Live Oak Bancshares, Inc.
Form 10-Q
November 08, 2016

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
ý Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended September 30, 2016
or
¨ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from to .
Commission file number: 001-37497
LIVE OAK BANCSHARES, INC.
(Exact name of registrant as specified in its charter)

North Carolina	26-4596286
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1741 Tiburon Drive Wilmington, North Carolina	28403
(Address of principal executive offices)	(Zip Code)

(910) 790-5867
(Registrant's telephone number, including area code)
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES ý NO ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES ý NO ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer ¨	Accelerated Filer x
Non-accelerated Filer ¨ (Do not check if smaller reporting company)	Smaller Reporting Company ¨

Indicate by check mark whether registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ¨ NO ý
APPLICABLE ONLY TO CORPORATE ISSUERS:
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.
As of November 7, 2016, there were 29,509,945 shares of the registrant's voting common stock outstanding and 4,723,530 shares of the registrant's non-voting common stock outstanding.

Table of Contents

Live Oak Bancshares, Inc. and Subsidiaries
Form 10-Q
For the Quarterly Period Ended September 30, 2016
TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION
Item 1. Financial Statements
Live Oak Bancshares, Inc.
Consolidated Balance Sheets
As of September 30, 2016 (unaudited) and December 31, 2015*
(Dollars in thousands)

	September 30, 2016	December 31, 2015*
Assets		
Cash and due from banks	$355,485	$102,607
Certificates of deposit with other banks	7,500	10,250
Investment securities available-for-sale	70,334	53,762
Loans held for sale	345,277	480,619
Loans held for investment	766,977	279,969
Allowance for loan losses	(15,178)	(7,415)
Net loans	751,799	272,554
Premises and equipment, net	60,646	62,653
Foreclosed assets	2,235	2,666
Servicing assets	49,729	44,230
Other assets	26,735	23,281
Total assets	$1,669,740	$1,052,622
Liabilities and Shareholders' Equity		
Liabilities		
Deposits:		
Noninterest-bearing	$28,461	$21,502
Interest-bearing	1,374,556	783,286
Total deposits	1,403,017	804,788
Long term borrowings	28,074	28,375
Other liabilities	24,497	19,971
Total liabilities	1,455,588	853,134
Shareholders' equity		
Preferred stock, no par value, 1,000,000 authorized, none issued or outstanding at September 30, 2016 and December 31, 2015	—	—
Class A common stock, no par value, 100,000,000 shares authorized, 29,491,520 and 29,449,369 shares issued and outstanding at September 30, 2016 and December 31, 2015, respectively	145,284	137,492
Class B common stock, no par value, 10,000,000 shares authorized, 4,723,530 shares issued and outstanding at September 30, 2016 and December 31, 2015	50,015	50,015
Retained earnings	18,723	12,140
Accumulated other comprehensive income (loss)	130	(192)
Total shareholders' equity attributed to Live Oak Bancshares, Inc.	214,152	199,455
Noncontrolling interest	—	33
Total equity	214,152	199,488
Total liabilities and shareholders' equity	$1,669,740	$1,052,622

* Derived from audited consolidated financial statements.
See Notes to Unaudited Consolidated Financial Statements

1

Live Oak Bancshares, Inc.
Consolidated Statements of Income
For the three and nine months ended September 30, 2016 and 2015 (unaudited)
(Dollars in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Interest income				
Loans and fees on loans	$14,961	$8,728	$38,868	$22,866
Investment securities, taxable	337	211	840	587
Other interest earning assets	264	84	650	220
Total interest income	15,562	9,023	40,358	23,673
Interest expense				
Deposits	3,689	1,997	9,376	5,274
Borrowings	242	395	725	1,280
Total interest expense	3,931	2,392	10,101	6,554
Net interest income	11,631	6,631	30,257	17,119
Provision for loan losses	3,806	1,212	8,692	2,339
Net interest income after provision for loan losses	7,825	5,419	21,565	14,780
Noninterest income				
Loan servicing revenue	5,860	4,216	15,725	11,678
Loan servicing asset revaluation	(3,421)	(2,650)	(5,051)	(4,234)
Net gains on sales of loans	21,833	15,424	52,813	46,604
Equity in loss of non-consolidated affiliates	—	—	—	(26)
Gain on sale of investment in non-consolidated affiliate	—	—	—	3,782
Gain on sale of investment securities available-for-sale	1	12	1	12
Construction supervision fee income	502	344	1,799	877
Other noninterest income	657	424	1,925	1,267
Total noninterest income	25,432	17,770	67,212	59,960
Noninterest expense				
Salaries and employee benefits	17,471	9,949	45,875	27,623
Travel expense	2,218	2,200	6,394	5,914
Professional services expense	907	493	2,345	1,891
Advertising and marketing expense	1,097	1,051	3,425	3,177
Occupancy expense	1,058	703	3,306	1,920
Data processing expense	1,252	773	3,864	2,388
Equipment expense	611	642	1,696	1,473
Other loan origination and maintenance expense	806	673	2,001	1,384
Other expense	1,798	1,579	5,155	3,811
Total noninterest expense	27,218	18,063	74,061	49,581
Income before taxes	6,039	5,126	14,716	25,159
Income tax expense	2,561	2,228	6,432	10,272
Net income	3,478	2,898	8,284	14,887
Net loss attributable to noncontrolling interest	1	3	9	23
Net income attributable to Live Oak Bancshares, Inc.	$3,479	$2,901	$8,293	$14,910
Basic earnings per share	$0.10	$0.09	$0.24	$0.50
Diluted earnings per share	$0.10	$0.09	$0.24	$0.48

See Notes to Unaudited Consolidated Financial Statements

Table of Contents

Live Oak Bancshares, Inc.
Consolidated Statements of Comprehensive Income
For the three and nine months ended September 30, 2016 and 2015 (unaudited)
(Dollars in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Net income	$3,478	$2,898	$8,284	$14,887
Other comprehensive (loss) income before tax:				
Net unrealized (loss) gain on investment securities arising during the period	(115)	151	525	15
Reclassification adjustment for (gain) loss on sale of securities available-for-sale included in net income	(1)	(12)	(1)	(12)
Other comprehensive (loss) income before tax	(116)	139	524	3
Income tax benefit (expense)	45	(53)	(202)	(1)
Other comprehensive (loss) income, net of tax	(71)	86	322	2
Total comprehensive income	$3,407	$2,984	$8,606	$14,889

See Notes to Unaudited Consolidated Financial Statements

Table of Contents

Live Oak Bancshares, Inc.
Consolidated Statements of Changes in Shareholders' Equity
For the nine months ended September 30, 2016 and 2015 (unaudited)
(Dollars in thousands)

	Common stock Shares Class A	Class B	Amount	Retained earnings (accumulated deficit)	Accumulated other comprehensive income (loss)	Non-controlling interest	Total equity
Balance at December 31, 2014	23,896,400	4,723,530	$98,672	$ (6,943)	$ 85	$ —	$91,814
Net income (loss)	—	—	—	14,910	—	(23)	14,887
Other comprehensive income	—	—	—	—	2	—	2
Consolidation of investment with non-controlling interest	—	—	—	—	—	35	35
Stock option exercises	47,570	—	215	—	—	—	215
Stock option based compensation expense	—	—	726	—	—	—	726
Restricted stock expense	—	—	83	—	—	—	83
Capital contribution from non-controlling interest	—	—	—	—	—	22	22
Issuance of common stock in connection with initial public offering, net of issue costs	5,500,000	—	87,171	—	—	—	87,171
Dividends (distributions to shareholders)	—	—	—	(859)	—	—	(859)
Balance at September 30, 2015	29,443,970	4,723,530	$186,867	$ 7,108	$ 87	$ 34	$194,096
Balance at December 31, 2015	29,449,369	4,723,530	$187,507	$ 12,140	$ (192)	$ 33	$199,488
Net income (loss)	—	—	—	8,293	—	(9)	8,284
Other comprehensive income	—	—	—	—	322	—	322
Issuance of restricted stock	16,745	—	—	—	—	—	—
Stock option exercises	25,406	—	147	—	—	—	147
Stock option based compensation expense	—	—	1,752	—	—	—	1,752
Restricted stock expense	—	—	5,893	—	—	—	5,893
Acquisition of non-controlling interest	—	—	—	—	—	(24)	(24)
Dividends (distributions to shareholders)	—	—	—	(1,710)	—	—	(1,710)
Balance at September 30, 2016	29,491,520	4,723,530	$195,299	$ 18,723	$ 130	$ —	$214,152

See Notes to Unaudited Consolidated Financial Statements

Table of Contents

Live Oak Bancshares, Inc.
Consolidated Statements of Cash Flows
For the nine months ended September 30, 2016 and 2015 (unaudited)
(Dollars in thousands)

	Nine Months Ended September 30,	
	2016	2015
Cash flows from operating activities		
Net income	$8,284	$14,887
Adjustments to reconcile net income to net cash used by operating activities:		
Depreciation and amortization	3,201	1,917
Provision for loan losses	8,692	2,339
Amortization of premium on securities, net of accretion	135	36
Amortization (accretion) of discount on unguaranteed loans, net	773	1,650
Deferred tax (benefit) expense	(510)	936
Originations of loans held for sale	(701,415)	(740,378)
Proceeds from sales of loans held for sale	555,192	508,322
Net gains on sale of loans held for sale	(52,813)	(46,604)
Net loss on sale of foreclosed assets	61	12
Net increase in servicing assets	(5,499)	(5,591)
Gain on sale of securities available-for-sale	(1)	(12)
Gain on sale of investment in non-consolidated affiliate	—	(3,782)
Net loss on disposal of premises and equipment	—	16
Stock option based compensation expense	1,752	726
Restricted stock expense	5,893	83
Equity in loss of non-consolidated affiliates	—	26
Changes in assets and liabilities:		
Other assets	(858)	(2,431)
Other liabilities	2,652	2,025
Net cash used by operating activities	(174,461)	(265,823)
Cash flows from investing activities		
Purchases of securities available-for-sale	(24,946)	(15,437)
Proceeds from sales, maturities, calls, and principal paydowns of securities available-for-sale	8,764	13,106
Proceeds from sale/collection of foreclosed assets	680	514
Maturities of certificates of deposit with other banks	2,750	—
Proceeds from sale of investment in non-consolidated affiliate	—	9,896
Net cash acquired in consolidation of equity method investment	—	319
Capital contribution from non-controlling interest	—	22
Loan originations and principal collections, net	(154,738)	66,835
Purchases of premises and equipment, net	(1,194)	(29,295)
Net cash (used in) provided by investing activities	(168,684)	45,960

See Notes to Unaudited Consolidated Financial Statements

5

Table of Contents

Live Oak Bancshares, Inc.
Consolidated Statements of Cash Flows (Continued)
For the nine months ended September 30, 2016 and 2015 (unaudited)
(Dollars in thousands)

	Nine Months Ended September 30,	
	2016	2015
Cash flows from financing activities		
Net increase in deposits	598,229	240,548
Proceeds from long term borrowings	—	12,960
Repayment of long term borrowings	(301)	(12,730)
Repayment of short term borrowings	—	(6,100)
Stock option exercises	147	215
Sale of common stock, net	—	87,171
Shareholder dividend distributions	(2,052)	(2,222)
Net cash provided by financing activities	596,023	319,842
Net increase in cash and cash equivalents	252,878	99,979
Cash and cash equivalents, beginning	102,607	29,902
Cash and cash equivalents, ending	$355,485	$129,881
Supplemental disclosure of cash flow information		
Interest paid	$10,120	$6,501
Income tax	5,739	11,312
Supplemental disclosures of noncash operating, investing, and financing activities		
Unrealized holding gains on available-for-sale securities, net of taxes	$322	$2
Transfers from loans to foreclosed real estate and other repossessions	406	700
Transfers from foreclosed real estate to SBA receivable	96	—
Transfers of loans accounted for as secured borrowing collateral to other assets	—	4,575
Transfer of loans held for sale to loans held for investment	339,322	7,410
Transfer of loans held for investment to loans held for sale	2,296	2,129
Contingent consideration in acquisition of controlling interest in equity method investment	24	170

See Notes to Unaudited Consolidated Financial Statements

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements
Note 1. Basis of Presentation
Nature of Operations

Live Oak Bancshares, Inc. (the “Company” or “LOB”) is a bank holding company headquartered in Wilmington, North Carolina incorporated under the laws of North Carolina in December 2008. The Company conducts business operations primarily through its commercial bank subsidiary, Live Oak Banking Company (the “Bank”). The Bank was established in May 2008 as a North Carolina-chartered commercial bank. The Bank specializes in providing lending services to small businesses nationwide in targeted industries. The Bank identifies and grows within credit-worthy industries through expertise within those industries. A significant portion of the loans originated by the Bank are guaranteed by the Small Business Administration (“SBA”) under the 7(a) program. On July 28, 2015 the Company completed its initial public offering. In 2010, the Bank formed Live Oak Number One, Inc., a wholly-owned subsidiary, to hold properties foreclosed on by the Bank.

During 2011, the Company formed Independence Aviation, LLC, a wholly-owned subsidiary, for the purpose of purchasing and operating aircraft used for business purposes of the Company. The net assets of Independence Aviation, LLC were transferred to the Company and the Bank effective December 31, 2015 resulting in its dissolution.

In addition to the Bank, the Company owns Live Oak Grove, LLC, opened in September 2015 for the purpose of providing Company employees and business visitors an on-site restaurant location, Government Loan Solutions, Inc. (“GLS”), a management and technology consulting firm that specializes in the settlement, accounting, and securitization processes for government guaranteed loans, including loans originated under the SBA 7(a) loan program and USDA-guaranteed loans, and 504 Fund Advisors, LLC (“504FA”), formed to serve as the investment adviser to the 504 Fund, a closed-end mutual fund organized to invest in SBA section 504 loans.

The Company acquired control over 504FA, previously carried as an equity method investment, on February 2, 2015 by increasing its ownership from 50.0% to 91.3%. The acquisition of an additional 41.3% of ownership occurred in exchange for contingent consideration estimated to total $170 thousand. Transactions in the third quarter of 2015 and first quarter of 2016 increased the Company’s ownership to 92.9%. On September 1, 2016, the Company acquired the remaining 7.1% ownership from a third party investor in exchange for contingent consideration estimated to total $24 thousand.

In August 2016, the Company formed Live Oak Ventures, Inc. for the purpose of investing in businesses that align with the Company's strategic initiative to be a leader in online banking for small businesses.

The Company earns revenue primarily from the sale of SBA-guaranteed loans. This income is comprised of net gains on the sale of loans, revenues on the servicing of sold loans and valuation of loan servicing rights. Net interest income is another contributor to earnings. Offsetting these revenues are the cost of funding sources, provision for loan losses, any costs related to foreclosed assets and other operating costs such as salaries and employee benefits, travel, professional services, advertising and marketing and tax expense.

General

In the opinion of management, all adjustments necessary for a fair presentation of the financial position and results of operations for the periods presented have been included, and all intercompany transactions have been eliminated in consolidation. Results of operations for the nine months ended September 30, 2016 are not necessarily indicative of the results of operations that may be expected for the year ending December 31, 2016. The consolidated balance sheet as of December 31, 2015 has been derived from the audited consolidated financial statements contained in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2015, filed with the Securities Exchange Commission on March 14, 2016 (SEC File No. 001-37497) (the "2015 Annual Report"). A summary description of the significant accounting policies followed by the Company is set forth in Note 1 of the Notes to Consolidated Financial Statements in the Company’s 2015 Annual Report. These unaudited interim consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes in the Company's 2015 Annual Report.

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

Amounts in all tables in the Notes to Unaudited Consolidated Financial Statements have been presented in thousands, except percentage, time period, stock option, share and per share data or where otherwise indicated.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Business Segments
Management has determined that the Company has one significant operating segment, which is providing a lending platform for small businesses nationwide. In determining the appropriateness of segment definition, the Company considers the materiality of a potential segment, the components of the business about which financial information is available, and components for which management regularly evaluates relative to resource allocation and performance assessment.
Loans Reclassified to Held for Investment
Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are classified as held for investment ("HFI") and reported at their outstanding principal amount adjusted for any charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans and unamortized premium or discount on purchased loans. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method. Loans originated and intended for sale are classified as held for sale ("HFS") and carried at the lower of cost or estimated fair value.
During the second quarter of 2016, the Bank transferred $318.8 million in unguaranteed loans from the HFS category to the HFI category to better reflect current intentions of the Company.
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 uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.
The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility 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.
Upon transfer from held for sale classification, loans held for investment become subject to the allowance for loan loss review process. As a result of this process, the above mentioned $318.8 million loan reclassification resulted in a $4.0 million increase in the provision for loan losses during the second quarter of 2016.
During the second quarter of 2016, the Company also implemented enhancements to the methodology for estimating the allowance for loan losses, including refinements to the measurement of qualitative factors in the estimation process. Management believes these enhancements will improve the precision of the process for estimating the allowance, but did not fundamentally change the Company's approach. These revisions resulted in a $390 thousand reduction in the provision for loan losses during the second quarter of 2016.
Reclassifications
Certain reclassifications have been made to the prior period's consolidated financial statements to place them on a comparable basis with the current year. Net income and shareholders' equity previously reported were not affected by these reclassifications.
Note 2. Recent Accounting Pronouncements
In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-08, "Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)" ("ASU 2016-08"). This guidance amends the previously issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)." ASU 2016-08 clarifies the implementation guidance on principal versus agent considerations in order to determine if revenue will be recognized on a gross or net basis. This guidance is effective for the Company on January 1, 2018 and is not expected to have a material impact on the consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, “Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting” (“ASU 2016-09”). ASU 2016-09 simplifies the accounting for share-based payment transactions for items including income tax consequences, classification of awards as equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 will be effective for the Company on January 1, 2017 and the Company is currently assessing the impact the adoption of this standard will have on the consolidated financial statements. Early adoption is permitted.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

In April 2016, the FASB issued ASU No. 2016-10, "Identifying Performance Obligations and Licensing" ("ASU 2016-10"). This guidance amends the previously issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)" ("ASU 2014-09"). ASU 2016-10 clarifies the guidance related to identifying performance obligations and accounting for licenses of intellectual property. The amendments will be effective for the Company on January 1, 2018. The Company does not expect these amendments to have a material effect on its consolidated financial statements.

In May 2016, the FASB issued ASU No. 2016-12, "Narrow-Scope Improvements and Practical Expedients" ("ASU 2016-12"). This guidance also amends the previously issued ASU No. 2014-09 to clarify guidance related to collectibility, noncash consideration, presentation of sales tax and transition. The amendments will be effective for the Company on January 1, 2018. The Company does not expect these amendments to have a material effect on its consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, "Measurement of Credit Losses on Financial Instruments" ("ASU 2016-13"). This new guidance replaces the incurred loss impairment methodology in current standards with an expected credit loss methodology and requires consideration of a broader range of information to determine credit loss estimates. ASU 2016-13 requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts and requires enhanced disclosures related to the significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization’s portfolio. In addition, ASU 2016-13 amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. ASU 2016-13 will be effective for the Company on January 1, 2020. The Company is currently evaluating the effect the implementation of the new standard will have on its consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, "Classification of Certain Cash Receipts and Cash Payments" ("ASU 2016-15"). This guidance amends the Accounting Standards Codification 230, "Statement of Cash Flows," to clarify how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The ASU addresses cash flow issues including: (i) debt prepayment or debt extinguishment costs, (ii) zero-coupon bonds, (iii) settlement of a contingent consideration liability, (iv) proceeds from the settlement of insurance claims, (v) proceeds from corporate-owned life insurance, (vi) distributions received from equity method investees, (vii) beneficial interests in securitization transactions, and (viii) the "predominance principle." ASU 2016-15 will be effective for the Company on January 1, 2018. The Company does not expect these amendments to have a material effect on its consolidated financial statements.

Note 3. Earnings Per Share

Basic and diluted earnings per share are computed based on the weighted average number of shares outstanding during each period. Diluted earnings per share reflects the potential dilution that could occur, upon the exercise of stock options or upon the vesting of restricted stock grants, any of which would result in the issuance of common stock that would then be shared in the net income of the Company.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Basic earnings per share:				
Net income available to common shareholders	$3,479	$ 2,901	$8,293	$ 14,910
Weighted-average basic shares outstanding	34,206,942	32,824,587	34,191,010	34,037,436
Basic earnings per share	$0.10	$ 0.09	$0.24	$ 0.50
Diluted earnings per share:				
Net income available to common shareholders, for diluted earnings per share	$3,479	$ 2,901	$8,293	$ 14,910

Total weighted-average basic shares outstanding	34,206,943	32,824,587	34,191,014	30,037,436
Add effect of dilutive stock options and restricted stock grants	794,874	1,092,695	812,408	892,794
Total weighted-average diluted shares outstanding	35,001,817	33,917,282	35,003,422	30,930,230
Diluted earnings per share	$ 0.10	$ 0.09	$ 0.24	$ 0.48
Anti-dilutive shares	1,778,995	1,391,828	1,778,995	1,562,168

9

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Note 4. Investment Securities
The carrying amount of investment securities and their approximate fair values are reflected in the following table:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
September 30, 2016				
US government agencies	$ 20,770	$ 98	$ 7	$20,861
Residential mortgage-backed securities	47,356	184	89	47,451
Mutual fund	1,997	25	—	2,022
Total	$ 70,123	$ 307	$ 96	$70,334
December 31, 2015				
US government agencies	$ 21,992	$ 81	$ 5	$22,068
Residential mortgage-backed securities	30,131	1	374	29,758
Mutual fund	1,951	—	15	1,936
Total	$ 54,074	$ 82	$ 394	$53,762

During the three and nine months ended September 30, 2016, the Company sold one mortgage-backed security for $1.9 million at a gain of $1 thousand.
During the three months ended September 30, 2015, the Company sold three US government agency securities for $8.3 million at a gain of $12 thousand. In addition, during the first and second quarters of 2015, the Company sold six mortgage-backed securities at their carrying amount for $3.4 million in an odd-lot consolidation.
The following tables show gross unrealized losses and fair value, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position.

	Less Than 12 Months		12 Months or More		Total	
September 30, 2016	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
US government agencies	$1,515	$ 7	$—	$ —	$1,515	$ 7
Residential mortgage-backed securities	20,696	76	1,676	13	22,372	89
Total	$22,211	$ 83	$1,676	$ 13	$23,887	$ 96

	Less Than 12 Months		12 Months or More		Total	
December 31, 2015	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
US government agencies	$7,990	$ 5	$—	$ —	$7,990	$ 5
Residential mortgage-backed securities	26,015	333	3,019	41	29,034	374
Mutual fund	1,936	15	—	—	1,936	15
Total	$35,941	$ 353	$3,019	$ 41	$38,960	$ 394

At September 30, 2016, there were two mortgage-backed securities in unrealized loss positions for greater than 12 months and seven mortgage-backed securities and one US government agency security in an unrealized loss position for less than 12 months. Unrealized losses at December 31, 2015 were comprised of three mortgage-backed securities in unrealized loss positions for greater than 12 months and one US government agency security, twelve mortgage-backed securities and the 504 Fund mutual fund investment in an unrealized loss position for less than 12 months.
These unrealized losses are primarily the result of volatility in the market and are related to market interest rates. Since none of the unrealized losses relate to marketability of the securities or the issuer’s ability to honor redemption

obligations, none of the securities are deemed to be other than temporarily impaired.

All residential mortgage-backed securities in the Company’s portfolio at September 30, 2016 and December 31, 2015 were backed by US government sponsored enterprises (“GSEs”).

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

The following is a summary of investment securities by maturity:

	September 30, 2016	
	Available-for-Sale	
	Amortized cost	Fair value
US government agencies		
Within one year	$7,998	$8,007
One to five years	12,772	12,854
Total	20,770	20,861
Residential mortgage-backed securities		
Five to ten years	7,817	7,872
After 10 years	39,539	39,579
Total	47,356	47,451
Total	$68,126	$68,312

The table above reflects contractual maturities. Actual results will differ as the loans underlying the mortgage-backed securities may repay sooner than scheduled. This table excludes the 504 Fund mutual fund investment.

At September 30, 2016 and December 31, 2015, an investment security with a fair market value of $1.5 million and $1.3 million, respectively, was pledged to secure a line of credit with the Company’s correspondent bank. At September 30, 2016, an investment security with a fair market value of $101 thousand was pledged to the Ohio State Treasurer to allow the Company's trust department to conduct business in the state of Ohio and an investment security with a fair market value of $1.2 million was pledged to the Company's trust department for uninsured trust assets held by the trust department.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Note 5. Loans Held for Investment and Allowance for Loan Losses
Loan Portfolio Segments
The following describes the risk characteristics relevant to each of the portfolio segments. Each loan category is assigned a risk grade during the origination and closing process based on criteria described later in this section.
Commercial and Industrial
Commercial and industrial loans (C&I) receive similar underwriting treatment as commercial real estate loans in that the repayment source is analyzed to determine its ability to meet cash flow coverage requirements as set forth by Bank policies. Repayment of the Bank's C&I loans generally comes from the generation of cash flow as the result of the borrower's business operations. This business cycle itself brings a certain level of risk to the portfolio. In some instances, these loans may carry a higher degree of risk due to a variety of reasons – illiquid collateral, specialized equipment, highly depreciable assets, uncollectable accounts receivable, revolving balances, or simply being unsecured. As a result of these characteristics, the SBA guarantee on these loans is an important factor in mitigating risk.
Construction and Development
Construction and development loans are for the purpose of acquisition and development of land to be improved through the construction of commercial buildings. Such loans are usually paid off through the conversion to permanent financing for the long-term benefit of the borrower's ongoing operations. At the completion of the project, if the loan is converted to permanent financing or if scheduled loan amortization begins, it is then reclassified to the "Commercial Real Estate" segment. Underwriting of construction and development loans typically includes analysis of not only the borrower's financial condition and ability to meet the required debt obligations, but also the general market conditions associated with the area and type of project being funded.
Commercial Real Estate
Commercial real estate loans are extensions of credit secured by owner occupied and non-owner occupied collateral. Underwriting generally involves intensive analysis of the financial strength of the borrower and guarantor, liquidation value of the subject collateral, the associated unguaranteed exposure, and any available secondary sources of repayment, with the greatest emphasis given to a borrower's capacity to meet cash flow coverage requirements as set forth by Bank policies. Such repayment of commercial real estate loans is commonly derived from the successful ongoing operations of the business occupying the property. These typically include small businesses and professional practices.
Commercial Land
Commercial land loans are extensions of credit secured by farmland. Such loans are often for land improvements related to agricultural endeavors that may include construction of new specialized facilities. These loans are usually repaid through the conversion to permanent financing, or if scheduled loan amortization begins, for the long-term benefit of the borrower's ongoing operations. Underwriting generally involves intensive analysis of the financial strength of the borrower and guarantor, liquidation value of the subject collateral, the associated unguaranteed exposure, and any available secondary sources of repayment, with the greatest emphasis given to a borrower's capacity to meet cash flow coverage requirements as set forth by Bank policies.
Each of the loan types referenced in the sections above is further segmented into verticals in which the Bank chooses to operate. The Bank chooses to finance businesses operating in specific industries because of certain similarities. The similarities range from historical default and loss characteristics to business operations. However, there are differences that create the necessity to underwrite these loans according to varying criteria and guidelines. When underwriting a loan, the Bank considers numerous factors such as cash flow coverage, the credit scores of the guarantors, revenue growth, practice ownership experience and debt service capacity. Minimum guidelines have been set with regard to these various factors and deviations from those guidelines require compensating strengths when considering a proposed loan.

12

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Loans consist of the following:

	September 30, 2016	December 31, 2015
Commercial & Industrial		
Agriculture	$1,503	$30
Death Care Management	9,584	4,832
Healthcare	33,822	15,240
Independent Pharmacies	80,317	41,588
Registered Investment Advisors	61,521	18,358
Veterinary Industry	34,922	21,579
Other Industries	41,660	3,230
Total	263,329	104,857
Construction & Development		
Agriculture	34,867	11,351
Death Care Management	2,500	769
Healthcare	28,454	7,231
Independent Pharmacies	2,387	101
Registered Investment Advisors	900	378
Veterinary Industry	11,662	3,834
Other Industries	20,080	658
Total	100,850	24,322
Commercial Real Estate		
Agriculture	5,637	1,863
Death Care Management	50,611	20,327
Healthcare	99,519	37,684
Independent Pharmacies	14,697	7,298
Registered Investment Advisors	8,388	2,808
Veterinary Industry	98,003	59,999
Other Industries	30,713	4,752
Total	307,568	134,731
Commercial Land		
Agriculture	94,111	16,036
Total	94,111	16,036
Total Loans[1]	765,858	279,946
Net Deferred Costs	7,613	3,056
Discount on SBA 7(a) Unguaranteed[2]	(6,494)	(3,033)
Loans, Net of Unearned	$766,977	$279,969

1 Total loans include $29.6 million and $17.2 million of U.S. government guaranteed loans as of September 30, 2016 and December 31, 2015, respectively.

2 The Company measures the carrying value of the retained portion of loans sold at fair value under ASC Subtopic 825-10. The value of these retained loan balances is discounted based on the estimates derived from comparable unguaranteed loan sales.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Credit Risk Profile

The Bank uses internal loan reviews to assess the performance of individual loans by industry segment. An independent review of the loan portfolio is performed annually by an external firm. The goal of the Bank's annual review of select borrowers' financial performance is to validate the adequacy of the risk grade assigned.

The Bank uses a grading system to rank the quality of each loan. The grade is periodically evaluated and adjusted as performance dictates. Loan grades 1 through 4 are passing grades and grade 5 is special mention. Collectively, grades 6 through 8 represent classified loans in the Bank's portfolio. The following guidelines govern the assignment of these risk grades:

Exceptional Loans (1 Rated): These loans are of the highest quality, with strong, well-documented sources of repayment. Debt service coverage ("DSC") is over 1.75X based on historical results. Secondary source of repayment is strong, with a loan to value ("LTV") of 65% or less if secured solely by commercial real estate ("CRE"). Discounted collateral coverage from all sources should exceed 125%. Guarantors have credit scores above 740.

Quality Loans (2 Rated): These loans are of good quality, with good, well-documented sources of repayment. DSC is over 1.25X based on historical or pro-forma results. Secondary source of repayment is good, with a LTV of 75% or less if secured solely by CRE. Discounted collateral coverage should exceed 100%. Guarantors have credit scores above 700.

Acceptable Loans (3 rated): These loans are of acceptable quality, with acceptable sources of repayment. DSC of over 1.00X based on historical or pro-forma results. Companies that do not meet these credit metrics must be evaluated to determine if they should be graded below this level.

Acceptable Loans (4 rated): These loans are considered very weak pass. These loans are riskier than a 3-rated credit, but due to various mitigating factors are not considered a Special mention or worse. The mitigating factors must clearly be identified to offset further downgrade. Examples of loans that may be put in this category include start-up loans and loans with less than 1:1 cash flow coverage with other sources of repayment.

Special mention (5 rated): These loans are considered as emerging problems, with potentially unsatisfactory characteristics. These loans require greater management attention. A loan may be put into this category if the Bank is unable to obtain financial reporting from a company to fully evaluate its position.

Substandard (6 rated): Loans graded Substandard are inadequately protected by current sound net worth, paying capacity of the borrower, or pledged collateral. They typically have unsatisfactory characteristics causing more than acceptable levels of risk, and have one or more well-defined weaknesses that could jeopardize the repayment of the debt.

Doubtful (7 rated): Loans graded Doubtful have inherent weaknesses that make collection or liquidation in full questionable. Loans graded Doubtful must be placed on non-accrual status.

Loss (8 rated): Loss rated loans are considered uncollectible and of such little value that their continuance as an active Bank asset is not warranted. The asset should be charged off, even though partial recovery may be possible in the future.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

The following tables summarize the risk grades of each category:

	Risk Grades 1 - 4	Risk Grade 5	Risk Grades 6 - 8	Total
September 30, 2016				
Commercial & Industrial				
Agriculture	$ 1,445	$ 58	$ —	$1,503
Death Care Management	9,351	225	8	9,584
Healthcare	26,658	1,497	5,667	33,822
Independent Pharmacies	73,847	4,790	1,680	80,317
Registered Investment Advisors	58,427	2,730	364	61,521
Veterinary Industry	30,736	1,980	2,206	34,922
Other Industries	41,660	—	—	41,660
Total	242,124	11,280	9,925	263,329
Construction & Development				
Agriculture	34,867	—	—	34,867
Death Care Management	2,500	—	—	2,500
Healthcare	26,042	2,412	—	28,454
Independent Pharmacies	2,387	—	—	2,387
Registered Investment Advisors	900	—	—	900
Veterinary Industry	10,177	1,485	—	11,662
Other Industries	20,080	—	—	20,080
Total	96,953	3,897	—	100,850
Commercial Real Estate				
Agriculture	5,637	—	—	5,637
Death Care Management	45,801	3,228	1,582	50,611
Healthcare	93,248	5,270	1,001	99,519
Independent Pharmacies	12,613	2,084	—	14,697
Registered Investment Advisors	8,388	—	—	8,388
Veterinary Industry	83,540	3,787	10,676	98,003
Other Industries	30,713	—	—	30,713
Total	279,940	14,369	13,259	307,568
Commercial Land				
Agriculture	92,379	1,582	150	94,111
Total	92,379	1,582	150	94,111
Total[1]	$ 711,396	$ 31,128	$ 23,334	$765,858

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

	Risk Grades 1 - 4	Risk Grade 5	Risk Grades 6 - 8	Total
December 31, 2015				
Commercial & Industrial				
Agriculture	$ 30	$ —	$ —	$30
Death Care Management	4,728	104	—	4,832
Healthcare	8,334	2,160	4,746	15,240
Independent Pharmacies	36,704	3,430	1,454	41,588
Registered Investment Advisors	17,508	850	—	18,358
Veterinary Industry	16,800	1,817	2,962	21,579
Other Industries	3,089	141	—	3,230
Total	87,193	8,502	9,162	104,857
Construction & Development				
Agriculture	11,194	157	—	11,351
Death Care Management	769	—	—	769
Healthcare	7,231	—	—	7,231
Independent Pharmacies	101	—	—	101
Registered Investment Advisors	378	—	—	378
Veterinary Industry	2,581	1,253	—	3,834
Other Industries	658	—	—	658
Total	22,912	1,410	—	24,322
Commercial Real Estate				
Agriculture	1,863	—	—	1,863
Death Care Management	18,223	425	1,679	20,327
Healthcare	33,529	2,930	1,225	37,684
Independent Pharmacies	6,210	1,088	—	7,298
Registered Investment Advisors	2,808	—	—	2,808
Veterinary Industry	45,453	3,171	11,375	59,999
Other Industries	4,752	—	—	4,752
Total	112,838	7,614	14,279	134,731
Commercial Land				
Agriculture	16,036	—	—	16,036
Total	16,036	—	—	16,036
Total[1]	$ 238,979	$ 17,526	$ 23,441	$279,946

1 Total loans include $29.6 million of U.S. government guaranteed loans as of September 30, 2016, segregated by risk grade as follows: Risk Grades 1 – 4 = $8.8 million, Risk Grade 5 = $7.0 million, Risk Grades 6 – 8 = $13.8 million. As of December 31, 2015, total loans include $17.2 million of U.S. government guaranteed loans, segregated by risk grade as follows: Risk Grades 1 – 4 = $0, Risk Grade 5 = $2.6 million, Risk Grades 6 – 8 = $14.6 million.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Past Due Loans
Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due. Loans less than 30 days past due and accruing are included within current loans shown below. The following tables show an age analysis of past due loans as of the dates presented.

	Less Than 30 Days Past Due & Not Accruing	30-89 Days Past Due & Accruing	30-89 Days Past Due & Not Accruing	Greater Than 90 Days Past Due	Total Not Accruing & Past Due Loans	Current Loans	Total Loans	Loans 90 Days or More Past Due & Still Accruing
September 30, 2016								
Commercial & Industrial								
Agriculture	$ —	$ —	$ —	$ —	$ —	$ 1,503	$ 1,503	$ —
Death Care Management	—	—	—	—	—	9,584	9,584	—
Healthcare	212	623	1,377	2,589	4,801	29,021	33,822	—
Independent Pharmacies	—	327	288	421	1,036	79,281	80,317	—
Registered Investment Advisors	—	—	—	—	—	61,521	61,521	—
Veterinary Industry	41	31	1,238	573	1,883	33,039	34,922	—
Other Industries	—	—	—	—	—	41,660	41,660	—
Total	253	981	2,903	3,583	7,720	255,609	263,329	—
Construction & Development								
Agriculture	—	—	—	—	—	34,867	34,867	—
Death Care Management	—	—	—	—	—	2,500	2,500	—
Healthcare	—	—	—	—	—	28,454	28,454	—
Independent Pharmacies	—	—	—	—	—	2,387	2,387	—
Registered Investment Advisors	—	—	—	—	—	900	900	—
Veterinary Industry	—	—	—	—	—	11,662	11,662	—
Other Industries	—	—	—	—	—	20,080	20,080	—
Total	—	—	—	—	—	100,850	100,850	—
Commercial Real Estate								
Agriculture	—	—	—	—	—	5,637	5,637	—
Death Care Management	—	—	204	1,423	1,627	48,984	50,611	—
Healthcare	—	201	127	46	374	99,145	99,519	—
Independent Pharmacies	—	550	—	—	550	14,147	14,697	—
Registered Investment Advisors	—	—	—	—	—	8,388	8,388	—
Veterinary Industry	1,119	3,460	2,178	2,037	8,794	89,209	98,003	—
Other Industries	—	—	—	—	—	30,713	30,713	—
Total	1,119	4,211	2,509	3,506	11,345	296,223	307,568	—
Commercial Land								
Agriculture	150	—	—	—	150	93,961	94,111	—
Total	150	—	—	—	150	93,961	94,111	—
Total[1]	$ 1,522	$ 5,192	$ 5,412	$ 7,089	$ 19,215	$ 746,643	$ 765,858	$ —

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

	Less Than 30 Days Past Due & Not Accruing	30-89 Days Past Due & Accruing	30-89 Days Past Due & Not Accruing	Greater Than 90 Days Past Due	Total Not Accruing & Past Due Loans	Current Loans	Total Loans	Loans 90 Days or More Past Due & Still Accruing
December 31, 2015								
Commercial & Industrial								
Agriculture	$ —	$ —	$ —	$ —	$ —	$ 30	$ 30	$ —
Death Care Management	—	—	—	—	—	4,832	4,832	—
Healthcare	—	1,854	30	2,337	4,221	11,019	15,240	—
Independent Pharmacies	314	603	—	—	917	40,671	41,588	—
Registered Investment Advisors	—	—	—	—	—	18,358	18,358	—
Veterinary Industry	208	466	1,131	394	2,199	19,380	21,579	—
Other Industries	—	—	—	—	—	3,230	3,230	—
Total	522	2,923	1,161	2,731	7,337	97,520	104,857	—
Construction & Development								
Agriculture	—	—	—	—	—	11,351	11,351	—
Death Care Management	—	—	—	—	—	769	769	—
Healthcare	—	—	—	—	—	7,231	7,231	—
Independent Pharmacies	—	—	—	—	—	101	101	—
Registered Investment Advisors	—	—	—	—	—	378	378	—
Veterinary Industry	—	—	—	—	—	3,834	3,834	—
Other Industries	—	—	—	—	—	658	658	—
Total	—	—	—	—	—	24,322	24,322	—
Commercial Real Estate								
Agriculture	—	—	—	—	—	1,863	1,863	—
Death Care Management	1,456	223	—	—	1,679	18,648	20,327	—
Healthcare	—	240	135	831	1,206	36,478	37,684	—
Independent Pharmacies	—	—	—	—	—	7,298	7,298	—
Registered Investment Advisors	—	—	—	—	—	2,808	2,808	—
Veterinary Industry	311	5,079	2,048	3,172	10,610	49,389	59,999	—
Other Industries	—	—	—	—	—	4,752	4,752	—
Total	1,767	5,542	2,183	4,003	13,495	121,236	134,731	—
Commercial Land								
Agriculture	—	—	—	—	—	16,036	16,036	—
Total	—	—	—	—	—	16,036	16,036	—
Total[1]	$ 2,289	$ 8,465	$ 3,344	$ 6,734	$ 20,832	$ 259,114	$ 279,946	$ —

1 Total loans include $29.6 million of U.S. government guaranteed loans as of September 30, 2016, of which $6.3 million is greater than 90 days past due, $5.8 million is 30-89 days past due and $17.5 million is included in current loans as presented above. As of December 31, 2015, total loans include $17.2 million of U.S. government guaranteed loans, of which $5.9 million is greater than 90 days past due, $6.7 million is 30-89 days past due and $4.6

million is included in current loans as presented above.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Nonaccrual Loans

Loans that become 90 days delinquent, or in cases where there is evidence that the borrower's ability to make the required payments is impaired, are placed in nonaccrual status and interest accrual is discontinued. If interest on nonaccrual loans had been accrued in accordance with the original terms, interest income would have increased by approximately $165 thousand and $358 thousand for the three months ended September 30, 2016 and 2015, respectively, and for the nine months ended September 30, 2016 and 2015 interest income would have increased approximately $451 thousand and $665 thousand, respectively. All nonaccrual loans are included in the held for investment portfolio.

Nonaccrual loans as of September 30, 2016 and December 31, 2015 are as follows:

September 30, 2016	Loan Balance	Guaranteed Balance	Unguaranteed Exposure
Commercial & Industrial			
Healthcare	$4,178	$ 2,862	$ 1,316
Independent Pharmacies	709	552	157
Veterinary Industry	1,852	1,648	204
Total	6,739	5,062	1,677
Commercial Real Estate			
Death Care Management	1,627	1,264	363
Healthcare	173	35	138
Veterinary Industry	5,334	4,270	1,064
Total	7,134	5,569	1,565
Commercial Land			
Agriculture	150	38	112
Total	150	38	112
Total	$14,023	$ 10,669	$ 3,354

December 31, 2015	Loan Balance	Guaranteed Balance	Unguaranteed Exposure
Commercial & Industrial			
Healthcare	$2,367	$ 2,188	$ 179
Independent Pharmacies	314	308	6
Veterinary Industry	1,733	1,572	161
Total	4,414	4,068	346
Commercial Real Estate			
Death Care Management	1,456	1,290	166
Healthcare	966	798	168
Veterinary Industry	5,531	4,174	1,357
Total	7,953	6,262	1,691
Total	$12,367	$ 10,330	$ 2,037

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Allowance for Loan Loss Methodology

The methodology and the estimation process for calculating the Allowance for Loan Losses ("ALL") is described below:

Estimated credit losses should meet the criteria for accrual of a loss contingency, i.e., a provision to the ALL, set forth in GAAP. The Company's methodology for determining the ALL is based on the requirements of GAAP, the Interagency Policy Statement on the Allowance for Loan and Lease Losses and other regulatory and accounting pronouncements. The ALL is determined by the sum of three separate components: (i) the impaired loan component, which addresses specific reserves for impaired loans; (ii) the general reserve component, which addresses reserves for pools of homogeneous loans; and (iii) an unallocated reserve component (if any) based on management's judgment and experience. The loan pools and impaired loans are mutually exclusive; any loan that is impaired is excluded from its homogenous pool for purposes of that pool's reserve calculation, regardless of the level of impairment.

The ALL policy for pooled loans is governed in accordance with banking regulatory guidance for homogenous pools of non-impaired loans that have similar risk characteristics. The Company follows a consistent and structured approach for assessing the need for reserves within each individual loan pool.

Loans are considered impaired when, based on current information and events, it is probable that the creditor will be unable to collect all interest and principal payments due according to the originally contracted, or reasonably modified, terms of the loan agreement. The Company has determined that loans that meet the criteria defined below must be reviewed quarterly to determine if they are impaired.

- All commercial loans classified substandard or worse.
- Any other delinquent loan that is in a nonaccrual status, or any loan that is delinquent more than 89 days and still accruing interest.
- Any loan which has been modified such that it meets the definition of a Troubled Debt Restructuring (TDR).

Prior to December 31, 2015, all loans subject to impairment recognition were individually evaluated for impairment. Effective December 31, 2015, the Company's policy for impaired loan accounting subjects all loans to impairment recognition; however, loan relationships with unguaranteed credit exposure of less than $100,000 are generally not evaluated on an individual basis for impairment and instead are evaluated collectively using a methodology based on historical specific reserves on similar sized loans. Any loan not meeting the above criteria and determined to be impaired is subjected to an impairment analysis, which is a calculation of the probable loss on the loan. This portion is the loan's "impairment," and is established as a specific reserve against the loan, or charged against the ALL. This revision to the allowance methodology did not have a material impact on the allowance recorded at December 31, 2015.

Individual specific reserve amounts imply probability of loss and may not be carried in the reserve indefinitely. When the amount of the actual loss becomes reasonably quantifiable, the amount of the loss is charged off against the ALL, whether or not all liquidation and recovery efforts have been completed. If the total amount of the individual specific reserve that will eventually be charged off cannot yet be sufficiently quantified but some portion of the impairment can be viewed as a confirmed loss, then the confirmed loss portion should be charged off against the ALL and the individual specific reserve reduced by a corresponding amount.

For impaired loans, the reserve amount is calculated on a loan-specific basis. The Company utilizes two methods of analyzing impaired loans not guaranteed by the SBA:

- The Fair Market Value of Collateral method utilizes the value at which the collateral could be sold considering the appraised value, appraisal discount rate, prior liens and selling costs. The amount of the reserve is the deficit of the estimated collateral value compared to the loan balance.
- The Present Value of Future Cash Flows method takes into account the amount and timing of cash flows and the effective interest rate used to discount the cash flows.

20

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

The following table details activity in the allowance for loan losses by portfolio segment allowance for the periods presented:

Three months ended:	Construction & Development	Commercial Real Estate	Commercial & Industrial	Commercial Land	Total
September 30, 2016					
Beginning Balance	$ 1,208	$ 4,079	$ 5,601	$ 1,421	$12,309
Charge offs	—	—	(939)	—	(939)
Recoveries	—	1	1	—	2
Provision	225	261	2,907	413	3,806
Ending Balance	$ 1,433	$ 4,341	$ 7,570	$ 1,834	$15,178
September 30, 2015					
Beginning Balance	$ 844	$ 2,346	$ 1,653	$ 340	$5,183
Charge offs	—	(7)	(280)	—	(287)
Recoveries	—	12	33	—	45
Provision	336	(260)	830	306	1,212
Ending Balance	$ 1,180	$ 2,091	$ 2,236	$ 646	$6,153

Nine months ended:	Construction & Development	Commercial Real Estate	Commercial & Industrial	Commercial Land	Total
September 30, 2016					
Beginning Balance	$ 1,064	$ 2,486	$ 2,766	$ 1,099	$7,415
Charge offs	—	(7)	(1,307)	(63)	(1,377)
Recoveries	—	4	444	—	448
Provision	369	1,858	5,667	798	8,692
Ending Balance	$ 1,433	$ 4,341	$ 7,570	$ 1,834	$15,178
September 30, 2015					
Beginning Balance	$ 586	$ 2,291	$ 1,369	$ 161	$4,407
Charge offs	—	(128)	(638)	—	(766)
Recoveries	—	100	73	—	173
Provision	594	(172)	1,432	485	2,339
Ending Balance	$ 1,180	$ 2,091	$ 2,236	$ 646	$6,153

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

The following tables detail the recorded allowance for loan losses and the investment in loans related to each portfolio segment, disaggregated on the basis of impairment evaluation methodology:

September 30, 2016	Construction & Development	Commercial Real Estate	Commercial & Industrial	Commercial Land	Total
Allowance for Loan Losses:					
Loans individually evaluated for impairment	$ —	$ 1,385	$ 1,563	$ —	$2,948
Loans collectively evaluated for impairment[2]	1,433	2,956	6,007	1,834	12,230
Total allowance for loan losses	$ 1,433	$ 4,341	$ 7,570	$ 1,834	$15,178
Loans receivable[1]:					
Loans individually evaluated for impairment	$ —	$ 13,541	$ 4,371	$ 144	$18,056
Loans collectively evaluated for impairment[2]	100,850	294,027	258,958	93,967	747,802
Total loans receivable	$ 100,850	$ 307,568	$ 263,329	$ 94,111	$765,858

December 31, 2015	Construction & Development	Commercial Real Estate	Commercial & Industrial	Commercial Land	Total
Allowance for Loan Losses:					
Loans individually evaluated for impairment	$ —	$ 1,090	$ 672	$ —	$1,762
Loans collectively evaluated for impairment[2]	1,064	1,396	2,094	1,099	5,653
Total allowance for loan losses	$ 1,064	$ 2,486	$ 2,766	$ 1,099	$7,415
Loans receivable[1]:					
Loans individually evaluated for impairment	$ —	$ 9,821	$ 3,226	$ —	$13,047
Loans collectively evaluated for impairment[2]	24,322	124,910	101,631	16,036	266,899
Total loans receivable	$ 24,322	$ 134,731	$ 104,857	$ 16,036	$279,946

1 Loans receivable includes $29.6 million of U.S. government guaranteed loans as of September 30, 2016, of which $13.9 million are impaired. As of December 31, 2015, loans receivable includes $17.2 million of U.S. government guaranteed loans, of which $14.1 million are considered impaired.

2 Included in loans collectively evaluated for impairment are impaired loans with individual unguaranteed exposure of less than $100 thousand. As of September 30, 2016, these balances totaled $8.6 million, of which $6.7 million are guaranteed by the U.S. government and $1.9 million are unguaranteed. As of December 31, 2015, these balances totaled $8.6 million, of which $7.5 million are guaranteed by the U.S. government and $1.1 million are unguaranteed. The allowance for loan losses associated with these loans totaled $406 thousand and $352 thousand as of September 30, 2016 and December 31, 2015, respectively.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Loans classified as impaired as of the dates presented are summarized in the following tables.

September 30, 2016	Recorded Investment	Guaranteed Balance	Unguaranteed Exposure
Commercial & Industrial			
Death Care Management	$ 8	$ —	$ 8
Healthcare	5,722	3,172	2,550
Independent Pharmacies	2,020	985	1,035
Registered Investment Advisors	735	—	735
Veterinary Industry	2,546	1,779	767
Total	11,031	5,936	5,095
Commercial Real Estate			
Death Care Management	1,785	1,264	521
Healthcare	1,001	290	711
Independent Pharmacies	552	—	552
Veterinary Industry	12,128	6,405	5,723
Total	15,466	7,959	7,507
Commercial Land			
Agriculture	144	38	106
Total	144	38	106
Total	$ 26,641	$ 13,933	$ 12,708

December 31, 2015	Recorded Investment	Guaranteed Balance	Unguaranteed Exposure
Commercial & Industrial			
Healthcare	$ 4,442	$ 3,341	$ 1,101
Independent Pharmacies	1,546	637	909
Veterinary Industry	2,256	1,731	525
Total	8,244	5,709	2,535
Commercial Real Estate			
Death Care Management	1,454	1,290	164
Healthcare	965	799	166
Veterinary Industry	11,003	6,349	4,654
Total	13,422	8,438	4,984
Total	$ 21,666	$ 14,147	$ 7,519

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

The following table presents evaluated balances of loans classified as impaired at the dates presented that carried an associated reserve as compared to those with no reserve. The recorded investment includes accrued interest and net deferred loan fees or costs.

	September 30, 2016				
	Recorded Investment				
	With a Recorded Allowance	With No Recorded Allowance	Total	Unpaid Principal Balance	Related Allowance Recorded
Commercial & Industrial					
Death Care Management	$—	$ 8	$8	$8	$ —
Healthcare	5,122	600	5,722	6,599	825
Independent Pharmacies	1,841	179	2,020	2,109	495
Registered Investment Advisors	735	—	735	731	412
Veterinary Industry	2,255	291	2,546	2,996	199
Total	9,953	1,078	11,031	12,443	1,931
Commercial Real Estate					
Death Care Management	1,422	363	1,785	1,921	8
Healthcare	800	201	1,001	1,001	61
Independent Pharmacies	552	—	552	550	310
Veterinary Industry	9,471	2,657	12,128	12,844	1,044
Total	12,245	3,221	15,466	16,316	1,423
Commercial Land					
Agriculture	—	144	144	213	—
Total	—	144	144	213	—
Total Impaired Loans	$22,198	$ 4,443	$26,641	$28,972	$ 3,354

	December 31, 2015				
	Recorded Investment				
	With a Recorded Allowance	With No Recorded Allowance	Total	Unpaid Principal Balance	Related Allowance Recorded
Commercial & Industrial					
Healthcare	$4,242	$ 200	$4,442	$4,742	$ 478
Independent Pharmacies	1,199	347	1,546	2,041	287
Veterinary Industry	2,051	205	2,256	3,270	138
Total	7,492	752	8,244	10,053	903
Commercial Real Estate					
Death Care Management	1,454	—	1,454	1,591	9
Healthcare	965	—	965	1,096	96
Veterinary Industry	9,265	1,738	11,003	11,856	1,106
Total	11,684	1,738	13,422	14,543	1,211
Total Impaired Loans	$19,176	$ 2,490	$21,666	$24,596	$ 2,114

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

	Three months ended September 30, 2016		Three months ended September 30, 2015	
	Average Balance	Interest Income Recognized	Average Balance	Interest Income Recognized
Commercial & Industrial				
Death Care Management	$9	$ —	$—	$ —
Healthcare	6,345	38	3,460	24
Independent Pharmacies	1,946	18	2,395	13
Registered Investment Advisors	742	7	—	—
Veterinary Industry	2,501	13	3,790	5
Total	11,543	76	9,645	42
Commercial Real Estate				
Death Care Management	1,801	2	1,412	—
Healthcare	1,012	12	2,474	—
Independent Pharmacies	551	2	—	—
Veterinary Industry	12,218	87	11,412	42
Total	15,582	103	15,298	42
Commercial Land				
Agriculture	156	—	—	—
Total	156	—	—	—
Total	$27,281	$ 179	$24,943	$ 84

	Nine months ended September 30, 2016		Nine months ended September 30, 2015	
	Average Balance	Interest Income Recognized	Average Balance	Interest Income Recognized
Commercial & Industrial				
Death Care Management	$9	$ —	$—	$ —
Healthcare	5,777	60	3,388	72
Independent Pharmacies	1,927	51	2,524	38
Registered Investment Advisors	588	13	—	—
Veterinary Industry	2,715	29	3,482	13
Total	11,016	153	9,394	123
Commercial Real Estate				
Death Care Management	1,811	5	1,461	—
Healthcare	1,013	27	2,372	—
Independent Pharmacies	551	2	—	—
Veterinary Industry	12,266	249	11,357	132
Total	15,641	283	15,190	132
Commercial Land				
Agriculture	355	—	—	—
Total	355	—	—	—
Total	$27,012	$ 436	$24,584	$ 255

25

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

The following table present the types of TDRs that were made during the three and nine months ended September 30, 2016 and 2015:

	Three months ended September 30, 2016 All Restructurings			Three months ended September 30, 2015 All Restructurings		
	Number of Loans	Pre-modification Recorded Investment	Post-modification Recorded Investment	Number of Loans	Pre-modification Recorded Investment	Post-modification Recorded Investment
Extended Amortization						
Commercial & Industrial						
Independent Pharmacies	—	$ —	$ —	2	$ 322	$ 313
Total Extended Amortization	—	—	—	2	322	313
Payment Deferral						
Commercial & Industrial						
Healthcare	1	440	440	—	—	—
Total Payment Deferral	1	440	440	—	—	—
Total	1	$ 440	$ 440	2	$ 322	$ 313

	Nine months ended September 30, 2016 All Restructurings			Nine months ended September 30, 2015 All Restructurings		
	Number of Loans	Pre-modification Recorded Investment	Post-modification Recorded Investment	Number of Loans	Pre-modification Recorded Investment	Post-modification Recorded Investment
Interest Only						
Commercial & Industrial						
Healthcare	—	$ —	$ —	3	$ 1,093	$ 1,093
Commercial Real Estate						
Healthcare	—	—	—	1	95	95
Total Interest Only	—	—	—	4	1,188	1,188
Extended Amortization						
Commercial & Industrial						
Independent Pharmacies	—	—	—	2	322	313
Total Extended Amortization	—	—	—	2	322	313
Payment Deferral						
Commercial & Industrial						
Healthcare	1	440	440	—	—	—
Veterinary Industry	1	420	420	—	—	—
Total Payment Deferral	2	860	860	—	—	—
Total	2	$ 860	$ 860	6	$ 1,510	$ 1,501

Concessions made to improve a loan's performance have varying degrees of success. No TDRs that were modified within the twelve months ended September 30, 2016 subsequently defaulted during the three months ended September 30, 2016. During the nine months ended September 30, 2016, one TDR that was modified within the twelve months ended September 30, 2016 subsequently defaulted. This TDR was a commercial and industrial veterinary loan that was previously modified for payment deferral. The recorded investment for this TDR at September 30, 2016 was $311 thousand.

No TDRs that were modified within the twelve months ended September 30, 2015 subsequently defaulted during the three and nine months ended September 30, 2015.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Note 6. Servicing Assets

Loans serviced for others are not included in the accompanying balance sheet. The unpaid principal balances of loans serviced for others were $2.24 billion and $1.94 billion at September 30, 2016 and December 31, 2015, respectively.

The following summarizes the activity pertaining to servicing rights:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Balance at beginning of period	$48,454	$39,983	$44,230	$34,999
Additions, net	4,964	3,613	11,923	10,322
Fair value changes:				
Due to changes in valuation inputs or assumptions	(1,452)	(1,320)	$(821)	$(682)
Decay due to increases in principal paydowns or runoff	(2,237)	(1,686)	$(5,603)	$(4,049)
Balance at end of period	$49,729	$40,590	$49,729	$40,590

The fair value of servicing rights was determined using discount rates ranging from 8.1% to 14.1% on September 30, 2016 and 9.2% to 13.5% on September 30, 2015. The fair value of servicing rights was determined using prepayment speeds ranging from 2.9% to 9.8% on September 30, 2016 and 4.1% to 9.9% on September 30, 2015, depending on the stratification of the specific right. Changes to fair value are reported in loan servicing asset revaluation within the consolidated statements of income.

The fair value of servicing rights is highly sensitive to changes in underlying assumptions. Changes in prepayment speed assumptions have the most significant impact on the fair value of servicing rights. Generally, as interest rates rise on variable rate loans, loan prepayments increase due to an increase in refinance activity, which results in a decrease in the fair value of servicing assets. Measurement of fair value is limited to the conditions existing and the assumptions used as of a particular point in time, and those assumptions may not be appropriate if they are applied at a different time.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Note 7. Borrowings
Total outstanding long term borrowings consisted of the following:

	September 30, 2016	December 31, 2015
Long term borrowings		
On September 11, 2014, the Company financed the construction of an additional building located on the Company's Tiburon Drive main campus with a $24 million construction line of credit with an unaffiliated commercial bank, secured by both properties at its Tiburon Drive main facility location. Payments are interest only through September 11, 2016 at a fixed rate of 3.95% for a term of 84 months. Monthly principal and interest payments beginning in October 2016 will be $146 thousand with all principal and accrued interest due on September 11, 2021. The terms of this loan require the Company to maintain minimum capital, liquidity and Texas ratios. The construction line is fully disbursed and there was no remaining available credit on this construction line at September 30, 2016.	$ 23,995	$ 24,000
On September 18, 2014, the Company entered into a note payable revolving line of credit of $8.1 million with an unaffiliated commercial bank, with the first advance of $5 million on December 14, 2014. The note is unsecured and accrues interest at LIBOR plus 3.50% for a term of 36 months. Payments are interest only with all principal and accrued interest due on September 18, 2017. This line of credit was paid in full on July 30, 2015 and there is $8.1 million of available credit remaining at September 30, 2016.	—	—
On February 23, 2015, the Company transferred two related party loans to an unaffiliated commercial bank in exchange for $4.7 million. The exchange price equated to the unpaid principal balance plus accrued but uncollected interest at the time of transfer. The terms of the transfer agreement with the unaffiliated commercial bank identified the transaction as a secured borrowing for accounting purposes. Interest accrues at prime plus 1% with monthly principal and interest payments over a term of 60 months. The interest rate at September 30, 2016 is 4.50%. The maturity date is October 5, 2019. The pledged collateral is classified in other assets with a fair value of $4.1 million at September 30, 2016. Underlying loans carry a risk grade of 3 and are current with no delinquencies. The terms of this loan require the Company to maintain minimum capital, liquidity and Texas ratios.	4,079	4,375
Total long term borrowings	$ 28,074	$ 28,375

The Company may purchase federal funds though secured and unsecured federal funds lines of credit with various correspondent banks, which totaled $26.5 million as of September 30, 2016 and December 31, 2015. These lines are intended for short-term borrowings and are subject to restrictions limiting the frequency and terms of advances. These lines of credit are payable on demand and bear interest based upon the daily federal funds rate. The Company had no outstanding balances on the lines of credit as of September 30, 2016 and December 31, 2015.

The Company has entered into a repurchase agreement with a third party for $5 million as of September 30, 2016 and December 31, 2015. At the time the Company enters into a transaction with the third party, the Company must transfer securities or other assets against the funds received. The terms of the agreement are set at market conditions at the time the Company enters into such transaction. The Company had no outstanding balance on the repurchase agreement as of September 30, 2016 and December 31, 2015.

The Company may borrow funds through the Federal Reserve Bank's discount window. These borrowings are secured by a blanket floating lien on qualifying loans with a balance of $255.8 million and $192.2 million as of September 30, 2016 and December 31, 2015, respectively. At September 30, 2016 and December 31, 2015, the Company had approximately $133.5 million and $86.7 million, respectively, in borrowing capacity available under these arrangements with no outstanding balance as of September 30, 2016 and December 31, 2015.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Note 8. 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.
Financial Instruments Measured at Fair Value
The following sections provide a description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the fair value hierarchy:
Investment Securities: Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities would include highly liquid government bonds, mortgage products and exchange traded equities. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics, discounted cash flow or at net asset value per share. Level 2 securities would include US government agency securities, mortgage-backed securities, obligations of states and political subdivisions and certain corporate, asset backed mutual fund and other securities. In certain cases where there is limited activity or less transparency around inputs to the valuation, securities are classified within Level 3 of the valuation hierarchy.
Impaired Loans: Impairment of a loan is based on the fair value of the collateral of the loan for collateral-dependent loans. 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. For non-collateral dependent loans, impairment is determined by the present value of expected future cash flows. Impaired loans classified as Level 3 are based on management's judgment and estimation.
Servicing Assets: Servicing rights do not trade in an active, open market with readily observable prices. While sales of servicing rights do occur, the precise terms and conditions typically are not readily available. Accordingly, the Company estimates the fair value of servicing rights using discounted cash flow models incorporating numerous assumptions from the perspective of a market participant including servicing income, servicing costs, market discount rates and prepayment speeds. Due to the nature of the valuation inputs, servicing rights are classified within Level 3 of the valuation hierarchy.
Foreclosed Assets: Foreclosed real estate is adjusted to fair value less selling costs upon transfer of the loans to foreclosed real estate. Subsequently, foreclosed real estate is carried at the lower of carrying value or fair value less selling costs. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. Given the lack of observable market prices for identical properties and market discounts applied to appraised values, the Company generally classifies foreclosed assets as nonrecurring Level 3.
Recurring Fair Value
The tables below present the recorded amount of assets and liabilities measured at fair value on a recurring basis.

September 30, 2016	Total	Level 1	Level 2	Level 3
Investment securities available-for-sale				
US government agencies	$20,861	$ —	$20,861	$—
Residential mortgage-backed securities	47,451	—	47,451	—
Mutual fund	2,022	—	2,022	—
Servicing assets[1]	49,729	—	—	49,729

Total assets at fair value	$120,063	$ —	$70,334	$49,729

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

December 31, 2015	Total	Level 1	Level 2	Level 3
Investment securities available-for-sale				
US government agencies	$22,068	$ —	$22,068	$—
Residential mortgage-backed securities	29,758	—	29,758	—
Mutual fund	1,936	—	1,936	—
Servicing assets[1]	44,230	—	—	44,230
Total assets at fair value	$97,992	$ —	$53,762	$44,230

1 See Note 6 for a rollforward of recurring Level 3 fair values for servicing assets.

Non-recurring Fair Value

The tables below present the recorded amount of assets and liabilities measured at fair value on a non-recurring basis.

September 30, 2016	Total	Level 1	Level 2	Level 3
Impaired loans	$18,878	$ —	$ —	$18,878
Foreclosed assets	2,235	—	—	2,235
Total assets at fair value	$21,113	$ —	$ —	$21,113

December 31, 2015	Total	Level 1	Level 2	Level 3
Impaired loans	$17,084	$ —	$ —	$17,084
Foreclosed assets	2,666	—	—	2,666
Total assets at fair value	$19,750	$ —	$ —	$19,750

Level 3 Analysis

For Level 3 assets and liabilities measured at fair value on a recurring or non-recurring basis as of September 30, 2016 and December 31, 2015 the significant unobservable inputs used in the fair value measurements were as follows:

September 30, 2016

Level 3 Assets with Significant Unobservable Inputs	Fair Value	Valuation Technique	Significant Unobservable Inputs	Range
Impaired Loans	$ 18,878	Discounted appraisals Discounted expected cash flows	Appraisal adjustments (1) Interest rate & repayment term	10% to 50% Weighted average discount rate 5.34%
Foreclosed Assets	$ 2,235	Discounted appraisals	Appraisal adjustments (1)	10% to 35%

December 31, 2015

Level 3 Assets with Significant Unobservable Inputs	Fair Value	Valuation Technique	Significant Unobservable Inputs	Range
Impaired Loans	$ 17,084	Discounted appraisals Discounted expected cash flows	Appraisal adjustments (1) Interest rate & repayment term	10% to 20% Weighted average discount rate 5.57%
Foreclosed Assets	$ 2,666	Discounted appraisals	Appraisal adjustments (1)	10% to 20%

(1) Appraisals may be adjusted by management for customized discounting criteria, estimated sales costs, and proprietary qualitative adjustments.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Estimated Fair Value of Other Financial Instruments

GAAP also requires disclosure of fair value information about financial instruments carried at book value on the balance sheet. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instruments. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company.

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments not measured at fair value on the balance sheet:

Cash and due from banks: The carrying amounts reported in the balance sheet for cash and due from banks approximate their fair values.

Certificates of deposit with other banks: The fair value of certificates of deposit with other banks is estimated based on discounting cash flows using the rates currently offered for instruments of similar remaining maturities.

Loans held for sale: The fair values of loans held for sale are based on quoted market prices, where available, and determined by discounting estimated cash flows using interest rates approximating the Company’s current origination rates for similar loans adjusted to reflect the inherent credit risk.

Loans held for investment: For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying amounts. The fair values for other loans are estimated using discounted cash flow analysis, based on interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Loan fair value estimates include judgments regarding future expected loss experience and risk characteristics. Fair values for impaired loans are estimated using discounted cash flow analysis or underlying collateral values, where applicable.

Accrued interest: The carrying amounts of accrued interest approximate fair value.

Deposits: The fair values disclosed for demand deposits (e.g., interest and non-interest checking, passbook savings, and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amounts). The carrying amounts of variable-rate, fixed-term money market accounts and certificates of deposit approximate their fair values at the reporting date. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Short and long term borrowings: The fair values of the Company’s short term borrowings approximate fair value while long term borrowings are estimated using discounted cash flow analyses based on the Company’s current incremental debt rates for similar types of debt arrangements.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

The carrying amounts and estimated fair values of the Company's financial instruments are as follows:

September 30, 2016	Carrying Amount	Quoted Price In Active Markets for Identical Assets /Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Financial assets					
Cash and due from banks	$355,485	$ 355,485	$ —	$ —	$355,485
Certificates of deposit with other banks	7,500	7,508	—	—	7,508
Investment securities, available-for-sale	70,334	—	70,334	—	70,334
Loans held for sale	345,277	—	—	379,416	379,416
Loans, net of allowance for loan losses	751,799	—	—	746,912	746,912
Servicing assets	49,729	—	—	49,729	49,729
Accrued interest receivable	6,761	6,761	—	—	6,761
Financial liabilities					
Deposits	1,403,017	—	1,409,993	—	1,409,993
Accrued interest payable	193	193	—	—	193
Long term borrowings	28,074	—	—	30,818	30,818

December 31, 2015	Carrying Amount	Quoted Price In Active Markets for Identical Assets /Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Financial assets					
Cash and due from banks	$102,607	$ 102,607	$ —	$ —	$102,607
Certificates of deposit with other banks	10,250	10,176	—	—	10,176
Investment securities, available-for-sale	53,762	—	53,762	—	53,762
Loans held for sale	480,619	—	—	497,868	497,868
Loans, net of allowance for loan losses	272,554	—	—	268,816	268,816
Servicing assets	44,230	—	—	44,230	44,230
Accrued interest receivable	5,556	5,556	—	—	5,556
Financial liabilities					
Deposits	804,788	—	792,820	—	792,820
Accrued interest payable	211	211	—	—	211
Long term borrowings	28,375	—	—	30,523	30,523

Loans held for sale that are carried at the lower of cost or estimated fair value as of September 30, 2016 significantly declined compared to December 31, 2015 because $318.8 million of these loans were reclassified to loans held for investment.

Note 9. Commitments and Contingencies

Litigation

In the normal course of business the Company is involved in various legal proceedings. Management believes that the outcome of such proceedings will not materially affect the financial position, results of operations or cash flows of the Company.

Financial Instruments with Off-balance-sheet Risk

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. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, credit risk in excess of the amount recognized in the balance sheet.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

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 and standby letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as for on-balance-sheet instruments. A summary of the Company's commitments is as follows:

	September 30, 2016	December 31, 2015
Commitments to extend credit	$1,446,813	$737,572
Standby letters of credit	343	—
Plexus Capital - Fund II Investment Commitment	100	100
Plexus Capital - Fund III Investment Commitment	225	300
Plexus Capital - Fund IV Investment Commitment	2,313	—
Five Points Mezzanine Fund III Commitment	1,464	1,500
Total unfunded off-balance-sheet credit risk	$1,451,258	$739,472

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments 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 party. Collateral held varies, but may include accounts receivable, inventory, property and equipment, residential real estate and income-producing commercial properties. In 2012, the Company began issuing commitment letters after approval of the loan by the Credit Department. Commitment letters generally expire ninety days after issuance.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Collateral held varies as specified above and is required in instances which the Company deems necessary.

Concentrations of Credit Risk

Although the Company is not subject to any geographic concentrations, a substantial amount of the Company's loans and commitments to extend credit have been granted to customers in the agriculture, healthcare and veterinary verticals. The concentrations of credit by type of loan are set forth in Note 5. The distribution of commitments to extend credit approximates the distribution of loans outstanding. The Company does not have a significant number of credits to any single borrower or group of related borrowers whereby their retained unguaranteed exposure exceeds $2.0 million, except for ten relationships that have a retained unguaranteed exposure of $35.9 million of which $31.6 million of the unguaranteed exposure has been disbursed.

The Company from time-to-time may have cash and cash equivalents on deposit with financial institutions that exceed federally-insured limits.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Note 10. Stock Plans
On March 20, 2015, the Company adopted the 2015 Omnibus Stock Incentive Plan which replaced the previously existing Amended Incentive Stock Option Plan and Nonstatutory Stock Option Plan. Subsequently on May 24, 2016, the 2015 Omnibus Stock Incentive Plan was amended to authorize awards covering a maximum of 7,000,000 common voting shares and has an expiration date of March 20, 2025. Options or restricted shares granted under the Amended and Restated 2015 Omnibus Stock Incentive Plan (the "Plan") expire no more than 10 years from the date of grant. Exercise prices under the Plan are set by the Board of Directors at the date of grant, but shall not be less than 100% of fair market value of the related stock at the date of the grant. Options or restricted shares vest over a minimum of three years from the date of the grant.
Stock Options
Compensation cost relating to share-based payment transactions are recognized in the financial statements with measurement based upon the fair value of the equity or liability instruments issued. For the three months ended September 30, 2016 and 2015, the Company recognized $580 thousand and $431 thousand in compensation expense for stock options, respectively. For the nine months ended September 30, 2016 and 2015, the Company recognized $1.8 million and $726 thousand in compensation expense for stock options, respectively.
Stock option activity under the Plan during the nine month periods ended September 30, 2016 and 2015 is summarized below.

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at December 31, 2015	3,546,992	$ 11.17		
Exercised	25,406	5.79		
Forfeited	166,483	9.01		
Granted	169,987	14.02		
Outstanding at September 30, 2016	3,525,090	$ 11.44	8.30 years	$14,212,513
Exercisable at September 30, 2016	478,141	$ 9.22	7.84 years	$2,887,741

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at December 31, 2014	1,737,570	$ 5.51		
Exercised	47,570	4.52		
Forfeited	192,671	8.38		
Granted	1,829,748	15.52		
Outstanding at September 30, 2015	3,327,077	$ 10.86	9.16 years	$29,197,309
Exercisable at September 30, 2015	158,950	$ 4.65	8.05 years	$2,382,744

The following is a summary of non-vested stock option activity for the Company for the nine months ended September 30, 2016 and 2015.

	Shares	Weighted Average Grant Date Fair Value

Non-vested at December 31, 2015	3,393,441	$	4.56
Granted	169,987		6.58
Vested	349,996		4.22
Forfeited	166,483		3.13
Non-vested at September 30, 2016	3,046,949	$	4.79

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

	Shares	Weighted Average Grant Date Fair Value
Non-vested at December 31, 2014	1,704,230	$ 1.18
Granted	1,829,748	6.79
Vested	173,180	0.97
Forfeited	192,671	2.63
Non-vested at September 30, 2015	3,168,127	$ 4.35

The total intrinsic value of options exercised at September 30, 2016 and 2015 was $223 thousand and $392 thousand, respectively.

At September 30, 2016, unrecognized compensation costs relating to stock options amounted to $13.1 million which will be recognized over a weighted average period of 3.51 years.

The weighted average fair value of each stock option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The expected volatility is based on historical volatility. The risk-free interest rates for periods within the contractual life of the awards are based on the U.S. Treasury yield curve in effect at the time of the grant. The expected life is based on historical exercise experience. The dividend yield assumption is based on the Company's history and expectation of dividend payouts. Weighted average assumptions used for options granted during 2016 were as follows: risk free rate of 1.56%, dividend yield of 0.05%, volatility of 44.20% and average life of 7 years.

Restricted Stock

Restricted stock awards are authorized in the form of restricted stock awards or units ("RSU"s) and restricted stock awards or units with a market price condition ("Market RSU"s).

RSUs have a restriction based on the passage of time and may also have a restriction based on a non-market-related performance criteria. The fair value of the RSUs is based on the closing price on the date of the grant.

Market RSUs also have a restriction based on the passage of time and non-market-related performance criteria, but also have a restriction based on market price criteria related to the Company's share price closing at or above $34.00 per share for at least twenty (20) consecutive trading days at any time prior to March 23, 2023. The amount of Market RSUs earned will not exceed 100% of the Market RSUs awarded. The fair value of the Market RSUs and the implied service period is calculated using the Monte Carlo Simulation method.

RSU stock activity under the Plan during the first nine months of 2016 is summarized below.

	Shares	Weighted Average Grant Date Fair Value
Non-vested at December 31, 2015	64,271	$ 16.17
Granted	589,566	15.58
Vested	16,745	15.94
Forfeited	1,374	12.55
Non-vested at September 30, 2016	635,718	$ 15.64

For the three months ended September 30, 2016 and 2015, the Company recognized $3.1 million and $67 thousand in compensation expense for RSUs, respectively. For the nine months ended September 30, 2016 and 2015, the Company recognized $5.3 million and $83 thousand in compensation expense for RSUs, respectively.

At September 30, 2016, unrecognized compensation costs relating to RSUs amounted to $4.7 million which will be recognized over a weighted average period of 1.75 years.

Table of Contents

Live Oak Bancshares, Inc.
Notes to Unaudited Consolidated Financial Statements

Market RSU stock activity under the Plan during the first nine months of 2016 is summarized below.

	Shares	Weighted Average Grant Date Fair Value
Non-vested at December 31, 2015	—	$ —
Granted	850,000	7.06
Vested	—	—
Forfeited	—	—
Non-vested at September 30, 2016	850,000	$ 7.06

The compensation expense for Market RSUs is measured based on their grant date fair value as calculated using the Monte Carlo Simulation and is recognized on a straight-line basis over the average vesting period. Related to the 850,000 Market RSUs granted during the nine months ended September 30, 2016, the Monte Carlo Simulation used 100,000 simulation paths to assess the expected date of achieving the market price criteria. The share price simulation was based on the Cox, Ross & Rubinstein option pricing methodology for a period of 6.83 years. The implied term of the restricted stock was 4.2 years. The Monte Carlo Simulation used various assumptions that include a risk free rate of return of 1.68%, expected volatility of 30.00% and a dividend yield of 0.25%.

For the three months ended September 30, 2016, the Company recognized $346 thousand in compensation expense for Market RSUs. For the nine months ended September 30, 2016, the Company recognized $577 thousand in compensation expense for Market RSUs. All of the Company's Market RSUs had an effective grant date of May 24, 2016.

At September 30, 2016, unrecognized compensation costs relating to Market RSUs amounted to $5.4 million which will be recognized over a weighted average period of 3.92 years.

Table of Contents

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following presents management’s discussion and analysis of the financial condition and results of operations of Live Oak Bancshares, Inc. (the “Company” or “LOB”). This discussion should be read in conjunction with the financial statements and related notes included elsewhere in this quarterly report on Form 10-Q and with the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2015 (the "2015 Annual Report"). Results of operations for the periods included in this review are not necessarily indicative of results to be obtained during any future period.

Important Note Regarding Forward-Looking Statements

This quarterly report on Form 10-Q contains statements that management believes are forward-looking statements, within the meaning of the Private Securities Litigation Reform Act of 1995. These statements generally relate to the Company’s financial condition, results of operations, plans, objectives, future performance or business. They usually can be identified by the use of forward-looking terminology, such as “believes,” “expects,” or “are expected to,” “plans,” “projects,” “goals,” “estimates,” “will,” “may,” “should,” “could,” “would,” “continues,” “intends to,” “outlook” or “anticipate of these and similar words, or by discussions of strategies that involve risks and uncertainties. You should not place undue reliance on these statements, as they are subject to risks and uncertainties, including but not limited to, those described in this quarterly report on Form 10-Q. When considering these forward-looking statements, you should keep in mind these risks and uncertainties, as well as any cautionary statements management may make. Moreover, you should treat these statements as speaking only as of the date they are made and based only on information actually known to the Company at the time. Management undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise. Forward-looking statements contained in this quarterly report on Form 10-Q are based on current expectations, estimates and projections about the Company’s business, management’s beliefs and assumptions made by management. These statements are not guarantees of the Company’s future performance and involve certain risks, uncertainties and assumptions, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in the forward-looking statements. These risks, uncertainties and assumptions include, without limitation:

- deterioration in the financial condition of borrowers resulting in significant increases in the Company’s loan losses and provisions for those losses and other adverse impacts to results of operations and financial condition;
- changes in Small Business Administration ("SBA") rules, regulations and loan products, including specifically the Section 7(a) program, changes in SBA standard operating procedures or changes to the Bank's status as an SBA Preferred Lender;
- changes in rules, regulations or procedures for other government loan programs, including those of the United States Department of Agriculture;
- changes in interest rates that affect the level and composition of deposits, loan demand and the values of loan collateral, securities, and interest sensitive assets and liabilities;
- the failure of assumptions underlying the establishment of reserves for possible loan losses;
- changes in loan underwriting, credit review or loss reserve policies associated with economic conditions, examination conclusions, or regulatory developments;
- a reduction in or the termination of the Company’s ability to use the technology-based platform that is critical to the success of the Company’s business model, including a failure in or a breach of the Company’s operational or security systems or those of its third party service providers;
- changes in financial market conditions, either internationally, nationally or locally in areas in which the Company conducts operations, including reductions in rates of business formation and growth, demand for the Company’s products and services, commercial and residential real estate development and prices, premiums paid in the secondary market for the sale of loans, and valuation of servicing rights;
- changes in accounting principles, policies, and guidelines applicable to bank holding companies and banking;
- fluctuations in markets for equity, fixed-income, commercial paper and other securities, which could affect availability, market liquidity levels, and pricing;
- the effects of competition from other commercial banks, non-bank lenders, consumer finance companies, credit unions, securities brokerage firms, insurance companies, money market and mutual funds, and other financial

institutions operating in the Company’s market area and elsewhere, including institutions operating regionally, nationally and internationally, together with such competitors offering banking products and services by mail, telephone and the Internet;

- the Company's ability to attract and retain key personnel;

Table of Contents

- governmental monetary and fiscal policies as well as other legislative and regulatory changes, including with respect to SBA lending programs;
- changes in political and economic conditions, including continuing political and economic effects of the global economic downturn and other major developments;
- the impact of heightened regulatory scrutiny of financial products and services, primarily led by the Consumer Financial Protection Bureau;
- the Company's ability to comply with any requirements imposed on it by regulators, and the potential negative consequences that may result;
- operational, compliance and other factors, including conditions in local areas in which the Company conducts business such as inclement weather or a reduction in the availability of services or products for which loan proceeds will be used, that could prevent or delay closing and funding loans before they can be sold in the secondary market;
- the effect of any mergers, acquisitions or other transactions, to which the Company or the Bank may from time to time be a party, including management's ability to successfully integrate any businesses acquired;
- other risk factors listed from time to time in reports that the Company files with the SEC, including in the Company's 2015 Annual Report; and
- the success at managing the risks involved in the foregoing.

Except as otherwise disclosed, forward-looking statements do not reflect: (i) the effect of any acquisitions, divestitures or similar transactions that have not been previously disclosed; (ii) any changes in laws, regulations or regulatory interpretations; or (iii) any change in current dividend or repurchase strategies, in each case after the date as of which such statements are made. All forward-looking statements speak only as of the date on which such statements are made, and the Company undertakes no obligation to update any statement, to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events.

Amounts in all tables in Management's Discussion and Analysis of Financial Condition and Results of Operations have been presented in thousands, except percentage, time period, stock option, share and per share data or where otherwise indicated.

Nature of Operations

LOB is a bank holding company headquartered in Wilmington, North Carolina incorporated under the laws of North Carolina in December 2008. The Company conducts business operations primarily through its commercial bank subsidiary, Live Oak Banking Company (the "Bank"). The Bank was established in May 2008 as a North Carolina-chartered commercial bank. The Bank specializes in providing lending services to small businesses nationwide in targeted industries. The Bank identifies and grows within selected industry sectors, or verticals, by leveraging expertise within those industries. A significant portion of the loans originated by the Bank are guaranteed by the SBA under the 7(a) program. In 2010, the Bank formed Live Oak Number One, Inc., a wholly-owned subsidiary, to hold properties foreclosed on by the Bank.

Effective July 29, 2016, the Company elected to become a "financial holding company" within the meaning of the Bank Holding Company Act. A financial holding company, and the nonbank companies under its control, are permitted to engage in activities considered financial in nature or incidental to financial activities. For the Company to become and remain eligible for financial holding company status, it and the Bank must meet certain criteria, including capital, management and Community Reinvestment Act ("CRA") requirements. The failure to meet such criteria could, depending on which requirements were not met, result in the Company facing restrictions on new financial activities or acquisitions or being required to discontinue existing activities that are not otherwise permissible for bank holding companies.

In addition to the Bank, the Company owns Live Oak Grove, LLC, opened in September 2015 for the purpose of providing Company employees and business visitors an on-site restaurant location, Government Loan Solutions, Inc. ("GLS"), a management and technology consulting firm that specializes in the settlement, accounting, and securitization processes for government guaranteed loans, including loans originated under the SBA 7(a) loan program and USDA-guaranteed loans, and 504 Fund Advisors, LLC ("504FA"), which was formed to serve as the investment advisor to The 504 Fund, a closed-end mutual fund organized to invest in SBA section 504 loans.

In August 2016, the Company formed Live Oak Ventures, Inc. for the purpose of investing in businesses that align with the Company's strategic initiative to be a leader in online banking for small businesses.

Table of Contents

The Company generates revenue primarily from the sale of SBA and USDA-guaranteed loans and net interest income. Income from the sale of loans is comprised of loan servicing revenue and related revaluation of the servicing rights asset and net gains on sales of loans. Offsetting these revenues are the cost of funding sources, provision for loan losses, any costs related to foreclosed assets and other operating costs such as salaries and employee benefits, travel, professional services, advertising and marketing and tax expense.

On July 23, 2015 the Company closed on its initial public offering.

Business Outlook

Below is a discussion of management's current expectations regarding company performance over the near-term based on market conditions, the regulatory environment and business strategies as of the time the Company filed this Report. Actual outcomes and results may differ materially from what is expressed or forecasted in these forward-looking statements. See "Important Note Regarding Forward-Looking Statements" in this Report for more information on forward-looking statements.

The Company expects to originate approximately $1.50 billion in loans in 2016.

The Company expects $3.4 million in additional stock based compensation expense during the fourth quarter of 2016 related to restricted stock awards for key employee retention with an effective grant date of May 24, 2016, as discussed in Note 10 of the quarterly report on Form 10-Q for the quarterly period ended March 31, 2016. The Company anticipates that subsequent expense after 2016 related to these awards will be approximately $350 thousand per quarter through the third quarter of 2020.

Results of Operations

Performance Summary

Three months ended September 30, 2016 compared with three months ended September 30, 2015

For the three months ended September 30, 2016, the Company reported net income of $3.5 million, or $0.10 per diluted share, as compared to $2.9 million, or $0.09 per diluted share, for the three months ended September 30, 2015. This increase in net income is primarily due to the following items:

- Increased net interest income of $5.0 million, or 75.4%, predominately driven by significant growth in total loans held for sale and held for investment portfolios combined with a higher net interest margin, driven largely by higher loan rates in the third quarter of 2016;
- Increased loan servicing revenue of $1.6 million, or 39.0%, as a result of continued growth in loan sales; and
- Increased net gains on sales of loans of $6.4 million, or 41.6%, due to a much higher volume of contracted loan sales, partly mitigated by lower average sale premiums.

Partially offsetting the above factors that contributed to increased levels of net income was increased provision for loan losses of $2.6 million combined with a $7.5 million increase in salaries and employee benefits. Salaries and employee benefits for the third quarter of 2016 included $3.4 million in stock based compensation expense related to restricted stock awards with an effective grant date of May 24, 2016 for key employee retention, as discussed in Note 10 of this quarterly report.

Nine months ended September 30, 2016 compared with nine months ended September 30, 2015

For the nine months ended September 30, 2016, the Company reported net income of $8.3 million, or $0.24 per diluted share, as compared to $14.9 million, or $0.48 per diluted share, for the nine months ended September 30, 2015. This decrease in net income is primarily attributable to the following items:

- Increased provision for loan losses of $6.4 million driven by the above-mentioned growth in loans held for investment which included the second quarter of 2016 transfer of $318.8 million in unguaranteed loans from being classified as held for sale to held for investment. The higher provision also reflected the increase of $336 thousand in net charge-offs during the first nine months of 2016.
- Decreased noninterest income from a one-time gain of $3.8 million in the first quarter of 2015 related to the sale of an investment in nCino, Inc., a former subsidiary of the Company ("nCino") combined with a higher negative loan servicing revaluation adjustment of $817 thousand.

39

Table of Contents

- Increased noninterest expense, predominantly in higher salaries and employee benefits of $18.3 million, or 66.1%, combined with increases of $1.4 million, or 72.2%, and $1.5 million, or 61.8%, in occupancy and data processing expense, respectively. The higher expense level was largely attributable to increased investments in human capital and infrastructure to support growing loan production from new and existing verticals as well as development of a new small-loan and deposit platform. Salaries and employee benefits for the first nine months of 2016 included $5.6 million in stock based compensation expense related to restricted stock awards with an effective grant date of May 24, 2016 for key employee retention, as discussed in Note 10 of this quarterly report.

Partially offsetting the above factors that contributed to decreased levels of net income were increases in net interest income of $13.1 million, or 76.7%, loan servicing revenue of $4.0 million, or 34.7%, and net gains on sale of loans of $6.2 million, or 13.3%.

Net Interest Income and Margin

Net interest income represents the difference between the income that the Company earns on interest-earning assets and the cost of interest-bearing liabilities. The Company's net interest income depends upon the volume of interest-earning assets and interest-bearing liabilities and the interest rates that the Company earns or pays on them. Net interest income is affected by changes in the amount and mix of interest-earning assets and interest-bearing liabilities, referred to as "volume changes." It is also affected by changes in yields earned on interest-earning assets and rates paid on interest-bearing deposits and other borrowed funds, referred to as "rate changes." Without a branch network, the Bank generates deposits over the Internet and in the community in which it is headquartered. Due to the nature of a branchless bank and the relatively low overhead required for deposit gathering, the rates that the Bank offers are generally above the industry average.

Three months ended September 30, 2016 compared with three months ended September 30, 2015

For the three months ended September 30, 2016, net interest income increased $5.0 million, or 75.4%, to $11.6 million compared to the three months ended September 30, 2015. This increase was due to growth in average interest earning assets along with higher yields on these assets which outpaced the growth and change in the cost of interest bearing liabilities. Average interest earning assets increased by $545.1 million, or 64.7%, to $1.39 billion for the three months ended September 30, 2016, compared to $842.9 million for the three months ended September 30, 2015, while the yield on average interest earning assets increased by twenty basis points to 4.45%. The cost of funds on interest bearing liabilities for the three months ended September 30, 2016 increased slightly by one basis point to 1.23%, and the average balance in interest bearing liabilities increased by $490.9 million, or 63.2%, over the same period. As indicated in the rate/volume table below, the slight increase in the cost of funds was outpaced by the positive effects of the increased volume of interest earning assets along with higher yields, resulting in increased interest income of $6.5 million and increased interest expense of $1.5 million for the three months ended September 30, 2016 compared to the third quarter of 2015. For the three months ended September 30, 2016 compared to the three months ended September 30, 2015, net interest margin increased from 3.12% to 3.32% due to the aforementioned effects.

Nine months ended September 30, 2016 compared with nine months ended September 30, 2015

For the nine months ended September 30, 2016, net interest income increased $13.1 million, or 76.7%, to $30.3 million compared to the nine months ended September 30, 2015. This increase was also due to increased yields and growth in average interest earning assets. Average interest earning assets increased by $444.6 million, or 58.8%, to $1.20 billion for the nine months ended September 30, 2016 compared to $756.5 million for the nine months ended September 30, 2015, while the yield on average interest earning assets increased by thirty basis points to 4.48%. The cost of funds on interest bearing liabilities for the nine months ended September 30, 2016 remained stable at 1.23%, and the average balance in interest bearing liabilities increased by $375.3 million, or 52.5%, during the same period. As indicated in the rate/volume table below, the stable cost of funds was outpaced by the effects of the increased yields and volume of interest earning assets, resulting in increased interest income of $16.7 million and increased interest expense of $3.5 million for the nine months ended September 30, 2016. For the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015, net interest margin increased from 3.03% to 3.36% due to the aforementioned effects.

Table of Contents

Average Balances and Yields. The following table presents information regarding average balances for assets and liabilities, the total dollar amounts of interest income and dividends from average interest-earning assets, the total dollar amount of interest expense on average interest-bearing liabilities, and the resulting average yields and costs. The yields and costs for the periods indicated are derived by dividing the income or expense by the average balances for assets or liabilities, respectively, for the periods presented and annualizing that result. Loan fees are included in interest income on loans.

	Three months ended September 30,					
	2016			2015		
	Average Balance	Interest	Average Yield/Rate	Average Balance	Interest	Average Yield/Rate
Interest earning assets:						
Interest earning balances in other banks	$231,238	$264	0.45 %	$110,425	$84	0.30 %
Investment securities	69,869	337	1.91	60,192	211	1.39
Loans held for sale	358,867	4,996	5.52	428,940	5,638	5.21
Loans held for investment (1)	728,041	9,965	5.43	243,346	3,090	5.04
Total interest earning assets	1,388,015	15,562	4.45	842,903	9,023	4.25
Less: allowance for loan losses	(12,188)			(5,202)		
Non-interest earning assets	146,159			142,414		
Total assets	$1,521,986			$980,115		
Interest bearing liabilities:						
Money market accounts	$471,447	$866	0.73 %	$376,495	$684	0.72 %
Certificates of deposit	767,887	2,823	1.46	358,738	1,313	1.45
Total deposits	1,239,334	3,689	1.18	735,233	1,997	1.08
Small business lending fund	—	—	—	6,800	26	1.52
Other borrowings	28,172	242	3.41	34,612	369	4.23
Total interest bearing liabilities	1,267,506	3,931	1.23	776,645	2,392	1.22
Non-interest bearing deposits	20,742			14,086		
Non-interest bearing liabilities	20,807			19,716		
Shareholders' equity	212,914			169,639		
Noncontrolling interest	17			29		
Total liabilities and shareholders' equity	$1,521,986			$980,115		
Net interest income and interest rate spread		$11,631	3.22 %		$6,631	3.03 %
Net interest margin			3.32			3.12
Ratio of average interest-earning assets to average interest-bearing liabilities			109.51 %			108.53 %

(1) Average loan balances include non-accruing loans.

41

Table of Contents

	Nine months ended September 30, 2016 Average Balance	Interest	Average Yield/Rate	2015 Average Balance	Interest	Average Yield/Rate
Interest earning assets:						
Interest earning balances in other banks	$189,944	$650	0.46 %	$90,981	$220	0.32 %
Investment securities	60,057	840	1.86	59,773	587	1.31
Loans held for sale	428,316	17,666	5.49	393,791	15,046	5.11
Loans held for investment(1)	522,757	21,202	5.40	211,906	7,820	4.93
Total interest earning assets	1,201,074	40,358	4.48	756,451	23,673	4.18
Less: allowance for loan losses	(9,463)			(4,943)		
Non-interest earning assets	143,876			117,186		
Total assets	$1,335,487			$868,694		
Interest bearing liabilities:						
Money market accounts	$423,923	$2,384	0.75 %	$342,270	$1,919	0.75 %
Certificates of deposit	637,469	6,992	1.46	326,968	3,355	1.37
Total deposits	1,061,392	9,376	1.18	669,238	5,274	1.05
Small business lending fund	—	—	—	6,800	77	1.51
Other borrowings	28,345	725	3.41	38,393	1,203	4.19
Total interest bearing liabilities	1,089,737	10,101	1.23	714,431	6,554	1.23
Non-interest bearing deposits	19,314			13,659		
Non-interest bearing liabilities	19,444			17,096		
Shareholders’ equity	206,967			123,494		
Noncontrolling interest	25			14		
Total liabilities and shareholders’ equity	$1,335,487			$868,694		
Net interest income and interest rate spread		$30,257	3.25 %		$17,119	2.95 %
Net interest margin			3.36			3.03
Ratio of average interest-earning assets to average interest-bearing liabilities			110.22 %			105.88 %

(1) Average loan balances include non-accruing loans.

Table of Contents

Rate/Volume Analysis. The following table sets forth the effects of changing rates and volumes on net interest income. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate). The total column represents the sum of the prior columns. For purposes of this table, changes attributable to changes in both rate and volume that cannot be segregated have been allocated proportionally based on the changes due to rate and the changes due to volume.

	Three months ended September 30, 2016 vs. 2015			Nine months ended September 30, 2016 vs. 2015		
	Increase (Decrease) Due to			Increase (Decrease) Due to		
	Rate	Volume	Total	Rate	Volume	Total
Interest income:						
Interest earning balances in other banks	$65	$115	$180	$141	$289	$430
Investment securities	86	40	126	250	3	253
Loans held for sale	306	(948)	(642)	1,248	1,372	2,620
Loans held for investment	481	6,394	6,875	1,343	12,039	13,382
Total interest income	938	5,601	6,539	2,982	13,703	16,685
Interest expense:						
Money market accounts	9	173	182	7	458	465
Certificates of deposit	9	1,501	1,510	341	3,296	3,637
Small business lending fund	—	(26)	(26)	—	(77)	(77)
Other borrowings	(65)	(62)	(127)	(192)	(286)	(478)
Total interest expense	(47)	1,586	1,539	156	3,391	3,547
Net interest income	$985	$4,015	$5,000	$2,826	$10,312	$13,138

Provision for Loan Losses. The provision for loan losses represents the amount necessary to be charged against the current period's earnings to maintain the allowance for loan losses at a level that is appropriate in relation to the estimated losses inherent in the loan portfolio. A number of factors are considered in determining the required level of loan loss reserves and the provision required to achieve the appropriate reserve level, including loan growth, credit risk rating trends, nonperforming loan levels, delinquencies, loan portfolio concentrations and economic and market trends.

The provision for loan losses for the third quarter of 2016 was $3.8 million compared to $1.2 million for the same period of 2015. For the nine months ended September 30, 2016, the provision for loan losses was $8.7 million, an increase of $6.4 million compared to $2.3 million in the same period in 2015. The increase in the provision for loan losses for both the quarterly and year-to-date comparisons was principally driven by growth in loans held for investment combined with the effect of higher net charge-offs.

Loans held for investment as of September 30, 2016 increased by $507.4 million compared to September 30, 2015. A significant portion of the increase was the result of the Company transferring $318.8 million in unguaranteed SBA loans from being classified as held for sale to held for investment during the second quarter of 2016. Timing of this transfer was largely influenced by the intent and ability to retain quality credits with higher long term yields. Upon transfer from held for sale classification, loans held for investment become subject to the allowance for loan loss review process. The result of this loan reclassification increased the provision for loan losses by $4.0 million during the second quarter of 2016.

Net charge-offs were $937 thousand, or 0.51% of average quarterly loans held for investment on an annualized basis, for the three months ended September 30, 2016, compared to net charge-offs of $242 thousand, or 0.40%, for the three months ended September 30, 2015. Net charge-offs for the first nine months of 2016 and 2015 totaled $929 thousand and $593 thousand, respectively. Year to date net charge-offs as a percentage of year to date average loans held for investment were 0.18% and 0.28% at September 30, 2016 and 2015, respectively. Net charge-offs are a key element

of historical experience in the Company's estimation of the allowance for loan losses.
In addition, at September 30, 2016, nonperforming loans not guaranteed by the SBA totaled $3.4 million, which was 0.4% of the held-for-investment loan portfolio compared to $2.6 million, or 1.0%, of loans held for investment at September 30, 2015.
Losses inherent in loan relationships are mitigated if a portion of the loan is guaranteed by the SBA. A typical SBA 7(a) loan carries a 75% guarantee, which reduces the risk profile of these loans. The Company believes that its focus on compliance with regulations and guidance from the SBA are key factors to managing this risk.

Table of Contents

Noninterest Income

Noninterest income is principally comprised of net gains from the sale of SBA-guaranteed loans along with loan servicing revenue and revaluation. Revenue from the sale of loans depends upon the volume, maturity structure and rates of underlying loans as well as the pricing and availability of funds in the secondary markets prevailing in the period between completed loan funding and closing of sale. In addition, the loan servicing revaluation is significantly impacted by changes in market rates and other underlying assumptions such as prepayment speeds and default rates. Other less common elements of noninterest income include nonrecurring gains and losses on investments.

The following table shows the components of noninterest income and the dollar and percentage changes for the periods presented.

	Three Months Ended September 30,		Increase (Decrease)	
	2016	2015	Amount	Percent
Noninterest income				
Loan servicing revenue	$5,860	$4,216	$1,644	38.99 %
Loan servicing asset revaluation	(3,421)	(2,650)	(771)	29.09
Net gains on sales of loans	21,833	15,424	6,409	41.55
Gain on sale of securities available-for-sale	1	12	(11)	(91.67)
Construction supervision fee income	502	344	158	45.93
Other noninterest income	657	424	233	54.95
Total noninterest income	$25,432	$17,770	$7,662	43.12 %

	Nine Months Ended September 30,		Increase (Decrease)	
	2016	2015	Amount	Percent
Noninterest income				
Loan servicing revenue	$15,725	$11,678	$4,047	34.65 %
Loan servicing asset revaluation	(5,051)	(4,234)	(817)	19.30
Net gains on sales of loans	52,813	46,604	6,209	13.32
Equity in loss of non-consolidated affiliates	—	(26)	26	100.00
Gain on sale of investment in non-consolidated affiliate	—	3,782	(3,782)	(100.00)
Gain on sale of investment securities available-for-sale	1	12	(11)	(91.67)
Construction supervision fee income	1,799	877	922	105.13
Other noninterest income	1,925	1,267	658	51.93
Total noninterest income	$67,212	$59,960	$7,252	12.09 %

For the three months ended September 30, 2016, noninterest income increased by $7.7 million, or 43.1%, compared to the three months ended September 30, 2015. Increases in the serviced loan portfolio and the volume of loans sold in the secondary market combined to generate $1.6 million of increased servicing revenue and $6.4 million of increased net gains on sale of loans. Offsetting the increase in noninterest income from the same period a year ago was a higher negative loan servicing revaluation adjustment of $771 thousand.

For the nine months ended September 30, 2016, noninterest income increased by $7.3 million, or 12.1%, compared to the nine months ended September 30, 2015. Increases in noninterest income were primarily the result of higher year to date levels in the serviced loan portfolio and the volume of loans sold in the secondary market which generated $4.0 million of increased servicing revenue and $6.2 million of increased net gains on sale of loans. There was also a $922 thousand increase in additional fees earned for monitoring higher levels of multi-advance loans in the first nine months of 2016. Significantly offsetting the overall increase in noninterest income was a $3.8 million one-time gain arising in the first quarter of 2015 related to the sale of the investment in nCino combined with a higher negative loan servicing revaluation adjustment of $817 thousand.

Table of Contents

The following table reflects loan production, sales of guaranteed loans and the aggregate balance in guaranteed loans sold. These components are key drivers of the Company's noninterest income.

	Three months ended September 30,		Three months ended June 30,		Three months ended March 31,	
	2016	2015	2016	2015	2016	2015
Amount of loans originated	$381,050	$302,962	$356,865	$276,822	$284,530	$248,058
SBA-guaranteed portions of loans sold	210,610	147,377	135,555	137,134	155,643	137,047
Outstanding balance of guaranteed loans sold (1)	2,102,468	1,608,197	1,970,908	1,504,115	1,894,428	1,403,968

	Nine months ended September 30,		For years ended December 31,			
	2016	2015	2015	2014	2013	2012
Amount of loans originated	$1,022,445	$827,842	$1,158,640	$848,090	$498,752	$413,763
SBA-guaranteed portions of loans sold	501,808	421,558	640,886	433,912	339,342	276,676
Outstanding balance of guaranteed loans sold (1)	2,102,468	1,608,197	1,779,989	1,302,828	1,005,764	767,721

(1) This represents the outstanding principal balance of guaranteed loans serviced, as of the last day of the applicable period, which have been sold into the secondary market.

Changes in various components of noninterest income are discussed in more detail below.

Loan Servicing Revenue: While portions of the loans that the Bank originates are sold and generate gain on sale revenue, servicing rights for all loans that the Bank originates, including loans sold, are retained by the Bank. In exchange for continuing to service loans that are sold, the Bank receives fee income represented in loan servicing revenue equivalent to one percent of the outstanding balance of the loans sold. In addition, the cost of servicing sold loans is approximately 0.40% of the balance of the loans sold, which is included in the loan servicing revaluation computations. Unrecognized servicing revenue is reflected in a servicing asset recorded on the balance sheet. Revenues associated with the servicing of loans are recognized over the expected life of the loan through the income statement, and the servicing asset is reduced as this revenue is recognized. For three and nine months ended September 30, 2016, loan servicing revenue increased $1.6 million and $4.0 million, or 39.0% and 34.7%, respectively, compared to the three and nine months ended September 30, 2015, as a result of an increase in the average outstanding balance of guaranteed loans sold. At September 30, 2016, the outstanding balance of guaranteed loans sold in the secondary market was $2.10 billion, with a weighted average servicing rate of 1.05%. At September 30, 2015, the outstanding balance of guaranteed loans sold was $1.61 billion, with a weighted average servicing rate of 1.08%. Prior to January 2010, the Company sold loans for servicing in excess of 1.0%. As loans sold for servicing fee rates in excess of 1.0% prior to fiscal year 2010 amortize, the Company expects that the weighted average servicing rate will approach and stabilize at approximately 1.0%.

Loan Servicing Revaluation: The Company revalues its serviced loan portfolio at least quarterly. The revaluation considers the amortization of the portfolio, current market conditions for loan sale premiums, and current prepayment speeds. For the three months ended September 30, 2016, there was a net negative loan servicing revaluation adjustment of $3.4 million compared to a net negative revaluation adjustment of $2.7 million for the three months ended September 30, 2015. For the nine months ended September 30, 2016 and 2015 the Company had a net negative loan servicing valuation adjustment of $5.1 million and $4.2 million, respectively. The $771 thousand and $817 thousand increase in negative adjustment in service valuation for the three-month and nine month periods ended September 30, 2016, compared to the same periods ended September 30, 2015, respectively, was primarily due to an increase in the amortization rate of the serviced portfolio and a decline in the premium market.

Net Gains on Sale of Loans: For the three and nine months ended September 30, 2016, net gains on sales of loans increased $6.4 million and $6.2 million, or 41.6% and 13.3%, respectively, compared to the three and nine months ended September 30, 2015, driven largely by the higher volume of loans sold during the third quarter of 2016. For the three months ended September 30, 2016, the volume of guaranteed loans sold increased $63.2 million, or 42.9%, to $210.6 million from $147.4 million for the three months ended September 30, 2015. The volume of guaranteed loans sold in the nine months ended September 30, 2016 was $501.8 million, an increase of $80.3 million, or 19.0%, from

$421.6 million in guaranteed loan sales in the nine months ended September 30, 2015. The volume-driven increases in the net gain on loan sale comparisons were partially mitigated by lower average premiums paid in the secondary market. The average net gain on sale of loans for the three and nine months ended September 30, 2016, was somewhat lower at $104 thousand and $105 thousand of revenue for each $1 million in loans sold, respectively, compared to $105 thousand and $111 thousand of revenue for each $1 million sold for the three and nine months ended September 30, 2015, respectively.

Table of Contents

Noninterest Expense

Noninterest expense comprises all operating costs of the Company, such as employee related costs, travel, professional services, advertising and marketing expenses, exclusive of interest and income tax expense.

The following table shows the components of noninterest expense and the related dollar and percentage changes for the periods presented.

	Three Months Ended September 30,		2015/2016 Increase (Decrease)	
	2016	2015	Amount	Percent
Noninterest expense				
Salaries and employee benefits	$17,471	$9,949	$7,522	75.61 %
Non-staff expenses:				
Travel expense	2,218	2,200	18	0.82
Professional services expense	907	493	414	83.98
Advertising and marketing expense	1,097	1,051	46	4.38
Occupancy expense	1,058	703	355	50.50
Data processing expense	1,252	773	479	61.97
Equipment expense	611	642	(31)	(4.83)
Other loan origination and maintenance expense	806	673	133	19.76
Other expense	1,798	1,579	219	13.87
Total non-staff expenses	9,747	8,114	1,633	20.13
Total noninterest expense	$27,218	$18,063	$9,155	50.68 %

	Nine Months Ended September 30,		2015/2016 Increase (Decrease)	
	2016	2015	Amount	Percent
Noninterest expense				
Salaries and employee benefits	$45,875	$27,623	$18,252	66.08 %
Non-staff expenses:				
Travel expense	6,394	5,914	480	8.12
Professional services expense	2,345	1,891	454	24.01
Advertising and marketing expense	3,425	3,177	248	7.81
Occupancy expense	3,306	1,920	1,386	72.19
Data processing expense	3,864	2,388	1,476	61.81
Equipment expense	1,696	1,473	223	15.14
Other loan origination and maintenance expense	2,001	1,384	617	44.58
Other expense	5,155	3,811	1,344	35.27
Total non-staff expenses	28,186	21,958	6,228	28.36
Total noninterest expense	$74,061	$49,581	$24,480	49.37 %

Total noninterest expense for the three and nine months ended September 30, 2016 increased $9.2 million, or 50.7%, and $24.5 million, or 49.4%, compared to the same periods in 2015. The increase in noninterest expense was predominately impacted by increased personnel, occupancy, data processing and other expenses predominantly driven by the significant growth of the Company's core business. Changes in various components of noninterest expense are discussed below.

Table of Contents

Salaries and employee benefits: Total personnel expense for the three and nine months ended September 30, 2016 increased by $7.5 million, or 75.6%, and $18.3 million, or 66.1%, compared to the same periods in 2015. This increase primarily resulted from further investment in human capital to support the growing loan production from new and existing verticals as well as development of a new small-loan and deposit platform. Full-time equivalent employees increased from 316 at September 30, 2015 to 400 at September 30, 2016. Salaries and employee benefits expense included $4.1 million and $498 thousand of stock based compensation in the three months ended September 30, 2016 and 2015, respectively, and $7.6 million and $808 thousand for the nine months ended September 30, 2016 and 2015, respectively. Expenses related to the employee stock purchase program, stock grants, stock options, stock option compensation and restricted stock expense are all considered stock based compensation. Of the total stock based compensation, $3.4 million for the third quarter of 2016 and $5.6 million for the first nine months of 2016 included in salaries and employee benefits is related to restricted stock unit ("RSU") awards for key employee retention with an effective grant date of May 24, 2016, as discussed in Note 10 of this quarterly report on Form 10-Q. On March 23, 2016, the 162(m) Subcommittee of the Compensation Committee of the Board of Directors of the Company approved these RSU awards covering a total of 1,357,500 shares of the Company's voting common stock; comprised of 507,500 shares related to RSU awards and 850,000 shares related to RSU awards with a market price condition of $34 per share. The vesting of the awards is subject to the Company achieving total revenue of at least $100 million for fiscal year 2016. In addition, vesting of the awards was subject to the approval by the Company's shareholders of certain amendments to the Company's 2015 Omnibus Plan, including an increase in the number of shares authorized under the 2015 Omnibus Plan, which were approved on May 24, 2016. The grant date of these awards was effective when shareholder approval was received. See Note 10 - Stock Plans for more information.

Occupancy expense: For the three and nine months ended September 30, 2016, total occupancy costs increased $355 thousand, or 50.5%, and $1.4 million, or 72.2%, respectively, compared to the same periods in 2015. The primary drivers of the increase in occupancy expense were increased levels of personnel to support loan production and portfolio service along with related infrastructure including a new building on the Company's main campus that was placed in service during the third quarter of 2015.

Data processing expense: For the three and nine months ended September 30, 2016, the total costs associated with data processing and development increased $479 thousand, or 62.0%, and $1.5 million, or 61.8%, respectively, compared to the same periods in 2015. This increase was principally due to the increased levels of activity in the core system from the substantial growth in loan originations, and related software and applications to operate and expand the Company's digital platform.

Loan related expenses: For the three and nine months ended September 30, 2016, total loan related expenses increased $133 thousand, or 19.8%, and $617 thousand, or 44.6%, respectively, compared to the same periods in 2015. Loans guaranteed by the SBA are assessed a guarantee fee. The primary factor for the increase in loan related expenses is the Bank's continued growth in originations of SBA guaranteed loans, requiring higher levels of guarantee fees.

Income Tax Expense

The effective tax rates for the three and nine months ended September 30, 2016 were 42.4% and 43.7%, respectively, compared to the effective tax rates of 43.5% and 40.8% for the three and nine months ended September 30, 2015, respectively. The effective tax rate for the nine months ended September 30, 2016 was higher than the corresponding period in 2015 principally due to higher levels of nondeductible expenses in 2016.

Table of Contents

Discussion and Analysis of Financial Condition

September 30, 2016 vs. December 31, 2015

Total assets at September 30, 2016 were $1.67 billion, an increase of $617.1 million, or 58.6%, compared to total assets of $1.05 billion at December 31, 2015. The growth in total assets was principally driven by the following:

- Growth in loan originations combined with longer retention times of loans held for sale, comprised largely of loans in newer verticals which require a period of loan advances to become fully funded prior to being sold; and
- Increased levels of deposits of $598.2 million, arising from a successful deposit gathering campaigns.

Cash and cash equivalents were $355.5 million at September 30, 2016, an increase of $252.9 million, or 246.5%, compared to $102.6 million at December 31, 2015, primarily as a result of increases in the deposit portfolio and high loan sales volume during the third quarter of 2016.

Total investment securities increased $16.6 million during the first nine months of 2016, from $53.8 million at December 31, 2015, to $70.3 million at September 30, 2016, an increase of 30.8%. The portfolio is comprised of US government agency securities, residential mortgage-backed securities and a mutual fund.

Loans held for sale decreased $135.3 million, or 28.2%, during the first nine months of 2016, from $480.6 million at December 31, 2015, to $345.3 million at September 30, 2016. The decrease was primarily the result of the second quarter reclassification of $318.8 million of unguaranteed loans to held for investment classification, offset by strong growth in loan origination activities throughout the first nine months of 2016.

Loans held for investment increased $487.0 million, or 174.0%, during the first nine months of 2016, from $280.0 million at December 31, 2015, to $767.0 million at September 30, 2016. The increase was primarily the result of the second quarter transfer of $318.8 million in unguaranteed loans from held for sale to held for investment combined with robust loan growth from loan origination activities during the first nine months of 2016.

Servicing assets increased $5.5 million, or 12.4%, during the first nine months of 2016, from $44.2 million at December 31, 2015, to $49.7 million at September 30, 2016. The increase in servicing assets is primarily the result of loan sales significantly outpacing the amortization of the existing serviced portfolio.

Total deposits were $1.40 billion at September 30, 2016, an increase of $598.2 million, or 74.3%, from $804.8 million at December 31, 2015. The increase in deposits was driven by success of deposit gathering campaigns to support the growth in loan originations.

Other assets increased $3.5 million, or 14.8%, during the first nine months of 2016, from $23.3 million at December 31, 2015 to $26.7 million at September 30, 2016. The change in other assets since December 31, 2015 was principally composed of increases in accrued interest receivable of $1.2 million and other cost method investments of $3.5 million, partially offset by collections on guarantee receivables from the SBA of $1.8 million.

Other liabilities increased $4.5 million, or 22.7%, during the first nine months of 2016, from $20.0 million at December 31, 2015 to $24.5 million at September 30, 2016. The change in other liabilities since December 31, 2015 was principally driven by increases in commitments for other cost method investments of $2.2 million and refundable loan commitment fees of $1.1 million.

Shareholders’ equity at September 30, 2016 was $214.2 million as compared to $199.5 million at December 31, 2015. The book value per share was $6.26 at September 30, 2016 and average equity to average assets was 15.5% for the nine months ended September 30, 2016, compared to a book value per share of $5.84 at December 31, 2015 and average equity to average assets of 15.5% for the year ended December 31, 2015. The change in shareholders’ equity principally represents net income to common shareholders for the nine months ended September 30, 2016 of $8.3 million combined with stock based compensation expense of $7.6 million partially offset by $1.7 million in dividends.

Table of Contents

Asset Quality

Management considers asset quality to be of primary importance. A formal loan review function, independent of loan origination, is used to identify and monitor problem loans. This function reports directly to the Audit & Risk Committee of the Board of Directors.

Nonperforming Assets

The Bank places loans on nonaccrual status when they become 90 days past due as to principal or interest payments, or prior to that if management has determined based upon current information available to them that the timely collection of principal or interest is not probable. When a loan is placed on nonaccrual status, any interest previously accrued as income but not actually collected is reversed and recorded as a reduction of loan interest and fee income. Typically, collections of interest and principal received on a nonaccrual loan are applied to the outstanding principal as determined at the time of collection of the loan.

Troubled debt restructurings occur when, because of economic or legal reasons pertaining to the debtor's financial difficulties, debtors are granted concessions that would not otherwise be considered. Such concessions would include, but are not limited to, the transfer of assets or the issuance of equity interests by the debtor to satisfy all or part of the debt, modification of the terms of debt or the substitution or addition of debtor(s).

The following table provides information with respect to nonperforming assets and troubled debt restructurings at the dates indicated.

	September 30, 2016	December 31, 2015
Nonperforming assets:		
Total nonperforming loans (all on nonaccrual)	$ 14,023	$ 12,367
Total accruing loans past due 90 days or more	—	—
Foreclosed assets	2,235	2,666
Total troubled debt restructurings	10,605	11,021
Less nonaccrual troubled debt restructurings	(8,434)	(8,814)
Total performing troubled debt restructurings	2,171	2,207
Total nonperforming assets and troubled debt restructurings	$ 18,429	$ 17,240
Total nonperforming loans to total loans held for investment	1.83 %	4.42 %
Total nonperforming loans to total assets	0.84 %	1.17 %
Total nonperforming assets and troubled debt restructurings to total assets	1.10 %	1.64 %

	September 30, 2016	December 31, 2015
Nonperforming assets guaranteed by U.S. government:		
Total nonperforming loans guaranteed by the SBA (all on nonaccrual)	$ 10,669	$ 10,330
Total accruing loans past due 90 days or more guaranteed by the SBA	—	—
Foreclosed assets guaranteed by the SBA	1,931	2,293
Total troubled debt restructurings guaranteed by the SBA	7,461	7,710
Less nonaccrual troubled debt restructurings guaranteed by the SBA	(7,330)	(7,550)
Total performing troubled debt restructurings guaranteed by SBA	131	160
Total nonperforming assets and troubled debt restructurings guaranteed by the SBA	$ 12,731	$ 12,783
Total nonperforming loans not guaranteed by the SBA to total held for investment loans	0.44 %	0.73 %
Total nonperforming loans not guaranteed by the SBA to total assets	0.20 %	0.19 %
Total nonperforming assets and troubled debt restructurings not guaranteed by the SBA to total assets	0.34 %	0.42 %

Table of Contents

Total nonperforming assets and troubled debt restructurings at September 30, 2016 were $18.4 million, which represented a $1.2 million, or 6.9%, increase from December 31, 2015. Total nonperforming assets at September 30, 2016 were comprised of $14.0 million in nonaccrual loans and $2.2 million in foreclosed assets. Of the $18.4 million of nonperforming assets and troubled debt restructurings ("TDRs"), $12.7 million carried an SBA guarantee, leaving an unguaranteed exposure of $5.7 million in total nonperforming assets and TDRs at September 30, 2016. The unguaranteed exposure in total nonperforming assets and TDRs at December 31, 2015 was $4.5 million. Unguaranteed exposure relating to nonperforming assets and TDRs at September 30, 2016 increased by $1.2 million, or 27.8%, compared to December 31, 2015.

As a percentage of the Bank's total capital, nonperforming loans represented 10.6% at September 30, 2016, compared to nonperforming loans of 12.0% of the Bank's total capital at December 31, 2015. Adjusting the ratio to include only the unguaranteed portion of nonperforming loans to reflect management's belief that the greater magnitude of risk resides in this portion, the ratios at September 30, 2016 and December 31, 2015 were 2.5% and 2.0%, respectively.

Risk Grades 5 through 8 represent the spectrum of criticized and impaired loans. As of September 30, 2016, potential problem loans and impaired loans totaled $54.5 million with loans in the Veterinary and Healthcare industries, our two largest verticals, comprising 37.0% and 29.1%, respectively. As of December 31, 2015, potential problem and impaired loans totaled $41.0 million with loans in the Veterinary and Healthcare industry verticals comprising 50.2% and 27.0%, respectively. The majority of the impaired loans in the Veterinary industry were originated prior to 2010. The Company believes that its underwriting and credit quality standards have improved as the business has matured. At September 30, 2016, the portion of criticized loans guaranteed by the SBA totaled $20.8 million resulting in unguaranteed exposure risk of $33.7 million, or 4.6% of total held for investment unguaranteed exposure. This compares to total criticized and impaired loans of $41.0 million at December 31, 2015, of which $17.2 million was guaranteed by the SBA.

The Bank does not classify loans that experience insignificant payment delays and payment shortfalls as impaired. The Bank considers an "insignificant period of time" from payment delays to be a period of 90 days or less. The Bank would consider a modification for a customer experiencing what is expected to be a short term event that has temporarily impacted cash flow. This could be due, among other reasons, to illness, weather, impact from a one-time expense, slower than expected start-up, construction issues or other short term issues. In all cases, credit will review the request to determine if the customer is stressed and how the event has impacted the ability of the customer to repay the loan long term. To date, the only types of short term modifications the Bank has given are payment deferral and interest only extensions. The Bank does not typically alter the rate or lengthen the amortization of the note due to insignificant payment delays. Short term modifications are not classified as TDRs, because they do not meet the definition set by the applicable accounting standards and the Federal Deposit Insurance Corporation.

Management endeavors to be proactive in its approach to identify and resolve special mention (Risk Grade 5) loans and is focused on working with the borrowers and guarantors of these loans to provide loan modifications when warranted. At September 30, 2016 and December 31, 2015, Risk Grade 5 loans totaled $31.1 million and $17.5 million, respectively. The increase in Risk Grade 5 loans from December 31, 2015 to September 30, 2016 was principally confined to three verticals; Healthcare ($4.1 million or 30.1% of increase), Deathcare ($2.9 million or 21.5% of increase), and Independent Pharmacies ($2.4 million or 17.3% of increase). The underlying cause of the increase in Risk Grade 5 loans from December 31, 2015 to September 30, 2016 was ongoing maturation of legacy verticals combined with a $1.4 million positive migration of Risk Grade 6 loans to Risk Grade 5. At September 30, 2016, approximately 97.0% of loans classified as Risk Grade 5 are performing with no current payments past due.

While the level of nonperforming assets fluctuates in response to changing economic and market conditions, the relative size and composition of the loan portfolio, and management's degree of success in resolving problem assets, management believes that a proactive approach to early identification and intervention is critical to successfully managing a small business loan portfolio.

The results of the recent Hurricane Matthew have been assessed and only one borrower in our Agriculture vertical was affected by this storm with minor damage.

Allowance for Loan Losses

The allowance for loan losses ("ALL"), a material estimate which could change significantly in the near-term in the event of rapidly deteriorating credit quality, is established through a provision for loan losses charged to earnings to account for losses that are inherent in the loan portfolio and estimated to occur, and is maintained at a level that management considers appropriate to absorb losses in the loan portfolio. Loan losses are charged against the ALL when management believes that the collectibility of the principal loan balance is unlikely. Subsequent recoveries, if any, are credited to the ALL when received.

Judgment in determining the adequacy of the ALL is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available and as situations and information change.

The ALL is evaluated on a quarterly basis by management and takes into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans and current economic conditions and trends that may affect the borrower's ability to repay.

Table of Contents

Estimated credit losses should meet the criteria for accrual of a loss contingency, i.e., a provision to the ALL, set forth in accounting principles generally accepted in the United States of America (“GAAP”). Methodology for determining the ALL is generally based on GAAP, the Interagency Policy Statement on the Allowance for Loan and Lease Losses and other regulatory and accounting pronouncements. The ALL is determined by the sum of three separate components: (i) the impaired loan component, which addresses specific reserves for impaired loans; (ii) the general reserve component, which addresses reserves for pools of homogeneous loans; and (iii) an unallocated reserve component (if any) based on management’s judgment and experience. The loan pools and impaired loans are mutually exclusive; any loan that is impaired should be excluded from its homogeneous pool for purposes of that pool’s reserve calculation, regardless of the level of impairment.

During the second quarter of 2016, the Company implemented enhancements to the methodology for estimating the allowance for loan losses, including refinements to the measurement of qualitative factors in the estimation process. Management believes these enhancements will improve the precision of the process for estimating the allowance.

The ALL of $7.4 million at December 31, 2015 increased by $7.8 million, or 104.7%, to $15.2 million at September 30, 2016. The ALL, as a percentage of loans held for investment, amounted to 2.0% at September 30, 2016 and 2.6% at December 31, 2015. The increase in the allowance for loan losses was largely attributable to continued growth in the loan portfolio combined with the effects of the transfer of $318.8 million of unguaranteed loans from held for sale to held for investment and charge-off experience, as addressed in the Provision for Loan Losses section of Results of Operations. General reserves as a percentage of non-impaired loans amounted to 1.60% at September 30, 2016 and 2.05% December 31, 2015. By transferring a $318.8 million pool of high quality unguaranteed credits into the held for investment portfolio during the second quarter, the allowance as a percentage of total loans held for investment and general reserves as a percentage of non-impaired loans has declined somewhat as compared to December 31, 2015. See the aforementioned Provision for Loan Losses section of this section for a discussion of the Company's charge-off experience.

Actual past due loans and charge-offs have increased as management continues to work to improve asset quality. Management believes the ALL of $15.2 million at September 30, 2016 is appropriate in light of the risk inherent in the loan portfolio. Management’s judgments are based on numerous assumptions about current events that it believes to be reasonable, but which may or may not be valid. Thus, there can be no assurance that loan losses in future periods will not exceed the current ALL or that future increases in the ALL will not be required. No assurance can be given that management’s ongoing evaluation of the loan portfolio in light of changing economic conditions and other relevant circumstances will not require significant future additions to the ALL, thus adversely affecting the Company’s operating results. Additional information on the ALL is presented in Note 5 to the consolidated financial statements included with this report.

Liquidity Management

Liquidity management refers to the ability to meet day-to-day cash flow requirements based primarily on activity in loan and deposit accounts of the Company’s customers. Liquidity is immediately available from four major sources: (a) cash on hand and on deposit at other banks; (b) the outstanding balance of federal funds sold; (c) the market value of unpledged investment securities; and (d) availability under lines of credit. At September 30, 2016, the total amount of these four items was $603.6 million, or 36.1% of total assets, an increase of $312.2 million from $291.4 million, or 27.7% of total assets, at December 31, 2015.

Loans and other assets are funded primarily by loan sales, wholesale deposits and core deposits. To date, an increasing retail deposit base and a level amount of brokered deposits have been adequate to meet loan obligations, while maintaining the desired level of immediate liquidity. Additionally, an investment securities portfolio is available for both immediate and secondary liquidity purposes.

At September 30, 2016, none of the investment securities portfolio was pledged to secure public deposits or pledged to retail repurchase agreements, while $101 thousand was pledged for trust activities in the state of Ohio, $1.2 million was pledged for uninsured trust assets and $1.5 million was pledged for secured federal funds lines of credit, leaving $67.5 million available as lendable collateral.

Table of Contents

Contractual Obligations

The following table presents the Company's significant fixed and determinable contractual obligations by payment date as of September 30, 2016. The payment amounts represent those amounts contractually due to the recipient. The table excludes liabilities recorded where management cannot reasonably estimate the timing of any payments that may be required in connection with these liabilities.

	Payments Due by Period				
	Total	Less than One Year	One to Three Years	Three to Five Years	More Than Five Years
Contractual Obligations					
Deposits without stated maturity	$530,029	$530,029	$—	$—	$ —
Time deposits	872,988	550,600	236,718	85,670	—
Long term borrowings	28,074	812	1,726	25,536	—
Operating lease obligations	1,969	660	1,095	214	—
Total	$1,433,060	$1,082,101	$239,539	$111,420	$ —

Asset/Liability Management and Interest Rate Sensitivity

One of the primary objectives of asset/liability management is to maximize the net interest margin while minimizing the earnings risk associated with changes in interest rates. One method used to manage interest rate sensitivity is to measure, over various time periods, the interest rate sensitivity positions, or gaps. This method, however, addresses only the magnitude of timing differences and does not address earnings or market value. Therefore, management uses an earnings simulation model to prepare, on a regular basis, earnings projections based on a range of interest rate scenarios to more accurately measure interest rate risk.

The balance sheet is liability-sensitive with a total cumulative gap position of -9.18% at September 30, 2016. During 2016, a large volume of deposits were obtained through a nationwide campaign, resulting in the liability-sensitive gap position. A liability-sensitive position means that net interest income will generally move in the opposite direction as interest rates. For instance, if interest rates increase, net interest income can be expected to decrease, and if interest rates decrease, net interest income can be expected to increase. The Company attempts to mitigate interest rate risk with the majority of assets and liabilities being short-term, adjustable rate instruments. The quarterly revaluation adjustment to the servicing asset, however, adjusts in an opposite direction to interest rate changes. Asset/liability sensitivity is primarily derived from the prime-based loans that adjust as the prime interest rate changes and the longer duration of indeterminate term deposits.

Table of Contents

Capital

The maintenance of appropriate levels of capital is a management priority and is monitored on a regular basis. The Company's principal goals related to the maintenance of capital are to provide adequate capital to support the Company's risk profile consistent with the risk appetite approved by the Board of Directors; provide financial flexibility to support future growth and client needs; comply with relevant laws, regulations, and supervisory guidance; achieve optimal credit ratings for the Company and its subsidiaries; and provide a competitive return to shareholders. Management regularly monitors the capital position of the Company on both a consolidated and bank level basis. In this regard, management's goal is to maintain capital at levels that are in excess of the regulatory "well capitalized" levels. Risk-based capital ratios, which include Tier 1 Capital, Total Capital and Common Equity Tier 1 Capital, are calculated based on regulatory guidance related to the measurement of capital and risk-weighted assets. Capital amounts and ratios as of September 30, 2016 and December 31, 2015, are presented in the table below.

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions (1)	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Consolidated - September 30, 2016						
Common Equity Tier 1 (to Risk-Weighted Assets)	$198,436	16.63%	$53,703	4.50%	N/A	N/A
Total Capital (to Risk-Weighted Assets)	$213,400	17.88%	$95,471	8.00%	N/A	N/A
Tier 1 Capital (to Risk-Weighted Assets)	$198,436	16.63%	$71,603	6.00%	N/A	N/A
Tier 1 Capital (to Average Assets)	$198,436	13.18%	$60,245	4.00%	N/A	N/A
Bank - September 30, 2016						
Common Equity Tier 1 (to Risk-Weighted Assets)	$117,575	10.26%	$51,559	4.50%	$74,474	6.50 %
Total Capital (to Risk-Weighted Assets)	$132,007	11.52%	$91,660	8.00%	$114,575	10.00%
Tier 1 Capital (to Risk-Weighted Assets)	$117,575	10.26%	$68,745	6.00%	$91,660	8.00 %
Tier 1 Capital (to Average Assets)	$117,575	8.21 %	$57,291	4.00%	$71,614	5.00 %
Consolidated - December 31, 2015						
Common Equity Tier 1 (to Risk-Weighted Assets)	$191,366	23.22%	$37,087	4.50%	N/A	N/A
Total Capital (to Risk-Weighted Assets)	$198,781	24.12%	$65,933	8.00%	N/A	N/A
Tier 1 Capital (to Risk-Weighted Assets)	$191,366	23.22%	$49,450	6.00%	N/A	N/A
Tier 1 Capital (to Average Assets)	$191,366	18.36%	$41,702	4.00%	N/A	N/A
Bank - December 31, 2015						
Common Equity Tier 1 (to Risk-Weighted Assets)	$96,056	12.28%	$35,207	4.50%	$50,855	6.50 %
Total Capital (to Risk-Weighted Assets)	$103,471	13.23%	$62,591	8.00%	$78,238	10.00%
Tier 1 Capital (to Risk-Weighted Assets)	$96,056	12.28%	$46,943	6.00%	$62,591	8.00 %
Tier 1 Capital (to Average Assets)	$96,056	9.75 %	$39,398	4.00%	$49,248	5.00 %

(1) Prompt corrective action provisions are not applicable at the bank holding company level.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements in accordance with GAAP requires the Company to make estimates and judgments that affect reported amounts of assets, liabilities, income and expenses and related disclosure of contingent assets and liabilities. The Company bases estimates on historical experience and on various other assumptions that are believed to be reasonable under current circumstances, results of which form the basis for making judgments about the carrying value of certain assets and liabilities that are not readily available from other sources. Estimates are evaluated on an ongoing basis. Actual results may differ from these estimates under different assumptions or conditions.

Accounting policies, as described in detail in the notes to the Company’s consolidated financial statements, are an integral part of the Company’s consolidated financial statements. A thorough understanding of these accounting policies is essential when reviewing the Company’s reported results of operations and financial position. Management believes that the critical accounting policies and estimates listed below require the Company to make difficult, subjective or complex judgments about matters that are inherently uncertain.

Table of Contents

- Determination of the allowance for loan losses;
- Valuation of servicing assets; and
- Valuation of foreclosed assets.

Changes in these estimates, that are likely to occur from period to period, or the use of different estimates that the Company could have reasonably used in the current period, would have a material impact on the Company's financial position, results of operations or liquidity.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Management considers interest rate risk the most significant market risk. Interest rate risk is the exposure to adverse changes in net interest income due to changes in interest rates. Consistency of net interest income is largely dependent upon the effective management of interest rate risk.

The Company's Asset/Liability Management Committee ("ALCO"), which includes senior management representatives and reports to the Board of Directors, monitors and manages interest rate risk. See "Asset/Liability Management and Interest Rate Sensitivity" in Item 2 of this Form 10-Q for further discussion.

The objective of asset/liability management is the maximization of net interest income within the Company's risk guidelines. This objective is accomplished through management of the balance sheet composition, maturities, liquidity, and interest rate risk exposures arising from changing economic conditions, interest rates and customer preferences.

To identify and manage its interest rate risk, the Company employs an earnings simulation model to analyze net interest income sensitivity to changing interest rates. The model is based on contractual cash flows and repricing characteristics and incorporates market-based assumptions regarding the effect of changing interest rates on the prepayment rates of certain assets and liabilities. The model also includes management projections for activity levels in each of the product lines offered by the Bank. Assumptions are inherently uncertain, and the measurement of net interest income or the impact of rate fluctuations on net interest income cannot be precisely predicted. Actual results may differ materially from simulated results due to timing, magnitude, and frequency of interest rate changes as well as changes in market conditions and management strategies.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

An evaluation of the Company's disclosure controls and procedures (as defined in Rules 13(a)-15(e) and 15(d)-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act")), was carried out under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer as of September 30, 2016, the last day of the period covered by this Quarterly Report. The Company's Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective as of September 30, 2016 in ensuring that the information required to be disclosed in the reports the Company files or submits under the Exchange Act is (i) accumulated and communicated to management (including the Company's Chief Executive Officer and Chief Financial Officer) as appropriate to allow timely decisions regarding required disclosures, and (ii) recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms.

Changes in Internal Control Over Financial Reporting

Management has not evaluated any changes in the Company's internal control over financial reporting that occurred during the quarterly period ended September 30, 2016 due to a transition period established by the rules of the Securities and Exchange Commission for newly public companies.

Table of Contents

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

In the ordinary course of operations, the Company is party to various legal proceedings. The Company is not involved in, nor has it terminated during the three and nine months ended September 30, 2016, any pending legal proceedings other than nonmaterial proceedings occurring in the ordinary course of business.

Item 1A. Risk Factors

There have been no material changes to the risk factors that have been previously disclosed in the Company’s 2015 Annual Report filed with the SEC.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibits to this report are listed in the Index to Exhibits section of this report.

Table of Contents

SIGNATURES

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

Live Oak Bancshares, Inc.
(Registrant)

Date: November 8, 2016 By:/s/ S. Brett Caines
S. Brett Caines
Chief Financial Officer

Table of Contents

INDEX TO EXHIBITS

Exhibit No.	Description of Exhibit
3.1	Amended and Restated Articles of Incorporation of Live Oak Bancshares, Inc. (incorporated by reference to Exhibit 3.1 of the registration statement on Form S-1, filed on June 19, 2015)
3.2	Amended Bylaws of Live Oak Bancshares, Inc. (incorporated by reference to Exhibit 3.2 of the registration statement on Form S-1, filed on June 19, 2015)
4.1	Form of Common Stock Certificate (incorporated by reference to Exhibit 4.1 of the registration statement on Form S-1, filed on June 19, 2015)
4.2	Registration and Other Rights Agreement between Live Oak Bancshares, Inc. and Wellington purchasers (incorporated by reference to Exhibit 4.2 of the registration statement on Form S-1, filed on June 19, 2015)
31.1	Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
31.2	Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
32	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**
101	Interactive data files pursuant to Rule 405 of Regulation S-T: (i) Consolidated Balance Sheets as of September 30, 2016 and December 31, 2015; (ii) Consolidated Statements of Income for the Three and Nine Months Ended September 30, 2016 and 2015; (iii) Consolidated Statements of Comprehensive Income for the Three and Nine Months Ended September 30, 2016 and 2015; (iv) Consolidated Statements of Changes in Shareholders' Equity for the Nine Months Ended September 30, 2016 and 2015; (v) Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2016 and 2015; and (vi) Notes to Consolidated Financial Statements*

* Indicates a document being filed with this Form 10-Q.

** Furnished herewith. This exhibit shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liability of that Section. Such exhibit shall not be deemed incorporated into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934.