that banks will experience increased competition for deposits and loans and, possibly, further increases in their cost of doing business.

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