Appalachian Community Capital Corporation

Report on Consolidated Financial Statements

For the years ended December 31, 2018 and 2017

Page

elliott davis

Independent Auditor's Report

To the Board of Directors
Appalachian Community Capital Corporation

Report on the Financial Statements
We have audited the accompanying consolidated financial statements of Appalachian Community Capital Corporation (the "Company"), which comprise the consolidated statements of financial position as of December 31, 2018 and 2017, and the related consolidated statements of activities and cash flows for the years then ended and the related notes to the consolidated financial statements (collectively, the financial statements).

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

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

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

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

Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Appalachian Community Capital Corporation as of December 31, 2018 and 2017, and the results of its activities and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Adoption of a New Accounting Standard
As discussed in Note 1, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-14, Not for Profit Entities: Presentation of Financial Statements of Not-for-Profit Entities. The update addresses presentation of net asset classifications for consistency and understandability, provides information about liquidity and availability of resources, and allows consistency in information provided about expenses and investment return. The Company adopted ASU 2016-14 during the year ended December 31, 2018, and it was applied retrospectively. The adoption of this standard did not have any impact on the Company's net assets or changes in net assets. Our opinion is not modified with respect to this matter.

Elliott Davis, PLLC

Raleigh, North Carolina
April 11, 2019

Appalachian Community Capital Corporation

Consolidated Statements of Financial Position

As of December 31, 2018 and 2017

	2018	2017
Assets		
Cash and cash equivalents	$ 2,465,160	$ 2,199,731
Cash funded loan loss reserves	150,000	150,000
Loans receivable, net of allowance for loan losses of $186,050 and $174,840 at December 31, 2018 and 2017, respectively	15,682,122	13,025,391
Grants receivable	831,613	487,499
Accrued interest receivable	31,061	26,159
Property and equipment, net	1,126	-
Prepaid expenses and other assets	36,293	39,784
Total assets	$ 19,197,375	$ 15,928,564
Liabilities and Net Assets		
Notes payable	$ 14,835,000	$ 12,000,000
Accrued interest payable	44,520	28,107
Accounts payable	9,050	-
Deferred revenue	637,769	488,499
Accrued expenses and other liabilities	32,080	15,319
Total liabilities	15,558,419	12,531,925
Net assets - without donor restrictions	651,956	409,639
Net assets - with donor restrictions	2,987,000	2,987,000
Total net assets	3,638,956	3,396,639
Total liabilities and net assets	$ 19,197,375	$ 15,928,564

See Notes to Consolidated Financial Statements

Appalachian Community Capital Corporation

Consolidated Statements of Activities

For the year ended December 31, 2018

	Without Donor Restrictions	With Donor Restrictions	Total
Support and revenue			
Grant income	$ 612,806	$ -	$ 612,806
Interest income - loans	463,436	-	463,436
Interest income - certificates of deposits	8,971	-	8,971
Other operating income	23,123	-	23,123
Total support and revenue	1,108,336	-	1,108,336
Expenses			
Program Services			
Interest expense	386,200	-	386,200
Provision for (recovery of) loan losses	11,210	-	11,210
Salaries and employee benefits	145,926	-	145,926
Data processing	38,709	-	38,709
Office and administrative	499	-	499
Professional fees	136,619	-	136,619
Travel expense	13,138	-	13,138
Dues and subscriptions	21,944	-	21,944
Board of Directors' expense	5,636	-	5,636
Other expense	35,847	-	35,847
Total program services expenses	795,728	-	795,728
Management and General			
Salaries and employee benefits	25,752	-	25,752
Data processing	6,831	-	6,831
Office and administrative	87	-	87
Professional fees	24,109	-	24,109
Travel expense	2,319	-	2,319
Dues and subscriptions	3,872	-	3,872
Board of Directors' expense	995	-	995
Other expense	6,326	-	6,326
Total management and general expenses	70,291	-	70,291
Total expenses	866,019	-	866,019
Change in net assets	242,317	-	242,317
Net assets - beginning of year	409,639	2,987,000	3,396,639
Net assets - end of year	$ 651,956	$ 2,987,000	$ 3,638,956

See Notes to Consolidated Financial Statements

Appalachian Community Capital Corporation

Consolidated Statements of Activities

For the year ended December 31, 2017

	Without Donor Restrictions	With Donor Restrictions	Total
Support and revenue			
Grant income	$ 524,239	$ -	$ 524,239
Interest income - loans	337,210	-	337,210
Interest income - certificates of deposits	8,865	-	8,865
Other operating income	250	-	250
Total support and revenue	870,564	-	870,564
Expenses			
Program Services			
Interest expense	261,621	-	261,621
Provision for (recovery of) loan losses	(5,160)	-	(5,160)
Salaries and employee benefits	80,877	-	80,877
Data processing	38,675	-	38,675
Office and administrative	226	-	226
Professional fees	103,156	-	103,156
Travel expense	4,621	-	4,621
Dues and subscriptions	19,681	-	19,681
Board of Directors' expense	2,277	-	2,277
Other expense	21,635	-	21,635
Total program services expenses	527,609	-	527,609
Management and General			
Salaries and employee benefits	14,272	-	14,272
Data processing	6,825	-	6,825
Office and administrative	40	-	40
Professional fees	18,204	-	18,204
Travel expense	815	-	815
Dues and subscriptions	3,473	-	3,473
Board of Directors' expense	402	-	402
Other expense	3,818	-	3,818
Total management and general expenses	47,849	-	47,849
Total expenses	575,458	-	575,458
Change in net assets	295,106	-	295,106
Net assets - beginning of year	114,533	2,987,000	3,101,533
Net assets - end of year	$ 409,639	$ 2,987,000	$ 3,396,639

See Notes to Consolidated Financial Statements

Appalachian Community Capital Corporation

Consolidated Statements of Cash Flows

For the years ended December 31, 2018 and 2017

	2018	2017
Cash flows from operating activities		
Change in net assets	$ 242,317	$ 295,106
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	66	50
Provision for (recovery of) loan losses	11,210	(5,160)
Change in assets and liabilities:		
Grants receivable	(344,114)	14,239
Prepaid expenses and other assets	3,491	2,624
Accounts payable	9,050	(10,200)
Accrued expenses and other liabilities	16,761	(3,032)
Deferred revenue	149,270	285,761
Accrued interest payable	16,413	9,887
Accrued interest receivable	(4,902)	(4,201)
Cash funded loan loss reserve	-	(150,000)
Net cash provided by operating activities	99,562	435,074
Cash flows from investing activities		
Net increase in loans	(2,667,941)	(1,202,911)
Purchase of property, plant, and equipment	(1,192)	-
Net cash used in investing activities	(2,669,133)	(1,202,911)
Cash flows from financing activities		
Increase in notes payable	2,835,000	1,000,000
Net cash provided by financing activities	2,835,000	1,000,000
Change in cash and cash equivalents	265,429	232,163
Cash and cash equivalents - beginning of year	2,199,731	1,967,568
Cash and cash equivalents - end of year	$ 2,465,160	$ 2,199,731

See Notes to Consolidated Financial Statements

Note 1. Nature of Activities and Summary of Significant Accounting Policies

Nature of Activities

Appalachian Community Capital Corporation ("ACC" or the "Company") is a non-profit, wholesale capital intermediary created to increase business lending in Appalachia by providing community loan funds with a new source of capital. Formed in 2013, ACC's mission is to increase business lending by providing member institutions, which serve underserved people and communities, with new sources of capital. The Company provides financing, as well as educational programs and technical assistance to its members and to small businesses throughout the thirteen-state Appalachian Region. ACC's work enables reliable and sufficient capital for all of its members, leading to a growing economy, increased entrepreneurship, higher quality jobs, and increased local wealth in the Appalachian region. Appalachian Community Capital Development Foundation is a non-profit organization that is under common control by ACC and is therefore consolidated for financial reporting purposes. The consolidation of this organization does not have a material impact on the financial statements of ACC.

The accounting and reporting policies of the Company follow generally accepted accounting principles and general practices within the non-profit and financial services industry. The following is a summary of the more significant policies:

Critical Accounting Policies

Management believes the policies with respect to the methodology for the determination of the allowance for loan losses and asset impairment judgments involve a high degree of complexity. Management must make difficult and subjective judgments which require assumptions or estimates about highly uncertain matters. Changes in these judgments, assumptions or estimates could cause reported results to differ materially. These critical policies and their application are periodically reviewed with the Audit Committee and Board of Directors.

Use of Estimates

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

The determination of whether or not grant conditions have been met has a significant impact on revenue and is, in some cases, an estimate.

Basis of Accounting

The financial statements are prepared on the accrual basis of accounting. Under this basis of accounting, revenues are recognized when earned and expenses are recognized when incurred.

Note 1. Nature of Activities and Summary of Significant Accounting Policies, continued

Financial Statement Presentation

Net assets, revenues and expenses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Company and changes therein are classified and reported as follows:

- Without Donor Restrictions – All resources over which the governing board has discretionary control. The Board of Directors of the Company may elect to designate such resources for specific purposes. This designation may be removed at the Board of Directors' discretion.

- With Donor Restrictions – Resources accumulated through donations or grants for specific operating or capital purposes. Such resources will be without restrictions when the requirements of the donor or grantee have been satisfied through expenditures for the specified purpose or program or through the passage of time. Also includes resources accumulated through donations or grants subject to donor-imposed stipulations that are to be maintained permanently by the Company. Generally, the donors of these assets permit the Company to use all or part of the income earned on related investments for general or specific purposes.

Cash and Cash Equivalents

For purposes of the statements of cash flows, cash and cash equivalents are considered to include those amounts included in "cash and cash equivalents" on the statement of financial position.

Loans Receivable

Loans receivable that management has the intent and ability to hold for the foreseeable future, until maturity or pay-off are reported at their outstanding principal amount adjusted for any charge-offs. Loan origination fees, net of certain direct origination costs, are deferred and recognized, as an adjustment of the related loan yield using the effective interest method.

Interest is accrued and credited to income based on the principal amount outstanding. The accrual of interest on impaired loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due. When interest accrual is discontinued, all unpaid accrued interest for the current year is reversed and any subsequent payments received are applied only to the loan's outstanding principal balance. When facts and circumstances indicate the borrower has regained the ability to meet the required payments, the loan is returned to accrual status. Past due status of loans is determined based on contractual terms.

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

Note 1. Nature of Activities and Summary of Significant Accounting Policies, continued

Allowance for Loan Losses, continued

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific and general components. The specific component relates to loans that are classified as impaired. For such loans, an allowance is established when the discounted cash flows, collateral's net realizable value or observable market price of the impaired loan is lower than the carrying value of that loan. The general component covers non-impaired loans and includes both a quantitative and qualitative component. The quantitative component is based on historical loss experience, while the qualitative component is based on specific internal and external factors that may have a negative impact on the performance of the loan portfolio.

In 2017, the Company had allocated $150,000 of a grant funding received from the Community Development Financial Institutions ("CDFI") Fund to create a cash funded loan loss reserve in order to offset losses in the Small/Emerging CDFI loan portfolio. The portion of the allowance for loan losses attributable to the Small/Emerging CDFI's will be a reduction against the overall allowance of loan losses as the funds can be used to offset small business loan losses and provisions per the grant document.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status and other circumstances impacting the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the net realizable value of the collateral if the loan is collateral dependent.

Grants Receivable, Revenue Recognition, and Deferred Revenue

Grants receivable and related deferred revenue are recorded at the time of notification from a grantor. Grants are classified in one of two categories, with donor restrictions and without donor restrictions. Classification is determined based on the designation by the grantor for the use of funds. Grant revenue is recognized when earned by the Company through performance as specified in each grant award.

Note 1. Nature of Activities and Summary of Significant Accounting Policies, continued

Property and Equipment

Property and equipment consists of computer equipment and is carried at cost, less accumulated depreciation computed by the straight-line method over three years. When items of property and equipment are sold or retired, the related costs and accumulated depreciation are removed from the accounts and any gain or loss is included in income. Maintenance and repairs are charged to expenses as incurred; major renewals and betterments are capitalized.

Functional Allocation of Expenses

The consolidated financial statements report certain categories of expenses that are attributable to one or more program or supporting functions of the Organization. Those expenses include salaries and employee benefits, the data processing, office and administrative, professional fees, travel, dues and subscriptions, Board of Directors', and other expenses. These costs are allocated based on estimates of time and effort.

Income Taxes

The Company is a not-for-profit organization that is exempt from income taxes under Section 501(c)(4) of the Internal Revenue Code. Management is not aware of any uncertain tax positions and has not accrued any expense for the effect of an uncertain tax position as of December 31, 2018 and 2017. Tax years beginning in 2015 are open to examination by taxing authorities.

Recent Accounting Pronouncements

The following accounting standards may affect the future financial reporting by Appalachian Community Capital Corporation:

In May 2014, the Financial Accounting Standards Board ("FASB") issued guidance to change the recognition of revenue from contracts with customers. The core principle of the new guidance is that an entity should recognize revenue to reflect the transfer of goods and services to customers in an amount equal to the consideration the entity receives or expects to receive. In August 2015, the FASB deferred the effective date of ASU 2014-09, *Revenue from Contracts with Customers.* As a result of the deferral, the guidance in ASU 2014-09 will be effective for the Company for reporting periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019. The Company will apply the guidance using a retrospective approach. The Company does not expect these amendments to have a material effect on its financial statements.

In January 2016, the FASB amended the Financial Instruments topic of the Accounting Standards Codification to address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The amendments will be effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. The Company will apply the guidance by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The Company does not expect these amendments to have a material effect on its financial statements.

Note 1. Nature of Activities and Summary of Significant Accounting Policies, continued

Recent Accounting Pronouncements, continued

In June 2016, the FASB issued guidance to change the accounting for credit losses and modify the impairment model for certain debt securities. The amendments will be effective for the Company for annual periods beginning after December 15, 2020, and interim periods within annual reporting periods beginning after December 15, 2021. Early adoption is permitted for all companies for periods beginning after December 15, 2018.

The Company will apply the amendments to the ASU through a cumulative-effect adjustment to net assets as of the beginning of the year of adoption. While early adoption is permitted beginning in first quarter 2019, the Company does not expect to elect that option. The Company is evaluating the impact of the ASU on the financial statements. The Company has not formed an expectation of what, if any impact on the recorded allowance for loan losses given the change to estimated losses over the contractual life of the loans adjusted for expected prepayments. The amount of the adjustments will be impacted by each portfolio's composition and credit quality at the adoption date as well as economic conditions and forecasts at that time.

In November 2016, the FASB amended the Statement of Cash Flows topic of the Accounting Standards Codification to clarify how restricted cash is presented and classified in the statement of cash flows. The amendments will be effective for the Company for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

In December 2016, the FASB issued technical corrections and improvements to the Revenue from Contracts with Customers Topic. These corrections make a limited number of revisions to several pieces of the revenue recognition standard issued in 2014. The effective date and transition requirements for the technical corrections will be effective for the Company for annual periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019. The Company expects to apply the guidance using a retrospective approach. The Company does not expect these amendments to have a material effect on its financial statements.

In June 2018, the FASB updated the Not-for-Profit Entities Topic of the Accounting Standards Codification. The amendments clarify and improve current guidance about whether a transfer of assets (or the reduction, settlement, or cancellation of liabilities) is a contribution or an exchange transaction. For contributions received, the amendments are effective for annual periods beginning after December 15, 2018, and interim periods within those annual periods beginning after December 15, 2019. For contributions made, the amendments are effective for annual periods beginning after December 15, 2019, and interim periods within those annual periods beginning after December 15, 2020. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company's financial position, results of operations or cash flows.

Note 2. Cash and Cash Equivalents

Cash and cash equivalents at December 31, 2018 and 2017 totaled $2,615,160 and $2,349,731, respectively. Of this balance, $1,600,944 exceeded the federally insured limit as of December 31, 2018.

Note 3. Loans Receivable

The major components of loans receivable as of December 31, 2018 and 2017 are as follows:

	2018	2017
Loans to CDFI's	$ 14,598,154	$ 13,200,231
Other loans	1,270,018	-
Allowance for loan losses	(186,050)	(174,840)
Total	$ 15,682,122	$ 13,025,391

There were no loans pledged at December 31, 2018 or 2017.

The Company is party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. This financial instrument includes commitments to extend credit. This instrument involves, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized on the balance sheets position. The contractual or notional amounts of this instrument reflect the extent of involvement the Company has in particular classes of financial instruments.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual or notional amount of this instrument. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Company upon extension of credit is based on management's credit evaluation of the counter-party.

As of December 31, 2018 and 2017, the Company had no commitments to extend credit.

Note 4. Allowance for Loan Losses

The allocation of the allowance for loan losses by loan components at December 31, 2018 was as follows:

Allowance for loan losses:	**Loans to CDFI's**	**Other loans**	**Total**
December 31, 2017	$ 174,840	$ -	$ 174,840
Provision for loan losses	11,210	-	11,210
December 31, 2018	$ 186,050	$ -	$ 186,050
Ending Balance:			
Individually evaluated for impairment	$ -	$ -	$ -
Collectively evaluated for impairment	$ 186,050	$ -	$ 186,050
Loans Receivable			
Ending Balance:			
Individually evaluated for impairment	$ -	$ -	$ -
Collectively evaluated for impairment	$ 14,598,154	$ 1,270,018	$ 15,868,172

Note 4. Allowance for Loan Losses, continued

The allocation of the allowance for loan losses by loan components at December 31, 2017 was as follows:

Allowance for loan losses:	**Loans to CDFI's**	**Other loans**	**Total**
December 31, 2016	$ 180,000	$ -	$ 180,000
Provision for loan losses	(5,160)	-	(5,160)
December 31, 2017	$ 174,840	$ -	$ 174,840
Ending Balance:			
Individually evaluated for impairment	$ -	$ -	$ -
Collectively evaluated for impairment	$ 174,840	$ -	$ 174,840
Loans Receivable			
Ending Balance:			
Individually evaluated for impairment	$ -	$ -	$ -
Collectively evaluated for impairment	$ 13,200,231	$ -	$ 13,200,231

There were no impaired loans as of December 31, 2018 and 2017. In addition, there were no loans identified as impaired during the years ended December 31, 2018 and 2017. As a result, there was no average recorded investment in impaired loans or interest income recognized on impaired loans for the years ended December 31, 2018 and 2017. In addition, there were no nonaccrual loans as of December 31, 2018 and 2017. The Company utilizes a cash funded loan loss reserve in the amount of $150,000 to offset reserves related to small business loans. This has resulted in a reserve balance of $0 related to "Other" loans as of December 31, 2018 and 2017.

As of December 31, 2018 and 2017, there were no loans past due.

Credit Quality Indicators:

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans as to credit risk.

Loans graded Good or Satisfactory are excluded from the scope of the annual review and considered "Pass Credits" until: (a) they become past due; (b) management becomes aware of a deterioration in the credit worthiness of the borrower; or (c) the customer contacts the Company for a modification. In these circumstances, the loan is specifically evaluated for potential classification as Watch, Substandard, Doubtful or Loss. Loans are graded as loss are charged off. The Company uses the following definitions for risk ratings:

Good - Loans in this category are of good quality. The borrower has a history of successful performance, but may be susceptible to economic changes. Asset quality and liquidity are considered good. Overall leverage is normal for the industry in which the borrower operates and is stable. Cash flow levels may fluctuate but are sufficient to meet obligations. Margins and ratios are generally in line with or exceed industry norms. Earnings may have been inconsistent in the past, but have now stabilized and are equivalent to or better than the industry average. Other sources of financing, particularly from a number of other financial institutions, should be obtainable.

Note 4. Allowance for Loan Losses, continued

Credit Quality Indicators, continued

Satisfactory - Loans in this category are of satisfactory quality and risk is well within the Company's range of acceptability. They may differ from loans rated "Good" because the borrower may be entering an expansion mode, acquiring another company, introducing new products or investing large amounts of capital in upgrading equipment or the facility. The borrower's business may be cyclical or its customer base may have concentrations. Asset quality is acceptable. Liquidity levels fluctuate and usage of short term credit may be needed on a regular basis to finance growth or fluctuations in revenues and current assets. Leverage may be slightly to moderately higher than the industry, but is stable. Cash flow may fluctuate, but is evident in sales and earnings. The long-term outlook should be favorable. Management and owners have unquestioned character, although depth of management may be an issue.

Watch - Loans in this grade are considered to have a higher than normal credit risk and servicing needs. Asset quality is marginally acceptable. Leverage may fluctuate and is above normal for the industry. Cash flow is marginally adequate, but is not clearly sufficient to ensure continued performance of contractual obligations without improving trends. A loss year or earnings decline may occur, but the borrower has sufficient strength and financial flexibility to offset these events. A reasonable expectation exists that operating performance will improve in the near future. Some management weaknesses may exist. These borrowers are currently performing as agreed, but may be adversely affected by deteriorating industry conditions, competition, operating deficiencies, pending litigation of a significant nature, or declining asset quality, and therefore should be monitored closely. Access to alternative financing sources may not be possible or limited to asset-based lenders and other institutions specializing in high risk financing. Management has determined these loans require enhanced monitoring.

Substandard - Substandard assets are inadequately protected by the net worth and paying capacity of the borrower or the collateral pledged. Sound worth and paying capacity of a guarantor should be considered only if judged to be strong and dependable. Customers in this category have well defined weaknesses and the possibility exists that the Company will sustain some loss if the deficiencies are not corrected. Characteristics of a substandard loan include one or more of the following characteristics: a significant deterioration in earnings, cash flow or balance sheet composition, a deficient equity position, insufficient cash flow to meet maturity obligations, recent evidence of slow payments, a lack of adequate collateral or a dependence on illiquid collateral for repayment.

Doubtful - Doubtful ratings are applied to loans that exhibit weaknesses that make collection or liquidation in full improbable. This rating is used when the expected loss cannot be calculated, but estimates indicate that the loss will be significant in relation to the outstanding loan balance. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors which may work to the advantage and strengthening of the loan, its classification as a loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition, or liquidation procedures, capital injection, perfecting liens on additional collateral, and refinancing plans.

Loss - This rating is applied when the borrower's outstanding debt is considered uncollectible or of such little value that continuance as a Company asset is not warranted. This rating does not suggest that there is absolutely no recovery or salvage value, but that it is not practical or desirable to defer charging off the loan.

Note 4. Allowance for Loan Losses, continued

Loans by Risk Rating as of December 31, 2018	Loans to CDFI's	Other Loans	Total
Pass Credits	$ 14,548,154	$ 1,270,018	$ 15,818,172
Watch	50,000	-	50,000
Total	$ 14,598,154	$ 1,270,018	$ 15,868,172

Loans by Risk Rating as of December 31, 2017	Loans to CDFI's	Other Loans	Total
Pass Credits	$ 13,200,231	$ -	$ 13,200,231
Watch	-	-	-
Total	$ 13,200,231	$ -	$ 13,200,231

Troubled Debt Restructurings

There were no loans modified in a troubled debt restructuring in 2018 or 2017.

Note 5. Grants Receivable

ACC was due to receive grant awards from outside funding agencies as of December 31, 2018 as follows:

Funding Agency	Amount Awarded	Amount Received	Amount Receivable
Appalachian Regional Commission – 2017 Operating Grant	$ 250,000	$ 143,387	$ 106,613
Appalachian Regional Commission – 2018 Operating Grant	175,000	-	175,000
CDFI – 2018 Financial Assistance Award	550,000	-	550,000
Total	$ 975,000	$ 143,387	$ 831,613

The receivable has not been discounted due to its short term status.

ACC was due to receive grant awards from outside funding agencies as of December 31, 2017 as follows:

Funding Agency	Amount Awarded	Amount Received	Amount Receivable
Appalachian Regional Commission – 2015 Operating Grant	$ 325,000	$ 292,500	$ 32,500
Appalachian Regional Commission – 2017 Operating Grant	250,000	94,001	155,999
Appalachian Regional Commission – 2013 Equity Grant	2,987,000	2,688,000	299,000
Total	$ 3,562,000	$ 3,074,501	$ 487,499

The receivable has not been discounted due to its short term status.

Note 6. Property and Equipment

Details related to property and equipment as of December 31, 2018 and 2017 is as follows:

	2018	2017
Computer equipment	$ 3,009	$ 1,817
Less, accumulated depreciation	(1,883)	(1,817)
Total	$ 1,126	$ -

Depreciation for the years ended December 31, 2018 and 2017 was $66 and $50, respectively.

Note 7. Concentration Risks

ACC has a potential risk associated with the concentration of support received from governmental agencies. Any change in future funding could have an adverse impact on ACC. The Company also has little diversification in its loan portfolio with the significant portion of loans outstanding to CDFIs as discussed in Note 3.

Note 8. Borrowings

Borrowings at December 31, 2018 and 2017, respectively, consist of the following:

Description	Rate	Maturity	2018	2017
Bank of America*	LIBOR+2.00%	05/01/2023	$ 3,000,000	$ 3,000,000
Calvert Foundation*	4.50%	05/06/2023	3,000,000	3,000,000
Deutsche Bank*	LIBOR+0.50%	05/06/2023	3,000,000	3,000,000
Ford Foundation*	1.00%	05/06/2023	3,000,000	3,000,000
Regions Bank**	LIBOR+2.50%	10/16/2020	735,000	-
Opportunity Finance Network**	3.00%	05/01/2023	400,000	-
BBVA Compass Bank**	2.50%	08/07/2025	200,000	-
PNC Bank**	1.00%	06/30/2024	500,000	-
Northern Trust***	2.00%	11/26/2023	1,000,000	-
			$ 14,835,000	$ 12,000,000

*Disbursements on each loan are not to exceed $3 million. Each loan is unsecured with interest payments due on a quarterly basis. Each loan requires principal payments of $1 million due in May 2021 and May 2022, the sixth and seventh anniversary of the loan closing date, with the remaining principal due at maturity.
** Each loan is unsecured with interest payments due on a quarterly basis, with the remaining principal due at maturity.
***The loan is unsecured with interest payments due on a semi-annual basis, with the remaining principal due at maturity.

Performance against debt covenants is measured on a quarterly basis. As of December 31, 2018, ACC was in compliance with all covenants.

Note 9. Fair Value of Financial Instruments

Fair Value Hierarchy

There are three levels of inputs in the fair value hierarchy that may be used to measure fair value. Financial instruments are considered *Level 1* when valuation can be based on quoted prices in active markets for identical assets or liabilities. *Level 2* financial instruments are valued using quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or models using inputs that are observable or can be corroborated by observable market data of substantially the full term of the assets or liabilities. Financial instruments are considered *Level 3* when their values are determined using pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable and when determination of the fair value requires significant management judgment or estimation.

Recurring Fair Value

The Company had no financial assets recorded at fair value on a recurring basis as of December 31, 2018 or 2017.

Non-Recurring Fair Value

The following describes the valuation techniques used by the Company to measure certain assets recorded at fair value on a nonrecurring basis in the financial statements:

Non-Recurring Fair Value, continued

Impaired Loans: Impairment of a loan is based on a loan’s observable market price, the fair value of the collateral of a collateral-dependent loan or the discounted cash flow method. Fair value of the loan's collateral, when the loan is dependent on collateral, is determined by appraisals or independent valuation which is then adjusted for the cost related to liquidation of the collateral. The value of business equipment is based upon an outside appraisal, if deemed significant, or the net book value on the applicable business’ financial statements if not considered significant using observable market data. Likewise, values for inventory and accounts receivables collateral are based on financial statement balances or aging reports. The Company had no impaired loans as of December 31, 2018 or 2017.

Note 10. Significant Contracts

During 2014, the Company entered into an agreement with another CDFI, Virginia Community Capital (“VCC”), to provide accounting and data processing services, including loan servicing. Under the terms of the contract, ACC paid an initial set-up fee and a monthly fee of $4,292, as well as additional fees for out of scope services as needed. ACC paid $45,540 and $45,500 under this agreement during the years ended December 31, 2018 and 2017, respectively. VCC is a member organization of ACC and a member of VCC’s management team serves on the Board of Directors of the Company.

Note 11. Related Parties

The Company currently has nine loans outstanding that have been made to CDFI's, each of which is a member organization of ACC. Each of these CDFI's have a member of management who also serves on the Board of Directors of the Company. Each of these loans are on substantially the same terms as those prevailing for comparable transactions with persons not related to the Company and do not involve more than normal risk of collection or present other unfavorable terms.

Note 12. Net Assets with Donor Restrictions

Net assets with donor restrictions are restricted for the following purposes or periods.

	2018	2017
Subject to expenditure for specified purpose:		
Community development lending	$ 2,987,000	$ 2,987,000
Total net assets with donor restrictions	$ 2,987,000	$ 2,987,000

Note 13. Liquidity and Availability of Financial Assets

The Company's financial assets available within one year of the balance sheet date for general expenditure are as follows:

	2018
Cash and due from banks	$ 1,244,332
Loans and interest receivable	3,835,455
Grants receivable	831,613
Cash funded loan loss reserves	150,000
Financial assets available within one year	$ 6,061,400

As part of ACC's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations become due. ACC invests excess cash in short-term investments, including money market accounts, and has the ability to redeem certain investments as necessary to meet its obligations.

Note 14. Subsequent Events

Subsequent events were evaluated through April 11, 2019, the date the financial statements were available to be issued. During this time, no subsequent events occurred that required revision to the financial statements.

MEMBERS OF APPALACHIAN COMMUNITY CAPITAL INCLUDE:

Access to Capital for Entrepreneurs (Georgia)

Alternatives Federal Credit Union (New York)

Appalachian Development Corporation (South Carolina)

Carolina Small Business Development Fund (North Carolina)

CommunityWorks (South Carolina)

Finance Fund Capital Corporation (Ohio)

Greensboro Community Development Fund (North Carolina)

Kentucky Highlands Investment Corporation (Kentucky)

LiftFund (Alabama)

Mountain Association for Community Economic Development (Kentucky)

Mountain BizWorks (North Carolina)

Natural Capital Investment Fund (West Virginia)

Pathway Lending (Tennessee)

People, Inc. (Virginia)

Southeast Kentucky Economic Development Corporation (Kentucky)

Three Rivers Planning & Development District (Mississippi)

Virginia Community Capital (Virginia)

Woodlands Community Lenders (West Virginia)