WEST COAST COMMUNITY BANCORP | SANTA CRUZ COUNTY BANK

2023

CONSOLIDATED FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT

Years Ended December 31, 2023 and 2022

WEST COAST COMMUNITY BANCORP

CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2023 and 2022

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INDEPENDENT AUDITOR'S REPORT

The Shareholders and Board of Directors
West Coast Community Bancorp
Santa Cruz, California

Report on the Audit of the Financial Statements

Opinion

We have audited the consolidated financial statements of West Coast Community Bancorp, which comprise the consolidated balance sheets as of December 31, 2023 and 2022, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of West Coast Community Bancorp as of December 31, 2023 and 2022, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with auditing standards generally accepted in the United States of America, West Coast Community Bancorp's internal control over financial reporting as of December 31, 2023, based on criteria established in the *Internal Control—Integrated Framework* (2013), issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) relevant to reporting objectives for the express purpose of meeting the regulatory requirements of Section 112 of the Federal Deposit Insurance Corporation Improvement Act (FDICIA) and our report dated March 22, 2024 expressed an unmodified opinion.

Emphasis of Matter

As discussed in Note 1 to the consolidated financial statements, West Coast Community Bancorp changed its method for accounting for credit losses effective January 1, 2023, due to the adoption of Financial Accounting Standards Board (FASB) Accounting Standards Codification No. 326, Financial Instruments - Credit Losses (ASC 326). Our opinion is not modified with respect to this matter.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of West Coast Community Bancorp and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

(Continued)

Responsibilities of Management for the Financial Statements

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

In preparing the consolidated financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about West Coast Community Bancorp's ability to continue as a going concern for one year from the date the consolidated financial statements are available to be issued.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the consolidated financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the consolidated financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about West Coast Community Bancorp's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control–related matters that we identified during the audit.

Crowe LLP

Crowe LLP

Sacramento, California
March 22, 2024

WEST COAST COMMUNITY BANCORP
CONSOLIDATED BALANCE SHEETS
As of December 31, 2023 and 2022
Dollar amounts in thousands

ASSETS	2023	2022
Cash and cash equivalents	$ 33,938	$ 42,693
Interest-bearing deposits in other financial institutions	10,457	34,690
Debt securities available-for-sale	262,566	320,730
Debt securities held-to-maturity (fair value 2023: $7,342; 2022: $2,834)	7,585	2,840
Loans held for sale	33,696	45,263
Loans	1,377,597	1,222,476
Less: Allowance for credit losses on loans	(23,943)	(21,444)
Loans, net of allowance	1,353,654	1,201,032
Non-marketable equity investments, at cost	8,897	8,630
Premises and equipment, net	11,030	15,026
Goodwill	25,762	25,762
Core deposit intangible asset, net	1,671	2,034
Bank-owned life insurance	18,059	17,605
Accrued interest receivable and other assets	27,047	28,182
Total assets	$ 1,794,362	$ 1,744,487
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits		
Noninterest-bearing	$ 576,456	$ 669,489
Interest-bearing	938,634	861,293
Total deposits	1,515,090	1,530,782
Federal Home Loan Bank advances and other borrowings	32,500	–
Accrued interest payable and other liabilities	16,736	16,029
Total liabilities	1,564,326	1,546,811
Commitments and contingencies – See Note 16 - "Loan Commitments and Other Related Activities"		
Shareholders' equity		
Preferred stock, no par value; 10,000,000 shares authorized; no shares issued or outstanding	–	–
Common stock, no par value; 30,000,000 shares authorized; 8,406,680 and 8,477,272 shares issued at December 31, 2023 and 2022	122,597	124,628
Retained earnings	117,263	89,239
Accumulated other comprehensive loss	(9,824)	(16,191)
Total shareholders' equity	230,036	197,676
Total liabilities and shareholders' equity	$ 1,794,362	$ 1,744,487

See accompanying notes.

WEST COAST COMMUNITY BANCORP
CONSOLIDATED STATEMENTS OF INCOME
Years ended December 31, 2023 and 2022
Dollar amounts in thousands

	2023	2022
Interest and dividend income		
Loans, including fees	$ 88,759	$ 65,744
Interest-bearing deposits in other financial institutions	1,199	2,003
Taxable securities	4,212	3,270
Tax-exempt securities	223	77
Dividends on FHLB, PCBB and TIB stock	510	437
Federal funds sold	10	530
Total interest and dividend income	94,913	72,061
Interest expense		
Deposits	11,506	1,850
Federal Home Loan Bank advances and other borrowings	643	2
Total interest expense	12,149	1,852
Net interest income before provision for credit losses	82,764	70,209
Provision for credit losses on loans	554	1,592
Provision for credit losses on unfunded loan commitments	859	19
Net interest income after provision for credit losses	81,351	68,598
Noninterest income		
Service charges on deposits	471	457
Net gains on sales of loans	–	1,245
Loan servicing fees	728	735
ATM fee income	885	916
Earnings on bank-owned life insurance	454	433
Other	1,034	758
Total noninterest income	3,572	4,544
Noninterest expense		
Salaries and employee benefits	19,699	17,076
Occupancy	2,347	2,074
Furniture and equipment	2,291	1,744
Marketing and business development	714	619
Data and item processing	1,939	1,364
Federal deposit insurance and other assessment	958	694
Amortization of core deposit intangibles	363	406
Professional fees	1,259	719
Other	5,583	4,687
Total noninterest expense	35,153	29,383
Income before income taxes	49,770	43,759
Income tax expense	14,620	12,815
Net income	$ 35,150	$ 30,944
Earnings per share:		
Basic	$ 4.19	$ 3.63
Diluted	$ 4.17	$ 3.62

See accompanying notes.

WEST COAST COMMUNITY BANCORP
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
Years ended December 31, 2023 and 2022
Dollar amounts in thousands

	2023	2022
Net income	$ 35,150	$ 30,944
Other comprehensive income (loss)		
Unrealized losses on securities		
Change in unrealized losses on available-for-sale securities	8,959	(21,034)
Amortization of net unrealized losses on securities transferred from available-for-sale to held-to-maturity	1	1
Tax effect	(2,649)	6,219
Net of tax	6,311	(14,814)
Defined benefit pension plans		
Actuarial net gain arising during the period	158	984
Reclassification adjustment for amortization of net gain included in net periodic pension cost	(78)	–
Tax effect	(24)	(291)
Net of tax	56	693
Total other comprehensive income (loss)	6,367	(14,121)
Comprehensive income	$ 41,517	$ 16,823

See accompanying notes.

WEST COAST COMMUNITY BANCORP
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Years ended December 31, 2023 and 2022
Dollar amounts in thousands, except per share data

	Shares	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance at December 31, 2021	8,536,000	$ 125,828	$ 62,332	$ (2,070)	$ 186,090
Net income	–	–	30,944	–	30,944
Stock repurchased, net of commissions	(81,000)	(2,001)	–	–	(2,001)
Other comprehensive loss	–	–	–	(14,121)	(14,121)
Cash dividends declared ($0.475 per share)	–	–	(4,037)	–	(4,037)
Stock-based compensation	–	583	–	–	583
Exercise of stock options	13,472	218	–	–	218
Restricted stock awards granted	8,800	–	–	–	–
Balance at December 31, 2022	8,477,272	124,628	89,239	(16,191)	197,676
Cumulative effect of change in accounting principal: adoption of ASU 2016-13 (see Note 1)	–	–	(3,263)	–	(3,263)
Net income	–	–	35,150	–	35,150
Stock repurchased, net of commissions	(121,079)	(2,999)	–	–	(2,999)
Other comprehensive income	–	–	–	6,367	6,367
Cash dividends declared ($0.460 per share)	–	–	(3,863)	–	(3,863)
Stock-based compensation	–	725	–	–	725
Exercise of stock options	22,712	243	–	–	243
Restricted stock awards granted	27,775	–	–	–	–
Balance at December 31, 2023	8,406,680	$ 122,597	$ 117,263	$ (9,824)	$ 230,036

See accompanying notes.

WEST COAST COMMUNITY BANCORP
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years ended December 31, 2023 and 2022
Dollar amounts in thousands

	2023	2022
Cash flows from operating activities		
Net income	$ 35,150	$ 30,944
Adjustments to reconcile net income to net cash from operating activities:		
Provision for credit losses on loans	554	1,592
Provision for credit losses on unfunded loan commitments	859	19
Depreciation and amortization of premises and equipment	1,363	1,002
Amortization of core deposit intangibles	363	406
	29	37
Net amortization of securities	1,618	1,912
Net accretion of acquired loans	(341)	(582)
Deferred income tax expense (benefit)	140	(323)
Net loss on sale of securities	30	1
Net gain on sale of loans	–	(1,245)
Stock-based compensation expense	725	583
Earnings on bank-owned life insurance	(454)	(433)
Stock dividends from equity investments	(5)	–
Originations of loans held for sale	(15,889)	(37,484)
Proceeds from sales of loans originated for sale	–	21,881
Gain on sale/disposal of premises and equipment	(249)	–
Non-cash lease expense	12	21
Deferred post-retirement benefit expense	322	162
Decrease (increase) in deferred loan fees, net of costs	1,153	(3,665)
Increase in accrued interest receivable and other assets	(740)	(3,064)
Decrease in accrued interest payable and other liabilities	(529)	(1,751)
Net cash provided by operating activities	24,111	10,013
Cash flows from investing activities		
Net change in interest-bearing deposits in other financial institutions	24,204	(13,061)
Available-for-sale securities:		
	17,195	110
Maturities, prepayments, calls, and principal repayments	57,340	30,206
Purchases	(9,042)	(101,161)
Held-to-maturity securities:		
Maturities, prepayments, calls, and principal repayments	1,219	406
Purchases	(5,949)	–
Loan originations and payments, net	(130,643)	(45,426)
Purchases of premises and equipment	(1,272)	(3,744)
Purchases of non-marketable equity investments	(261)	(2,698)
Proceeds from sale of premises and equipment	4,154	–
Net cash used in investing activities	(43,055)	(135,368)

See accompanying notes.

WEST COAST COMMUNITY BANCORP
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years ended December 31, 2023 and 2022
Dollar amounts in thousands

	2023	2022
Cash flows from financing activities		
(Decrease) increase in deposits	(15,692)	34,446
Proceeds from borrowings	32,500	–
Cash dividends paid	(3,863)	(4,037)
Proceeds from exercise of stock options, including tax benefit	243	218
Cash paid for stock repurchases	(2,999)	(2,001)
Net cash from financing activities	10,189	28,626
Net change in cash and cash equivalents	(8,755)	(96,729)
Beginning cash and cash equivalents	42,693	139,422
Ending cash and cash equivalents	$ 33,938	$ 42,693
Supplemental cash flow information		
Interest paid	$ 11,345	$ 1,706
Income taxes paid	$ 13,820	$ 17,000
Supplemental noncash disclosure		
Transfer from loans held for sale to portfolio loans	$ 25,532	$ 39,950

See accompanying notes.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations: Santa Cruz County Bank ("the Bank") is a California state-chartered bank and was incorporated on September 10, 2003. The Bank commenced banking operations on February 3, 2004, upon receipt of final regulatory approval and is an insured bank by the Federal Deposit Insurance Corporation ("FDIC"). West Coast Community Bancorp ("the Bancorp") was incorporated in the State of California on November 10, 2009. The Bancorp obtained approval from the Board of Governors of the Federal Reserve System on June 2, 2023 to become a bank holding company and became the sole shareholder of the Bank on August 18, 2023 through a reorganization agreement, pursuant to which all the outstanding common stock of the Bank was exchanged for an equal number of shares of common stock of the Bancorp. Upon formation of the holding company, Bancorp became subject to regulation under the Bank Holding Company Act of 1956, as amended, and reporting and examination requirements by the Board of Governors of the Federal Reserve System. The Bank is subject to regulations and undergoes periodic examinations by the Department of Financial Protection and Innovation and the FDIC.

Basis of Presentation: The consolidated financial statements include West Coast Community Bancorp and its wholly owned subsidiary, Santa Cruz County Bank, together referred to as "the Company", "we," "our," or "us". Significant intercompany transactions and balances are eliminated in consolidation. Our accounting and reporting policies conform to U.S. generally accepted accounting principles ("GAAP"), general practice, and regulatory guidance within the banking industry.

Virtually all our business is conducted through Bancorp's subsidiary, the Bank, which is headquartered in Santa Cruz, California and offers a full range of commercial and personal banking services to residents and businesses in Santa Cruz County and adjacent Monterey and Santa Clara counties, through our eight full-service offices located in Aptos, Capitola, Cupertino, Monterey, Salinas, Santa Cruz, Scotts Valley, and Watsonville. Our primary deposit products are checking, savings, and term certificate accounts, and our primary lending products are commercial, commercial real estate, construction, multifamily, agriculture, single-family home equity loans, municipal loans, asset-backed loans, and installment loans. Bank lending products also include various government guarantee programs such as Small Business Administration ("SBA") 7(a) and 504 programs, as well as US Department of Agriculture ("USDA") programs. Our largest industry concentration is in hotels and lodging, as commercial real estate loans with hotel related collateral as well as commercial loans to hotel and related borrowers composed 16% of total outstanding loans as of December 31, 2023. The single largest borrower had combined outstanding and unfunded commitments that represented 3% of total outstanding loans as of December 31, 2023.

Presentation of Notes 2 to 17: All dollar amounts presented in the tables in Notes 2 to 17 are in thousands, unless otherwise indicated, except per share information. Dollar amounts in paragraphs are in whole dollars, unless otherwise indicated.

Subsequent Events: We have evaluated subsequent events for recognition and disclosure from December 31, 2023 through March 22, 2024, which is the date the financial statements were available to be issued.

Use of Estimates: The preparation of these financial statements, in conformity with U.S. GAAP, requires management to make estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided, and actual results could differ from those estimates.

Cash Flows: For purposes of reporting cash flows, cash and cash equivalents include cash, due from banks, federal funds sold, and deposits with other financial institutions with maturities at origination fewer than 90 days. Federal funds are sold for a one-day period and are highly liquid investments. Net cash flows are reported for customer loan and deposit transactions, interest-bearing deposits in other financial institutions with maturities shorter than 90 days at origination, and federal funds purchased.

Interest-Bearing Deposits in Other Financial Institutions: Interest bearing deposits in other financial institutions mature beyond 90 days at origination are carried at amortized cost.

Debt Securities: Debt securities are classified as held-to-maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Debt securities are classified as available-for-sale when they might be sold before maturity. Securities available-for-sale are carried at fair value with unrealized holding gains and losses reported in other comprehensive income, net of tax. At the time of purchase, we designate securities as either held-to-maturity or available-for-sale based on its investment objectives, operational needs, and intent.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized on the level-yield method to prepayment date for mortgage-backed securities where prepayments are anticipated. For callable debt securities purchased at a premium, premiums are amortized to the earliest call date. Realized gains and losses on sales are recorded on the settlement date and determined using the specific identification method.

Securities transferred from the available-for-sale to held-to-maturity are recorded at fair value at the date of transfer. Unrealized holding gains or losses on the date of transfer are included in the balance of accumulated other comprehensive income (losses), net of tax. The unrealized gains or losses are amortized over the remaining life of the securities as yield adjustments in a manner consistent with the amortization or accretion of purchase premiums or discounts.

Allowance for Credit Losses on Debt Securities: The allowance for credit losses on held-to-maturity securities is a contra-asset valuation account that is deducted from the amortized cost basis of held-to-maturity securities to present the net amount expected to be collected. Management measures expected credit losses on held-to-maturity debt securities on a collective basis for securities with similar risk characteristics using historical credit loss information that is adjusted for current conditions and reasonable and supportable forecasts. Securities that are determined to be uncollectible are written off against the allowance for credit losses.

For available-for-sale debt securities in an unrealized loss position, we first assess whether we intend to sell, or it is more likely than not that it will be required to sell the security before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the security's amortized cost basis is written down to fair value through income. For debt securities available-for-sale that do not meet these conditions, we evaluate whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers the extent to which fair value is less than amortized cost, any changes to the rating of the security by a rating agency, and adverse conditions specifically related to the security, among other factors. If this assessment indicates that a credit loss exists, the present value of cash flows expected to be collected from the security are compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis, a credit loss exists and an allowance for credit losses is recorded for the credit loss, limited by the amount that the fair value is less than the amortized cost basis. Any impairment that has not been recorded through an allowance for credit losses is recognized in other comprehensive income. Changes in the allowance for credit losses are recorded as credit loss expense (or reversal). Losses are charged against the allowance when management believes the uncollectibility of an available-for-sale security is confirmed or when either of the criteria regarding intent or requirement to sell is met.

Accrued interest receivable on debt securities is excluded from the estimate of credit losses. A debt security is placed on nonaccrual status at the time any principal or interest payments become contractually past due more than ninety days delinquent, or management does not expect full payment of principal and interest. Interest accrued but not received for a security placed on nonaccrual is reversed against interest income. There were no nonaccrual debt securities recorded in the consolidated financial statements for year ended 2023 or 2022. The Bank did not record an allowance for credit losses on available-for-sale or held-to-maturity investment securities upon the adoption of CECL as the investment portfolio consisted primarily of debt securities backed by the U.S. government and high credit quality obligations of state and political subdivisions. Refer to Note 2, Debt Securities, for more information.

Loans Held for Sale: Loans originated and intended for sale in the secondary market are carried at the lower of aggregate cost or fair value. Net unrealized losses, if any, are recorded as a valuation allowance and charged to earnings. These loans are generally held for approximately one and a half years from their origination date at which time they are reclassified to loans for held for investment at the lower of cost or fair value.

Loans held for sale are generally sold with servicing rights retained. The carrying value of loans sold is reduced by the amount allocated to the servicing right. If the loans are sold with servicing retained, the fair value of the servicing asset or liability is recorded on the balance sheet. Gains and losses on the sold portion of the loans are recognized at the time of sale based on the difference between the sale proceeds and the carrying value of the related loans sold.

Loans: Loans that management has the intent and ability to hold for the foreseeable future, or until maturity or payoff, are reported at the amount of unpaid principal balances outstanding, net of deferred loan fees and costs, and an allowance for credit losses. Interest income is accrued on the unpaid principal balance daily and credited to income as it is earned. When a loan pays off or is sold, any unamortized balance of any related premiums, discounts, loan origination fees, and direct loan origination costs is recognized in income. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income over the expected life of the loan using a method that approximates the level yield method without anticipating prepayments.

Interest income on loans is generally discontinued and placed on nonaccrual status at the time the loan is 90 days delinquent or when management believes, after considering economic and business conditions and collection efforts, that the borrower's financial condition is such that collection of interest is doubtful unless the loan is well-secured and in the process of collection. Past-due status is based on the contractual terms of the loan. A loan is moved to nonaccrual status in accordance with the loan policy, typically after 90 days of non-payment. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. Nonaccrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

When a loan is placed on nonaccrual status, all interest previously accrued but not collected is reversed against current period interest income. Interest received on such loans is accounted for on the cash-basis method and recognized only to the extent that cash is received and where the future collection of principal is probable, until qualifying for return to accrual. Generally, loans will be restored to an accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Concentration of Credit Risk: More than half of our business activity is with customers located within Santa Cruz County. Therefore, exposure to credit risk is significantly affected by changes in the economy in the Santa Cruz County area.

Allowance for Credit Losses on Loans (“ACL”): The ACL is a valuation account that is deducted from the amortized cost basis of the loan portfolio at the balance sheet date to present the net amount of loans expected to be collected. Amortized cost does not include accrued interest, which management elected to exclude from the estimate of expected credit losses. On a quarterly basis, management conducts estimations for the ACL, employing relevant information sourced both internally and externally. This information encompasses data on past events, current conditions, and reasonable and supportable forecasts. This process aligns with established financial disclosure practices, ensuring a comprehensive and transparent representation of the allowance determination.

The allowance is established through a provision for credit losses, which is charged to expense. Additions to the allowance are expected to maintain the adequacy of the total allowance after credit losses and loan growth. Loan losses are charged against the allowance when management believes a loan balance is uncollectible. Cash received on previously charged-off amounts is recorded as a recovery to the allowance. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, forecasted economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged-off.

The ACL consists of specific and general reserves. The general reserve portion of the allowance is measured on a collective basis for portfolios of loans when similar risk characteristics exist. Loans exhibiting risk characteristics distinct from pooled loans undergo individual credit loss assessments and specific reserves are established when appropriate and are excluded from the general pools. This evaluation typically encompasses nonaccrual loans, collateral-dependent loans, certain troubled debt restructured loans, and loans graded as substandard or worse by management.

The ACL model utilizes the average charge off method to measure the expected credit losses on loans at the instrument level. It incorporates historical loss rates ("HLR"), qualitative factors, and a forward look ("FL") estimate to determine overall reserve rates on a loan-by-loan basis. Despite loans being evaluated on a loan level basis for the purpose of HLR, qualitative factor adjustments and the FL adjustment to loans are pooled together by asset class, including the following:

- Commercial and Industrial
- Commercial Real Estate
- Construction and Land
- Agriculture Land, Real Estate and Production
- Consumer

Commercial and Industrial – Commercial and industrial loans generally possess a lower inherent risk of loss than real estate portfolio segments because these loans are generally underwritten to existing cash flows of operating businesses. Debt coverage is provided by business cash flows and economic trends influenced by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans.

Commercial Real Estate – Commercial real estate mortgage loans generally possess a higher inherent risk of loss than other real estate portfolio segments, except land and construction loans. Adverse economic developments or an overbuilt market impact commercial real estate projects and may result in troubled loans. Trends in vacancy rates of commercial properties impact the credit quality of these loans. High vacancy rates reduce operating revenues and the ability for properties to produce sufficient cash flow to service debt obligations.

Construction and Land – Construction and land loans generally possess a higher inherent risk of loss than other real estate portfolio segments. A major risk arises from the necessity to complete projects within specified cost and timelines. Trends in the construction industry significantly impact the credit quality of these loans, as demand drives construction activity. In addition, trends in real estate values significantly impact the credit quality of these loans, as property values determine the economic viability of construction projects.

Agricultural Land, Real Estate and Production – Agricultural real estate mortgage loans generally possess a lower inherent risk of loss than other real estate portfolio segments, including land and construction loans. Adverse economic developments may result in troubled loans. Loans related to crop production and livestock are especially vulnerable to two risk factors that are largely outside our control and borrowers: commodity prices and weather conditions.

Consumer – Comprised of single-family residential real estate, home equity lines of credit and personal lines. The degree of risk in residential real estate lending depends primarily on the loan amount in relation to collateral value, the interest rate, and the borrower's ability to repay in an orderly fashion. These loans generally possess a lower inherent risk of loss than other real estate portfolio segments. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Weak economic trends indicate that the borrowers' capacity to repay their obligations may be deteriorating.

Historical loss rates are based on peer bank loss data using Call Report data and are calculated using a rolling 4 quarter average of the previous 20 years, in lieu of using our own data due to limited loss history. Qualitative factors are then based on standard deviations off of the historical average loss rate by asset class. The FL is defined as an adjustment representing the value of a reasonable and supportable forecast. To support this forecast we chose to utilize national GDP and unemployment rates as the economic drivers of the regression analysis used to determine the adjustments. The forecasted GDP and Unemployment Rate are sourced from the Federal Open Market Committee, and the regression analysis is updated quarterly by PCBB and is applied to these forecasted rates and applied to the first 12 months of each loan level calculation. After 12 months, the reserve rates revert back to historical averages plus corresponding qualitative adjustments.

Expected credit losses are estimated over the contractual term of the loans, but are adjusted for expected prepayments and curtailments, when appropriate. The pooled loans' contractual terms exclude extensions, renewals, and modifications unless one or more of the following applies: 1) Management has a reasonable expectation at the reporting date that a loan modification will be executed with an individual borrower, 2) The extension or renewal options are included in the original or modified contract, 3) An existing loan modification is within 6 months of maturity.

Pre-payment assumptions are based upon our current market interest rate compared to each loan's existing current interest rate. Market rates are calculated based upon pooling assets classes for loans approved within the preceding quarters.

In determining the quantitative portion of the ACL, management assesses the necessity for adjustments, considering differences in risk characteristics specific to the segment. Additionally, adjustments may be made to reflect variations in current conditions and reasonable and supportable forecasts of economic conditions compared to the conditions during the period covered by the HLR calculation. Qualitative factors, both internal and external, are considered in this process. These factors include, but are not limited to, the following:

- Changes in the experience, ability, and depth of lending management and other relevant staff
- Changes in the value of underlying collateral for collateral dependent loans
- The existence and effect of any concentrations of credit and changes in the level of such concentrations
- Changes in international, national, regional, and local economic and business conditions and developments that affect the collectability of the portfolio, including the condition of various market segments
- The effect of other external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the loan portfolio
- Changes in the volume and severity of past due loans, the volume of nonaccrual loans, and the volume and severity of adversely classified or graded loans
- Changes in the quality of our institution's loan review systems
- Changes in the nature and volume of the loan portfolio and in the terms of loans
- Changes in lending policies and procedures including changes in underwriting standards and collection, charge off, and recovery practices not considered elsewhere in estimating credit losses
- Additional specific qualitative factors to account for model deficiencies

At least quarterly, the Board of Directors reviews the adequacy of the allowance, including consideration of the relative risks in the portfolio, current economic conditions and other factors. Although management strives to use the most reliable information for determining the ACL and believes it to be adequate, the ultimate sufficiency of the allowance is contingent upon a diverse set of intricate factors, some of which may fall outside of management's direct control. Factors contributing to this assessment include volatility in the real estate market, shifts in interest rates, and fluctuations in economic and political environments. Actual losses may vary from its estimates if circumstances deviate substantially from the assumptions used in the allowance determination process. Our ACL model exhibits sensitivity to changes in unemployment rate and GDP forecasts, and the prevailing interest rate environment can lead to substantial fluctuations in the prepayment speeds on our loans and the resulting expected lives of the loans and the related allowance for credit losses. These fluctuations, if significant, have the potential to adversely impact our financial condition and results of operations.

Allowance for Credit Losses on Unfunded Commitments: We engage in commitments to extend credit, both in the form of loans and standby letters of credit, to fulfill the financing needs of our customers. In the event of a deterioration in the credit quality of the borrower, resulting in nonperformance, we are exposed to credit losses over the contractual period of a loan. To account for potential losses on unfunded loan commitments, we record an allowance. The allowance is established based on estimates that consider the probability of these commitments being drawn upon, guided by historical utilization experience across various types of commitments. The loss factors applied in estimating the allowance for unfunded loan commitments align with those used for the funded portion of the loan portfolio. This approach ensures consistency in evaluating credit risk across our entire commitment portfolio, contributing to a comprehensive and uniform assessment of potential credit losses.

The ACL on unfunded commitments is a liability account included in the interest payable and other liabilities on the consolidated balance sheet. Adjustments to the allowance for unfunded commitments are included as a provision for (or reversal of) the ACL. The allowance for unfunded credit commitments totaled $1,783,000 and $403,000 at December 31, 2023 and 2022, respectively, and is included in other liabilities on the consolidated balance sheet.

Loan Servicing Rights: When loans are sold with servicing retained, servicing rights are initially recorded at fair value with the income statement effect recorded in gains on sales of loans. Fair value is based on market prices for comparable loan servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. All classes of servicing assets are subsequently measured using the amortization method, which requires servicing rights to be amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying loans. Loan servicing rights were $506,000 and $859,000 at December 31, 2023 and 2022, respectively, and were included in accrued interest receivable and other assets on the consolidated balance sheets.

Servicing rights are evaluated for impairment based upon the fair value of the rights as compared to carrying amount. Impairment is determined by stratifying rights into groupings based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual grouping, to the extent that fair value is less than the carrying amount. If we later determine that all or a portion of the impairment no longer exists for a particular grouping, a reduction of the allowance may be recorded as an increase to income. Changes in valuation allowances are reported with loan servicing fees income on the income statement. The fair values of servicing rights are subject to significant fluctuations as a result of changes in estimated and actual prepayment speeds and default rates and losses.

Servicing fee income, which is reported on the income statement as loan servicing fees, is recorded for fees earned on servicing loans. The fees are based on a fixed amount per loan and recorded as income when earned. The amortization of servicing rights is netted against loan servicing fee income. Servicing fees totaled $728,000 and $735,000 for December 31, 2023 and 2022, respectively. Late fees and ancillary fees related to loan servicing are not material.

Non-marketable Equity Investments Carried at Cost: Equity securities without readily determinable fair market values are carried at cost, minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for an identical or similar investment. The carrying amount of equity securities without readily determinable fair market values totaled $8,897,000 and $8,630,000 at December 31, 2023 and 2022, respectively, and include the following:

Federal Home Loan Bank Stock - The Bank, as a member of the Federal Home Loan Bank (“FHLB”) system, is required to maintain an investment in the capital stock of the FHLB of San Francisco based on the Bank’s asset size or the level of borrowings and other factors. FHLB stock is carried at cost, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends, if any, are reported as income. The FHLB stock cannot be purchased or sold except between the FHLB and its members and is redeemable at its par value of $100 per share at the discretion of the FHLB of San Francisco and therefore is classified as restricted investment without readily determinable fair values. The FHLB can suspend dividends and redemptions upon notification to its members.

Bankers’ Bank Stock - Stock of Pacific Coast Bankers Bank (“PCBB”) and The Independent Bankers Bank (“TIB”) are classified as restricted securities carried at cost, and are periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends, if any, are reported as income.

Clearinghouse Community Development Financial Institution (“CCDFI”) Stock - Stock of CCDFI is classified as restricted securities carried at cost, and is periodically evaluated for impairment based on ultimate recovery of par value. Cash dividends, if any, are reported as income.

Premises and Equipment: Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Depreciation is determined using the straight-line method over the estimated useful lives of the related asset. Building and related components are depreciated over 39½ years. Furniture, fixtures and equipment are depreciated with useful lives ranging from 5 to 7 years. Leasehold improvements are amortized over the shorter of the estimated useful life of the assets or the initial term of the respective leases. The useful lives of leasehold improvements are estimated to be 3 to 15 years. When assets are sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recognized in income for the period. All other maintenance and repair expenditures are charged to expense as incurred.

Goodwill and Intangible Assets: Goodwill arises from business combinations and is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. We accounted for the acquisition of Lighthouse Bank in 2019 using the acquisition method of accounting. Under the acquisition method, assets and liabilities assumed are recorded at their estimated fair values at the date of acquisition. Management utilizes various valuation techniques to determine these fair values. Any excess of the purchase price over amounts allocated to the acquired assets, including identifiable intangible assets, and liabilities assumed is recorded as goodwill.

Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but tested for impairment at least annually or more frequently if events and circumstances exists that indicate that a goodwill impairment test should be performed. We perform a qualitative impairment analysis as of each quarter end. Management assessed qualitative factors, including performance trends, and noted no factors indicating goodwill impairment. Goodwill is the only intangible asset with an indefinite life on our balance sheet.

Core deposit intangibles represent the estimated fair value of the core deposit relationships acquired in the business combination with Lighthouse Bank and are being amortized using an accelerated basis based on dollar weighted deposit runoff on an annualized basis over an estimated life of ten years from the date of acquisition.

Bank-Owned Life Insurance ("BOLI"): We purchased life insurance policies on certain key executives and former executives. Bank-owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

Loan Commitments and Related Financial Instruments: Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

Revenue Recognition: In general, for revenue not associated with financial instruments, guarantees and lease contracts, we apply the following steps when recognizing revenue from contracts with customers: (i) identify the contract, (ii) identify the performance obligations, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations and (v) recognize revenue when a performance obligation is satisfied. Contracts with customers are generally short term in nature, typically due within one year or less or cancellable by us or our customer upon a short notice period. Performance obligations for our customer contracts are generally satisfied at a single point in time, typically when the transaction is complete, or over time. For performance obligations satisfied over time, we primarily use the output method, directly measuring the value of the products/services transferred to the customer, to determine when performance obligations have been satisfied. We typically receive payment from customers and recognize revenue concurrent with the satisfaction of its performance obligations. In most cases, this occurs within a single financial reporting period. For payments received in advance of the satisfaction of performance obligations, revenue recognition is deferred until such time as the performance obligations have been satisfied. In cases where we have not received payment despite satisfaction of our performance obligations, an estimate of the amount due in the period the performance obligations have been satisfied is accrued. For contracts with variable components, only amounts for which collection is probable are accrued.

We generally act in a principal capacity, in most of our contracts with customers. In such transactions, we recognize revenue and the related costs to provide services on a gross basis in the financial statements. These transactions primarily relate to service charges on deposit accounts, which consist of monthly maintenance fees, business accounting analysis fees and business online banking fees that are generally recognized monthly when we satisfy our performance obligation each month. Certain transaction-based services, such as check order charges and wire transfer fees, are recognized at a point in time typically when the transaction is completed.

In some cases, we act in an agent capacity, deriving revenue through assisting other entities in transactions with our customers. In such transactions, we recognize revenue and the related costs to provide these services on a net basis in the financial statements. These transactions recognized on a net basis primarily relate to fees derived from our customers' use of various interchange and ATM/debit card networks.

Stock-Based Compensation: Compensation cost is recognized for stock options and restricted stock awards issued to employees and directors, based on the fair value of these awards at the date of grant. We estimate the fair value of each stock option award as of the date of grant using a Black-Scholes model, while the market price of our common stock at the date of grant is used for restricted stock awards.

Compensation cost is recognized over the required service period, generally defined as the vesting period. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award. Our accounting policy is to recognize forfeitures as they occur.

Income Taxes: Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred taxes are computed using the asset and liability method, which represents the tax effects for the temporary differences between carrying amounts and tax bases of assets and liabilities, based on current tax law, of future deductible or taxable amounts attributable to events that have been recognized in the financial statements. A valuation allowance is established to reduce the deferred tax asset to the level at which it is “more likely than not” that the tax asset or benefits will be realized. Deferred tax assets and liabilities are calculated by applying current enacted tax rates against future deductible or taxable amounts. Realization of tax benefits of deductible temporary differences and operating loss carry forwards depends on having sufficient taxable income of an appropriate character within the carry forward periods.

Accounting for Uncertainty in Income Taxes: We use a comprehensive model for recognizing, measuring, presenting and disclosing in the financial statements tax positions taken or expected to be taken on a tax return. A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded.

We recognize interest and/or penalties related to income tax matters in income tax expense.

Retirement Plans: Pension expense is the net of service and interest cost, return on plan assets and amortization of gains and losses not immediately recognized. Employee 401(k) plan expense is the amount of employer matching contributions. Deferred compensation and supplemental retirement plan expense allocates the benefits over years of service.

Earnings Per Common Share: Basic earnings per common share are calculated by dividing net income by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable under stock options. There is no adjustment to the number of outstanding shares for potential dilutive instruments, such as stock options, when a loss occurs because the conversion of potential common stock is anti-dilutive or when stock options are not in-the-money. Earnings and dividends per share are restated for all stock splits and stock dividends through the date of issuance of the financial statements.

Comprehensive Income: Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes the adjustment to fully recognize the liability associated with the Supplemental Executive Retirement Plan (“SERP”), changes in the unrealized gains and losses on securities available-for-sale, and amortization of net unrealized gains and losses on securities transferred from available-for-sale to held-to-maturity, net of taxes, which are also recognized as separate components of equity on the consolidated statements of comprehensive income.

Loss Contingencies: Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there now are such matters that will have a material effect on the financial statements.

Restrictions on Cash and Due from Banks: The Federal Reserve Act Regulation D requires banks to maintain average reserve balances with the Federal Reserve Bank. Reserve requirements are offset by usable cash reserves. We had no reserve requirement at December 31, 2023 or 2022 to meet regulatory reserve and clearing requirements.

Dividend Restriction: Banking regulations require maintaining certain capital levels and may limit the dividends paid by the Bank to the holding company or by the holding company to shareholders.

The California Financial Code and California General Corporation Law also impose restrictions on dividends that may be paid from the Bank and Bancorp, respectively. Refer to Note 15 for further details.

Fair Value of Financial Instruments: The fair value of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect these estimates.

Reclassifications: Certain reclassifications have been made to prior period financial statements to conform to the current year presentation. These reclassifications had no impact on prior year net income or shareholders' equity.

Adoption of New Accounting Standards: On January 1, 2023, we adopted *FASB Accounting Standard Update ("ASU") No. 2016-13, Financial Instruments – Credit Losses ("ASU 326"): Measurement of Credit Losses on Financial Instruments*, as amended, which replaces the incurred loss methodology with an expected loss model that is referred to as the current expected credit loss ("CECL") model. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loan receivables and held-to-maturity debt securities. It also applies to off-balance sheet credit exposures not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in certain leases recognized by a lessor in accordance with Topic 842 on leases. In addition, ASC 326 made changes to the accounting for available-for-sale debt securities. One such change is to require credit losses to be presented as a valuation allowance rather than as a direct write-down on available-for-sale debt securities management does not intend to sell or believes that it is more likely than not they will be required to sell.

We adopted ASC 326 using the modified retrospective method for all financial assets measured at amortized cost and off-balance sheet credit exposures. Results for reporting periods beginning after January 1, 2023 are presented under ASC 326 while prior period amounts continue to be reported in accordance with previously applicable GAAP. A one-time cumulative effect adjustment was recorded to the allowance for credit losses of $4,112,000 as well as $521,000 increase to allowance on unfunded credit commitments, with the after-tax effect of $3,263,000 recorded against retained earnings upon adoption. Refer to Note 3 for additional information.

As allowed by ASC 326, we elected to maintain pools of loans accounted for under ASC 310-30. These loan pools are described in detail in this Note earlier and in Note 3. In accordance with the standard, management did not reassess whether modifications to individual acquired financial assets accounted for in pools were troubled debt restructurings as of the date of adoption.

On January 1, 2023, we adopted *ASU No. 2022-02, Financial Instruments - Credit Losses (Topic 326) - Troubled Debt Restructurings and Vintage Disclosures* – In March 2022, the FASB issued an Update to eliminate the recognition and measurement guidance for troubled debt restructurings ("TDRs") by creditors in ASC 310-40, *Receivables-Troubled Debt Restructurings by Creditors*, while enhancing disclosure requirements for certain loan refinancings and restructurings by creditors when a borrower is experiencing financial difficulty. Specifically, rather than applying the recognition and measurement guidance for TDRs, an entity now applies the loan refinancing and restructuring guidance to determine whether a modification or other form of restructuring results in a new loan or a continuation of an existing loan. Additionally, for public business entities, the amendments in this ASU require a public business entity to disclose current-period gross write-offs by year of origination for financing receivables and net investments in leases in the existing disclosures. The adoption of this standard did not have a material impact on our consolidated financial statements.

Newly Issued Accounting Standards Not Yet Effective: *ASU No. 2020-04, Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting, as amended* - On March 12, 2020, the FASB issued guidance to ease the potential burden in accounting for reference rate reform. The amendments in Update 2020-04 are elective and apply to all entities that have contracts, hedging relationships, and other transactions that reference London Interbank Offered Rate ("LIBOR") or another reference rate are expected to be discontinued due to reference rate reform. The new guidance provides a number of optional expedients that reduce costs and complexity of accounting for reference rate reform. Topic 848 was amended in January 2021 with ASU No. 2021-01, which provided additional guidance on certain optional expedients and scope of derivative instruments, and further amended in December 2022 with ASU 2022-06 to defer the sunset of Topic 848 from December 31, 2022 to December 31, 2024, after which entities will no longer be permitted to apply the relief in Topic 848. We do not anticipate a material impact on our consolidated financial statements due to lack of contracts that reference LIBOR.

ASU No. 2023-09, Income Taxes (Topic 740): Improvements To Income Tax Disclosures - On December 14, 2023, the FASB issued guidance to enhance the transparency and decision usefulness of income tax disclosures. The amendments require additional information to disclose specific categories in the rate reconciliation and reconciling items that meet a quantitative threshold. In addition, the amendments require that all entities disclose on an annual basis the amount of income taxes paid, net of refunds received on a disaggregated basis. The guidance is effective for annual periods beginning after December 15, 2024. Early adoption is permitted for annual financial statements that have not yet been issued or made available for issuance. We do not anticipate the adoption of this guidance to have a material impact on our consolidated financial statements.

NOTE 2 - DEBT SECURITIES

The fair value of available-for-sale securities reflected net unrealized losses of $15,004,000 and $23,963,000 at December 31, 2023 and 2022, respectively. The unrealized loss recorded is net of $4,436,000 and $7,085,000 tax effect as accumulated other comprehensive income within shareholders' equity at December 31, 2023 and 2022, respectively.

The following table summarizes the carrying value and estimated fair value of securities available-for-sale at December 31, 2023:

December 31, 2023	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale:				
U.S. Treasury Bonds	$ 210,956	$ –	$ (12,168)	$ 198,788
U.S. Government sponsored agencies	12,901	–	(547)	12,354
SBA backed securities	10,616	1	(129)	10,488
Mortgage-backed securities: residential	9,364	149	(556)	8,957
Mortgage-backed securities: commercial	28,156	–	(1,381)	26,775
Collateralized mortgage obligations	58	–	(1)	57
State and political subdivision	5,519	126	(498)	5,147
Total available-for-sale	$ 277,570	$ 276	$ (15,280)	$ 262,566

The following table summarizes the carrying value, allowance for credit losses, and estimated fair value of securities held-to-maturity at December 31, 2023:

December 31, 2023	Amortized Cost	Allowance for Credit Losses	Carrying Value	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Held-to-maturity:						
Mortgage-backed securities: residential	$ 190	$ –	$ 190	$ –	$ (4)	$ 186
Collateralized mortgage obligations	575	–	575	3	(20)	558
State and political subdivision	6,820	–	6,820	30	(252)	6,598
Total held-to-maturity	$ 7,585	$ –	$ 7,585	$ 33	$ (276)	$ 7,342

Most of the portfolio's unrealized losses are related to U.S. Treasury bonds. With regard to U.S. Treasury and residential and commercial mortgage-backed securities issued by the U.S. government, or debentures issued by its sponsored agencies, it is expected that the securities will not be settled at prices less than the par value bases of the securities, as such securities are backed by the full faith and credit of and/or guaranteed by the U.S. Government. The decline in fair value on these investments is attributable to changes in interest rates and or factors other than credit quality. As of December 31, 2023, we neither had the intent to sell these securities, nor is more likely than not that we will be required to sell the securities before their anticipated recovery.

Regarding potential credit losses on securities issued by states and political subdivisions, management considers (i) issuer bond ratings, (ii) historical probability of default and loss given default rates for given bond ratings and remaining maturity, (iii) whether issuers continue to make timely principal and interest payments under the contractual terms of the securities, (iv) internal and external credit review of the latest financial information of the issuers, and (v) whether or not such securities are guaranteed by insurance or the Texas Permanent School Fund ("PSF"), have other credit enhancements, contain a defeasance clause, or pre-refunded by the issuers.

Based on a comprehensive assessment of the portfolio as discussed in the preceding two paragraphs, no credit losses are expected. For that reason, no allowance for credit losses has been recognized on available-for-sale or held-to-maturity securities as of December 31, 2023.

The following table summarizes the carrying value and estimated fair value of securities available-for-sale and held-to-maturity at December 31, 2022:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
December 31, 2022				
Available-for-sale:				
U.S. Treasury bonds	$ 266,862	$ –	$ (19,898)	$ 246,964
U.S. Government sponsored agencies	19,879	–	(856)	19,023
SBA backed securities	15,481	1	(170)	15,312
Mortgage-backed securities: residential	6,581	–	(768)	5,813
Mortgage-backed securities: commercial	31,217	–	(1,596)	29,621
Collateralized mortgage obligations	128	–	(3)	125
State and political subdivision	4,545	–	(673)	3,872
Total available-for-sale	$ 344,693	$ 1	$ (23,964)	$ 320,730
Held-to-maturity:				
Mortgage-backed securities: residential	$ 290	$ –	$ (7)	$ 283
Collateralized mortgage obligations	721	3	(26)	698
State and political subdivision	1,829	24	–	1,853
Total held-to-maturity	$ 2,840	$ 27	$ (33)	$ 2,834

There were no transfers between available-for-sale and held-to-maturity during 2023 or 2022.

Five available-for-sale securities were sold in 2023 with total proceeds of $17,195,000 and combined net losses of $30,000 recorded. A downgraded available-for-sale municipal bond was sold in 2022 with proceeds of $110,000 and a loss of $1,000 recorded.

The amortized cost and estimated fair value of debt securities at December 31, 2023 are shown by contractual maturity. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately.

	December 31, 2023	
	Amortized Cost	Estimated Fair Value
Available-for-sale:		
Within one year	$ 77,400	$ 75,926
One to five years	145,469	134,400
Five to ten years	4,534	3,941
Beyond ten years	1,973	2,022
SBA-backed securities	10,616	10,488
Mortgage-backed securities	37,520	35,732
Collateralized mortgage obligations	58	57
Total	$ 277,570	$ 262,566
Held-to-maturity:		
Within one year	$ –	$ –
One to five years	505	507
Five to ten years	366	394
Beyond ten years	5,949	5,697
Mortgage-backed securities	190	186
Collateralized mortgage obligations	575	558
Total	$ 7,585	$ 7,342

Securities pledged at December 31, 2023 and 2022 to secure local public agency deposits and State of California deposits had an amortized cost of $69,176,000 and $64,212,000, respectively and a fair value of $65,061,000 and $59,658,000, respectively.

At December 31, 2023 and 2022, there were no holdings of securities of any one issuer, other than those issued by U.S. Government and its sponsored agencies, in an amount greater than 10% of shareholders' equity.

The following tables summarize investment securities with unrealized losses at December 31, 2023 and December 31, 2022, aggregated by major security type and length of time in a continuous unrealized or unrecognized loss position:

December 31, 2023	Less Than 12 months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-sale:						
U.S. Treasury bonds	$ –	$ –	$ 198,788	$ (12,168)	$ 198,788	$ (12,168)
U.S. Government sponsored agencies	–	–	12,354	(547)	12,354	(547)
SBA-backed securities	–	–	10,169	(129)	10,169	(129)
Mortgage-backed securities: residential	–	–	4,969	(556)	4,969	(556)
Mortgage-backed securities: commercial	6,971	(255)	19,803	(1,126)	26,774	(1,381)
Collateralized mortgage obligations	–	–	57	(1)	57	(1)
State and political subdivision	–	–	3,551	(498)	3,551	(498)
Total available-for-sale	$ 6,971	$ (255)	$ 249,691	$ (15,025)	$ 256,662	$ (15,280)
Held-to-maturity:						
Mortgage-backed securities: residential	$ –	$ –	$ 184	$ (4)	$ 184	$ (4)
Collateralized mortgage obligations	73	(1)	391	(19)	464	(20)
State and political subdivision	5,697	(252)	–	–	5,697	(252)
Total held-to-maturity	$ 5,770	$ (253)	$ 575	$ (23)	$ 6,345	$ (276)

December 31, 2022	Less Than 12 months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-sale:						
U.S. Treasury bonds	$ 65,595	$ (2,108)	$ 181,369	$ (17,790)	$ 246,964	$ (19,898)
U.S. Government sponsored agencies	13,911	(184)	5,113	(672)	19,024	(856)
SBA-backed securities	–	–	14,845	(170)	14,845	(170)
Mortgage-backed securities: residential	–	–	5,813	(768)	5,813	(768)
Mortgage-backed securities: commercial	21,846	(905)	7,775	(691)	29,621	(1,596)
Collateralized mortgage obligations	125	(3)	–	–	125	(3)
State and political subdivision	3,872	(673)	–	–	3,872	(673)
Total available-for-sale	$ 105,349	$ (3,873)	$ 214,915	$ (20,091)	$ 320,264	$ (23,964)
Held-to-maturity:						
Mortgage-backed securities: residential	$ 283	$ (7)	$ –	$ –	$ 283	$ (7)
Collateralized mortgage obligations	580	(26)	–	–	580	(26)
Total held-to-maturity	$ 863	$ (33)	$ –	$ –	$ 863	$ (33)

As of December 31, 2023, our securities portfolio consisted of 131 investment securities, 6 of which were in an unrealized loss position for less than twelve months and 118 were in a loss position and had been in a loss position for twelve months or more. As of December 31, 2022, our securities portfolio consisted of 151 investment securities, 64 of which were in an unrealized loss position for less than twelve months and 80 were in a loss position and had been in a loss position for twelve months or more.

NOTE 3 - LOANS RECEIVABLE

The outstanding loan portfolio balances at amortized cost, net of deferred fees and costs at December 31, 2023 and 2022 were as follows:

	2023	2022
Commercial and industrial	$ 228,597	$ 222,586
Commercial real estate	909,427	737,952
Land and construction	151,321	170,935
Agricultural land, real estate and production	46,661	44,342
Consumer	41,591	46,661
Loans, net of deferred fees and costs	1,377,597	1,222,476
Allowance for credit losses on loans	(23,943)	(21,444)
Loans receivable, net of allowance	$ 1,353,654	$ 1,201,032

Deferred fees at December 31, 2023 and 2022 were $6,783,000 and $6,252,000 respectively. Deferred costs at December 31, 2023 and 2022 were $8,942,000 and $9,198,000 respectively.

At December 31, 2023 and 2022, loans held for sale that were originated under SBA totaled $33,696,000 and $45,263,000, respectively.

Salaries and employee benefits totaling $5,031,000 and $5,082,000 have been deferred as loan origination costs for the years ended December 31, 2023 and 2022, respectively.

The following tables present the activity in the ACL by portfolio segment for each of the years ended December 31, 2023 and 2022.

December 31, 2023	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Unallocated	Total
Allowance for credit losses:							
Beginning balance	$ 5,581	$ 6,692	$ 8,742	$ 88	$ 341	$ -	$ 21,444
Impact of adopting ASC 326	134	10,877	(7,727)	283	545	-	4,112
Provisions	255	133	(352)	(18)	(353)	889	554
Loans charged off	(2,171)	-	-	-	-	-	(2,171)
Recoveries	-	-	-	4	-	-	4
Ending balance	$ 3,799	$ 17,702	$ 663	$ 357	$ 533	$ 889	$ 23,943

December 31, 2022	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Unallocated	Total
Allowance for loan losses:							
Beginning balance	$ 5,264	$ 5,831	$ 8,448	$ 137	$ 298	$ -	$ 19,978
Provisions	372	863	294	20	43	-	1,592
Loans charged off	(87)	(2)	-	(69)	-	-	(158)
Recoveries	32	-	-	-	-	-	32
Ending balance	$ 5,581	$ 6,692	$ 8,742	$ 88	$ 341	$ -	$ 21,444

The following table presents the balance in the allowance for loan losses and the recorded investment, net of deferred fees and costs in loans by portfolio segment and based on incurred loss method as of December 31, 2022:

December 31, 2022	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Total
Allowance for loan losses						
Allowance balance attributable to loans:						
Individually evaluated for impairment	$ 1,526	$ –	$ –	$ –	$ –	$ 1,526
Collectively evaluated for impairment	4,055	6,692	8,742	88	341	19,918
Total allowance balance	$ 5,581	$ 6,692	$ 8,742	$ 88	$ 341	$ 21,444
Loans						
Loans individually evaluated for impairment	$ 1,527	$ –	$ 990	$ –	$ 834	$ 3,351
Loans collectively evaluated for impairment	221,059	737,952	169,945	44,342	45,827	1,219,125
Total loans balance	$ 222,586	$ 737,952	$ 170,935	$ 44,342	$ 46,661	$ 1,222,476

The following table presents the recorded investment, net of deferred fees and costs in nonaccrual loans and loans past due over 89 days by class of loans as of December 31, 2023 and 2022.

	Nonaccrual		Loans Past Due Over 89 Days and Still Accruing	
	2023	2022	2023	2022
Commercial and industrial	$ –	$ 1,363	$ –	$ 10
Commercial real estate	6,526	–	2,999*	–
Land and construction	–	990	–	–
Agricultural land, real estate and production	–	–	–	–
Consumer	–	808	–	–
Total	$ 6,526	$ 3,161	$ 2,999	$ 10

*A $3.0 million delinquent commercial real estate loan was subsequently paid off in January 2024.

The following table presents the aging of the recorded investment, net of deferred fees and costs in past due loans as of December 31, 2023 and 2022 by class of loans.

December 31, 2023	30 – 59 Days Past Due	60 – 89 Days Past Due	Greater Than 89 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial and industrial	$ -	$ -	$ -	$ -	$ 228,597	$ 228,597
Commercial real estate	-	-	9,525	9,525	899,902	909,427
Land and construction	-	-	-	-	151,321	151,321
Agricultural land, real estate and production	-	-	-	-	46,661	46,661
Consumer	-	-	-	-	41,591	41,591
Total	$ -	$ -	$ 9,525	$ 9,525	$ 1,368,072	$ 1,377,597

December 31, 2022	30 – 59 Days Past Due	60 – 89 Days Past Due	Greater Than 89 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial and industrial	$ 501	$ 483	$ 1,373	$ 2,357	$ 220,229	$ 222,586
Commercial real estate	-	-	-	–	737,952	737,952
Land and construction	-	-	990	990	169,945	170,935
Agricultural land, real estate and production	-	-	-	–	44,342	44,342
Consumer	-	-	808	808	45,853	46,661
Total	$ 501	$ 483	$ 3,171	$ 4,155	$ 1,218,321	$ 1,222,476

The following table presents the gross charge-offs in 2023, by year of origination.

	Charge offs by Origination Year					
	2023	2022	2021	Prior Periods	Revolving	Totals
Commercial and industrial	$ -	$ -	$ -	$ -	$ 2,171	$ 2,171
Total	$ -	$ -	$ -	$ -	$ 2,171	$ 2,171

The following table presents the recorded investment of loan modifications, segregated by type of modification, to borrowers experiencing financial difficulty during 2023.

December 31, 2023	Payment Delay	Percent of Total Class of Loans
Modifications:		
Commercial and industrial	$ 299	0.13%
Consumer	22	0.05%
Total	$ 321	0.02%

The Bank had a recorded investment, net of deferred fees and costs of $26,000 in one consumer troubled debt restructure as of December 31, 2022. No specific allowance had been set aside for the troubled debt restructure loan. The modification terms included a payment reduction but no permanent reduction in the recorded investment of the loan. The loan was performing according to its modified terms at December 31, 2023.

Credit Quality Indicators: We assign loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial condition of borrowers and guarantors, historical payment experience, credit documentation, public information, and current economic trends, among other factors. We analyze all loans individually by classifying the loans according to credit risk. This analysis includes loans with an outstanding balance greater than $25,000 and non-homogeneous loans, such as commercial and commercial real estate loans. The loans are evaluated and rated at the time of underwriting, at renewal, if payment becomes past due, or if an event of default occurs. These risk ratings are also subject to examination by independent specialists we engage and our regulators. The risk categories can be grouped into four major categories, defined as follows:

Pass – A pass loan is a credit with no existing or known potential weaknesses deserving of management's close attention.

Special Mention – A special mention loan has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or in our credit position at some future date. Special Mention loans are not adversely classified and do not expose us to sufficient risk to warrant adverse classification.

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

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

Overdraft lines of credit and loans that do not meet the criteria above are considered to be pass-rated loans.

Based on the most recent analysis performed, the following table presents the risk category of loans by class and year of origination of loans as of December 31, 2023:

	Term Loans Amortized Cost Basis by Origination Year					
	2023	2022	2021	Prior Periods	Revolving	Totals
Commercial and industrial						
Pass	$ 21,376	$ 30,841	$ 24,589	$ 50,513	$ 84,529	$ 211,848
Special mention	-	344	1,549	2,810	11,573	16,276
Substandard	-	-	-	473	-	473
Total	$ 21,376	$ 31,185	$ 26,138	$ 53,796	$ 96,102	$ 228,597
Commercial real estate						
Pass	$ 210,897	$ 161,622	$ 126,112	$ 367,565	$ 24,238	$ 890,434
Special mention	-	-	2,269	2,777	-	5,046
Substandard	-	-	-	7,421	-	7,421
Substandard-nonaccrual	-	-	-	6,526	-	6,526
Total	$ 210,897	$ 161,622	$ 128,381	$ 384,289	$ 24,238	$ 909,427
Land and construction						
Pass	$ 17,098	$ 60,618	$ 41,792	$ 21,410	$ 415	$ 141,333
Special mention	-	-	9,988	-	-	9,988
Total	$ 17,098	$ 60,618	$ 51,780	$ 21,410	$ 415	$ 151,321
Agriculture land, real estate and production						
Pass	$ 5,636	$ 9,562	$ 9,372	$ 17,323	$ 940	$ 42,833
Special mention	-	331	2,251	1,101	145	3,828
Total	$ 5,636	$ 9,893	$ 11,623	$ 18,424	$ 1,085	$ 46,661
Consumer						
Pass	$ 7,549	$ 7,479	$ 5,382	$ 13,283	$ 7,876	$ 41,569
Substandard	-	-	-	22	-	22
Total	$ 7,549	$ 7,479	$ 5,382	$ 13,305	$ 7,876	$ 41,591
Total						
Pass	$ 262,556	$ 270,122	$ 207,247	$ 470,094	$ 117,998	$ 1,328,017
Special mention	-	675	16,057	6,688	11,718	35,138
Substandard	-	-	-	7,916	-	7,916
Substandard-nonaccrual	-	-	-	6,526	-	6,526
Total	$ 262,556	$ 270,797	$ 223,304	$ 491,224	$ 129,716	$ 1,377,597

The following table shows the risk category of the loan portfolio by class at December 31, 2022:

	Pass	Special Mention	Substandard	Doubtful	Total
December 31, 2022					
Commercial and industrial	$ 216,215	$ 4,022	$ 2,349	$ –	$ 222,586
Commercial real estate	725,255	10,635	2,062	–	737,952
Land and construction	169,945	–	990	–	170,935
Agricultural land, real estate and production	43,807	535	–	–	44,342
Consumer	45,827	–	834	–	46,661
Total	$ 1,201,049	$ 15,192	$ 6,235	$ –	$ 1,222,476

Impaired Loans: Prior to the adoption of CECL under ASU 326 on January 1, 2023, loans were reported as impaired when, based on then current information and events, it was probable we would be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. If a loan was impaired, a specific valuation allowance was allocated, if necessary, so that the loan was reported net, at the present value of estimated future cash flows using the loan's effective interest rate or at the fair value of collateral if repayment was expected solely from the collateral (collateral dependent loans). Interest payments on impaired loans were typically applied to principal unless collectability of the principal amount was reasonably assured, in which case interest was recognized on a cash basis. Impaired loans, or portions thereof, were charged off when deemed uncollectible. The following table shows information related to impaired loans at December 31, 2022:

December 31, 2022	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Land and construction	$ 990	$ 990	$ –	$ 992	$ 21
Consumer	824	834	–	835	27
Total impaired loans without allowance	$ 1,814	$ 1,824	$ –	$ 1,827	$ 48
With an allowance recorded:					
Commercial and industrial	$ 1,526	$ 1,527	$ 1,526	$ 1,553	$ 85
Total impaired loans with allowance established	$ 1,526	$ 1,527	$ 1,526	$ 1,553	$ 85
Total:					
Commercial and industrial	$ 1,526	$ 1,527	$ 1,526	$ 1,553	$ 85
Land and construction	990	990	–	992	21
Consumer	824	834	–	835	27
Total impaired loans	$ 3,340	$ 3,351	$ 1,526	$ 3,380	$ 133

NOTE 4 - FAIR VALUE

Fair Value Hierarchy: Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. We group our assets and liabilities measured at fair value into three levels. Valuations within these levels are based upon:

Level 1 – Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2 – Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

We used the following methods and significant assumptions to estimate fair value:

Cash and Cash Equivalents: The carrying amount of cash and cash equivalents is a reasonable estimate of fair value and are classified as Level 1.

Interest-Bearing Deposits in Other Financial Institutions: The fair values were calculated using discounted cash flow models based on market rates resulting in a Level 2 classification.

Debt Securities: The fair values of debt securities classified as available-for-sale and held-to-maturity are based on quoted market prices, if available (Level 1) at the reporting date. For securities where quoted prices are not available, fair values are calculated based on market prices of similar securities (Level 2), using matrix pricing. Matrix pricing is a mathematical technique commonly used to price debt securities that are not actively traded, values debt securities without relying exclusively on quoted prices for the specific securities but rather relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3).

Loans Held for Sale: Loans held for sale are carried at the lower of cost or fair value, which is evaluated on a pool-level basis. The fair value of loans held for sale is determined using quoted prices for similar assets, adjusted for specific attributes of that loan or other observable market data, such as outstanding commitments from third party investors (Level 2).

Loans: The fair value of loans is determined as the present value of expected future cash flows discounted at the rate that represents current market rates for new origination of comparable loans and included adjustments for interest rate, credit, equity return, servicing and liquidity risk factors, resulting in a Level 3 classification. Loans are grouped according to similar characteristics such as loan type, risk classification, past due status, fixed or variable terms, repricing frequency, amortization and terms. The estimated fair values of financial instruments disclosed below follow the guidance in ASU 2016-01, which prescribes an "exit price" approach in estimating and disclosing fair value of financial instruments.

Accrued Interest Receivable/Payable: The respective carrying values of certain on-balance-sheet financial instruments approximated their fair values. These financial instruments include accrued interest receivable and accrued interest payable. Carrying values were assumed to approximate fair values for these financial instruments as they are short term in nature and their recorded amounts approximate fair values or are receivable or payable on demand. We do not use derivative financial instruments. The carrying amounts of accrued interest approximate their fair value resulting in a Level 2 or Level 3 classification.

Deposits: The fair values of demand deposits, savings deposits, and money market deposits without defined maturities were the amounts payable on demand at the reporting date resulting in a Level 1 classification. For variable rate deposits where we have the contractual right to change rates, carrying value was assumed to approximate fair value resulting in a Level 1 classification. For certificates of deposit with defined maturities, the fair values were calculated using discounted cash flow models based on market interest rates for different product types and maturity dates. The discount rates used were based on rates for comparable deposits resulting in a Level 2 classification.

Assets Recorded at Fair Value: Our assets measured at fair value on a recurring basis as of December 31, 2023 and 2022 are summarized below:

	Fair Value Measurements at December 31, 2023 Using:			
	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3	Total Fair Value
Securities available-for-sale:				
U.S. Treasury bonds	$ -	$ 198,788	$ -	$ 198,788
U.S. Government sponsored agencies	-	12,354	-	12,354
SBA-backed securities	-	10,488	-	10,488
Mortgage-backed securities: residential	-	8,957	-	8,957
Mortgage-backed securities: commercial	-	26,775	-	26,775
Collateralized mortgage obligations	-	57	-	57
State and political subdivision	-	5,147	-	5,147
Total assets measured at fair value	$ -	$ 262,566	$ -	$ 262,566

	Fair Value Measurements at December 31, 2022 Using:			
	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level3	Total Fair Value
Securities available-for-sale:				
U.S. Treasury bonds	$ -	$ 246,964	$ -	$ 246,964
U.S. Government sponsored agencies	-	19,023	-	19,023
SBA-backed securities	-	15,312	-	15,312
Mortgage-backed securities: residential	-	5,813	-	5,813
Mortgage-backed securities: commercial	-	29,621	-	29,621
Collateralized mortgage obligations	-	125	-	125
State and political subdivision	-	3,872	-	3,872
Total assets measured at fair value	$ -	$ 320,730	$ -	$ 320,730

There were no transfers between Level 1 and Level 2 during 2023 and 2022. There were no recurring Level 3 assets or liabilities measured at fair value during 2023 or 2022.

We may be required, from time to time, to measure certain assets at fair value on a non-recurring basis. These include assets that are measured at the lower of cost or market value that were recognized at fair value, which was below cost at the reporting date. There were no assets measured at fair value on a non-recurring basis at year-end 2023 or 2022.

Fair Value of Financial Instruments: The carrying amounts and estimated fair values of financial instruments not carried at fair value, at December 31, 2023 and 2022 are summarized in the table below. Financial instruments specifically excluded from disclosure requirements such as bank-owned life insurance policies, lease obligations and non-maturity deposit liabilities are not included below.

		Fair Value Measurements at December 31, 2023 Using:			
	Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Financial assets:					
Cash and cash equivalents	$ 33,938	$ 33,938	$ -	$ -	$ 33,938
Interest-bearing deposits in other financial institutions	10,457	-	10,123	-	10,123
Debt securities held-to-maturity	7,585	-	1,645	5,697	7,342
Loans held for sale	33,696	-	36,264	-	36,264
Loans, net of allowance	1,353,654	-	-	1,330,952	1,330,952
Accrued interest receivable	8,140	-	1,263	6,877	8,140
Financial liabilities:					
Time deposits	$ 179,612	$ -	$ 178,191	$ -	$ 178,191
Overnight borrowings	32,500	32,500	-	-	32,500
Accrued interest payable	1,044	108	936	-	1,044

		Fair Value Measurements at December 31, 2022 Using:			
	Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Financial assets:					
Cash and cash equivalents	$ 42,693	$ 42,693	$ -	$ -	$ 42,693
Interest-bearing deposits in other financial institutions	34,690	-	34,632	-	34,632
Debt securities held-to-maturity	2,840	-	2,834	-	2,834
Loans held for sale	45,263	-	48,623	-	48,623
Loans, net of allowance	1,201,032	-	-	1,166,982	1,166,982
Accrued interest receivable	6,825	-	1,693	5,132	6,825
Financial liabilities:					
Time deposits	$ 114,128	$ -	$ 111,893	$ -	$ 111,893
Accrued interest payable	240	16	224	-	240

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

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

There were no transfers between Level 1, Level 2, and Level 3 during 2023 or 2022.

NOTE 5 - PREMISES AND EQUIPMENT

The following presents the cost of premises and equipment including leasehold improvements and the related accumulated depreciation and amortization at December 31, 2023 and 2022:

	2023	2022
Land	$ 1,682	$ 2,512
Building	6,390	9,168
Furniture, fixtures and equipment	3,688	3,410
Software and capitalized data & item processing	350	391
Computer equipment	1,378	1,664
Automobile	0	16
Leasehold improvements	3,221	3,284
Construction-in-progress	254	728
Total premises and equipment	16,963	21,173
Less accumulated depreciation and amortization	(5,933)	(6,147)
Premises and equipment, net	$ 11,030	$ 15,026

Depreciation expense was $1,363,000 and $1,002,000 for 2023 and 2022, respectively. During the third quarter of 2023, we sold our vacant property with the associated furniture and equipment and recognized a $255,000 gain.

NOTE 6 - LEASES

Lessee Arrangements: We enter into leases in the normal course of business primarily for branches, back-office operations, and loan production offices. Our leases have remaining terms ranging from 1 to 10 years, some of which include renewal options to extend the lease for up to 5 years. The weighted average lease term at December 31, 2023 is 5.99 years, and the weighted average discount rate used in the calculations is 1.56%. Our leases do not include residual value guarantees or covenants.

We lease certain branch properties and equipment under long-term operating lease agreements. These leases expire on various dates through 2033 and have various renewal options of five years each. Some leases may include a free rent period or have net operating costs associated with them.

We include lease extension options in the lease term if, after considering relevant economic factors, it is reasonably certain we will exercise the option. In addition, we have elected to account for any non-lease components in its real estate leases as part of the associated lease component. We have also elected not to recognize leases with original lease terms of 12 months or less (short-term leases) on our balance sheet.

Leases are classified as operating or finance leases at the lease commencement date. Lease expense for operating leases and short-term leases is recognized on a straight-line basis over the lease term. Right-of-use assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. Right-of-use assets and lease liabilities are recognized at the lease commencement date based on the estimated present value of lease payments over the lease term.

We use the incremental borrowing rate at lease commencement to calculate the present value of lease payments when the rate implicit in a lease is not known. Our incremental borrowing rate is based on the FHLB amortizing advance rate, adjusted for the lease term and other factors.

Right-of-use assets and lease liabilities by lease type, and the associated balance sheet classifications, as follows:

	Balance Sheet Classification	2023	2022
Right-of-use assets:			
Operating leases	Accrued interest receivable and other assets	$ 4,192	$ 4,591
Lease liabilities:			
Operating leases	Accrued interest receivable and other assets	$ 4,424	$ 4,811

Lease Expense: The components of total lease cost were as follows for the period ending:

	2023	2022
Operating lease cost	$ 850	$ 850
Short-term lease cost	-	-
Total lease cost, net	$ 850	$ 850

Lease Obligations: Future undiscounted lease payments for operating leases with initial terms of one year or more as of December 31, 2023 are as follows:

	Operating Leases
2024	$ 803
2025	752
2026	664
2027	473
2028	468
Thereafter	1,785
Total undiscounted lease payments	4,945
Less: imputed interest	(521)
Net lease liabilities	$ 4,424

NOTE 7 - GOODWILL AND INTANGIBLE ASSETS

Business combinations involving our acquisition of the equity interests or net assets of another enterprise give rise to goodwill. Total goodwill at December 31, 2023 and 2022 of $25,762,000 represented the excess of the purchase consideration of Lighthouse Bank over the fair value of assets acquired net of fair value liabilities assumed in the 2019 business combination accounted for under the purchase method of accounting. The value of goodwill is dependent on our ability to generate net earnings after the acquisition and is not deductible for tax purposes. Goodwill is assessed at least quarterly for impairment at the reporting unit level. There was no change or impairment on goodwill in 2023 or 2022.

Other Acquired Intangible Assets: Other acquired intangible assets were as follows for the years ended December 31, 2023 and 2022:

	2023		2022	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets:				
Core deposit intangibles	$ 3,707	$ 2,036	$ 3,707	$ 1,673

The other acquired intangible assets at December 31, 2023 represent the estimated fair value of the core deposit relationships acquired in the acquisition of Lighthouse Bank in 2019 of $3,707,000. Core deposit intangibles are being amortized using a dollar weighted deposit runoff on an annualized basis over an estimated life of ten years from the date of acquisition. At December 31, 2023, the weighted average remaining amortization period is 5.75 years. The carrying value of intangible assets at December 31, 2023 and 2022 was $1,671,000 and $2,034,000, net of accumulated amortization expense. Amortization expense recognized was $363,000 for 2023 and $406,000 for 2022.

The following table summarizes our estimated core deposit intangible amortization expense for each of the next five years:

December 31, 2023	Estimated Core Deposit Intangible Amortization
2024	$ 331
2025	312
2026	293
2027	276
2028	260
Thereafter	199
Total	$ 1,671

NOTE 8 - DEPOSITS

Interest-bearing deposits at December 31, 2023 and 2022, consisted of the following:

	2023	2022
Demand deposit	$ 219,641	$ 246,265
Money market	434,369	363,092
Time deposits $250,000 or more	66,211	66,491
Time deposits less than $250,000	113,401	47,637
Savings	105,012	137,808
Total interest-bearing deposits	$ 938,634	$ 861,293

Aggregate annual maturities of time deposits are as follows:

2024	$ 172,392
2025	2,846
2026	1,239
2027	2,888
2028	247
	$ 179,612

NOTE 9 - BORROWED FUNDS

We have established a secured borrowing arrangement, secured by loans totaling approximately $727,489,000 and $769,380,000 with the Federal Home Loan Bank of San Francisco ("FHLB") as of December 31, 2023 and 2022, respectively. Overnight and term advances are available under the FHLB borrowing arrangement and the credit limit varies according to the amount and composition of the investments and loan portfolios pledged to FHLB as collateral. We had no overnight advances nor any term advances through the FHLB as of December 31, 2023 or 2022.

We also have an available line of credit with the Federal Reserve Bank of San Francisco ("FRB") secured by certain loans totaling approximately $322,052,000 as of December 31, 2023. No borrowings were outstanding from the FRB's discount window or its Bank Term Funding Program at December 31, 2023 or 2022.

At December 31, 2023 and 2022, we had unsecured lines of credit with our correspondent banks in an aggregate amount of $80,000,000 and $71,000,000, respectively. At year-end, correspondent banks offered overnight advances at fixed rates above the federal funds rate ranging from 5.65% to 6.31%, averaging 6.05%. As of December 31, 2023, outstanding amount of overnight borrowing under these lines was $32,500,000.

The following table summarizes our borrowing capacity under various lines of credit and the outstanding borrowings as of December 31, 2023 and 2022:

	2023	2022
Line of credit from the FHLB - collateralized	$ 434,961	$ 354,677
Line of credit from the FRB - collateralized	251,641	–
Lines at correspondent banks – unsecured	80,000	71,000
Total external contingency liquidity capacity	766,602	425,677
Less: overnight borrowings	(32,500)	–
Net available borrowing capacity	$ 734,102	$ 425,677

NOTE 10 - PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS

We established the Supplemental Executive Retirement Plan, an unfunded noncontributory defined benefit pension plan, to provide supplemental retirement benefits to a select group of key executives and senior officers. We use December 31 as the measurement date for this plan.

The following table reflects the changes in obligations and plan assets of the defined benefit pension plan as of December 31, 2023 and 2022:

	2023	2022
Change in benefit obligation:		
Beginning benefit obligation	$ 3,573	$ 4,230
Service cost	258	381
Interest cost	166	99
Actuarial (gain) loss	(158)	(984)
Benefits paid	(186)	(153)
Ending benefit obligation	3,653	3,573
Change in plan assets:		
Beginning plan assets	–	–
Employer contributions	186	153
Benefits paid	(186)	(153)
Ending plan assets	–	–
Funded status at end of year	$ (3,653)	$ (3,573)

Amounts recognized in accumulated other comprehensive income at December 31 consist of:

	2023	2022
Change in benefit obligation:		
Unrecognized net actuarial (gain) loss	$ (1,058)	$ (978)
Unrecognized prior service cost	–	–
	$ (1,058)	$ (978)

The following components of net periodic benefit cost, other than the service cost component, are included in the line item “other noninterest expense” in the income statement:

Components of net periodic benefit cost	2023	2022
Service cost	$ 258	$ 381
Interest cost	166	99
Amortization of prior service cost	–	–
Amortization of unrecognized actuarial gains	(78)	–
Net periodic benefit cost	$ 346	$ 480

	2023	2022
Net gain	$ (158)	$ (984)
Amortization of gain	78	–
Amortization of prior service cost	–	–
Total recognized in other comprehensive income	(80)	(984)
Total recognized in net periodic benefit cost and other comprehensive (income) loss	$ (266)	$ (504)

Assumptions: Weighted average assumptions used to determine pension benefit obligations and net periodic pension cost at December 31:

	2023	2022
Discount rate used to determine net periodic benefit cost	4.78%	2.38%
Discount rate used to determine benefit obligations	5.18%	4.78%
Future salary increases	N/A	N/A

NOTE 11 - EMPLOYEE BENEFIT PLANS

401(k) Plan: All employees are eligible to participate in our 401(k) benefit plan, which is a tax-deferred savings plan designed to assist employees in preparing for their retirement years. The 401(k) Plan allows employees to contribute to the plan up to certain limits prescribed by the Internal Revenue Service. We match 30% of contributions up to 6% of compensation. Total expense for the years ended December 31, 2023 and 2022 was $368,000 and $305,000, respectively.

Split-Dollar Life Insurance: We account for split-dollar life insurance in accordance with ASC 715-60, Compensation – Non-retirement Post-employment Benefits, which requires that endorsement split-dollar life insurance arrangements which provide a post-retirement benefit to an employee be recorded based on the substance of the agreement with the employee. When we effectively agreed to maintain a life insurance policy during the covered employees' retirement, the present value of the cost of future premiums of insurance policy during post-retirement is accrued. The total liability recorded as of December 31, 2023 and 2022 was $1,311,000 and $1,336,000, respectively. Total gain recognized for the years ended December 31, 2023 and 2022 was $25,000 and $319,000, respectively.

NOTE 12 - INCOME TAXES

The provision for income taxes is as follows for the years ended December 31, 2023 and 2022:

	2023	2022
Current expense:		
Federal	$ 9,168	$ 8,145
State	5,312	4,993
Total current	14,480	13,138
Deferred expense (benefit):		
Federal	106	(98)
State	34	(225)
Total deferred	140	(323)
Total provision for income taxes	$ 14,620	$ 12,815

The effective tax rates differ from the federal statutory rate of 21% for 2023 and 2022 applied to income before income taxes due to the following:

	2023	2022
Federal statutory rate	21.00%	21.00%
State income tax, net of federal effect	8.46%	8.63%
Tax exempt interest	(0.26%)	(0.30%)
Bank owned life insurance	(0.19%)	(0.21%)
Split dollar expense	(0.01%)	(0.15%)
Stock-based compensation	0.15%	0.13%
Other	0.22%	0.18%
Total	29.37%	29.28%

Deferred income taxes are the result of differences between income tax accounting and accounting principles generally accepted in the United States of America, with respect to income and expense recognition. The net deferred taxes are reported in Accrued Interest Receivable and Other Assets in the Balance Sheets as of December 31, 2023 and 2022.The tax effects of temporary differences that gave rise to deferred tax assets and deferred tax liabilities at December 31, 2023 and 2022 are as follows:

	2023	2022
Deferred tax assets:		
Allowance for credit losses	$ 7,078	$ 6,340
Deferred compensation	1,393	1,345
Accrued expenses	633	739
State income tax	1,115	1,007
Fair value adjustment on loans and deposits	98	415
Lease liability	1,308	1,422
Unrealized losses on available-for-sale securities	4,436	7,085
Other deferred tax assets	632	188
Gross deferred tax assets	16,693	18,541
Deferred tax liabilities:		
Deferred loan costs	(1,994)	(2,354)
Core deposit intangibles	(494)	(601)
Premises and equipment	(948)	(880)
Right-of-use asset	(1,239)	(1,357)
Other deferred tax liabilities	(169)	(83)
Unrealized gain on pension	(313)	(289)
Gross deferred tax liabilities	(5,157)	(5,564)
Net deferred tax asset	$ 11,536	$ 12,977

Management believes that it is more likely than not, that the deferred tax assets will be realized as a result of expected continued profitability. Accordingly, no valuation allowance has been established as of December 31, 2023 or 2022.

The Bancorp and the Bank have entered into a tax allocation agreement, which provides that income taxes shall be allocated between the parties on a separate entity basis. The intent of this agreement is that each member of the consolidated group will incur no greater tax liability than it would have incurred on a stand-alone basis.

We have no material unrecognized tax benefits at December 31, 2023 or 2022 and do not expect the total amount of unrecognized tax benefits to significantly increase or decrease within the next twelve months. The total amount of interest and penalties recorded in the income statement for the year ended December 31, 2023 was $1,000. The amounts accrued for interest and penalties at December 31, 2022 was $28,000.

We are subject to U.S. Federal income tax as well as income tax of the states of California and Oregon. We are no longer subject to examination by taxing authorities for years before 2020 and 2019, for federal, California, and Oregon purposes.

NOTE 13 - RELATED PARTY TRANSACTIONS

Loan related activity to principal officers, directors, and their affiliates during 2023 and 2022 were as follows:

	2023	2022
Beginning balance	$ 17,600	$ 27,428
New loans or disbursements	8,453	3,093
Changes in borrower status	(6,394)	(10,250)
Principal repayments	(1,831)	(2,671)
Ending balance	$ 17,828	$ 17,600

At December 31, 2023 and 2022, no related party loans were on nonaccrual status or classified for regulatory reporting purposes. Deposits from principal officers, directors, and their affiliates at December 31, 2023 and 2022 were $9,003,000 and $7,225,000, respectively.

We solicited services from a member of our Board of Directors for legal services and incurred legal expenses of $41,000 and $8,000 in 2023 and 2022, respectively.

NOTE 14 - STOCK-BASED COMPENSATION

We have two share-based compensation plans as described below. Total compensation cost that has been charged against income for those plans was $554,000 and $583,000 for December 31, 2023 and 2022, respectively. The total income tax benefit was $93,491 and ($2,200) for December 31, 2023 and 2022, respectively.

We estimate the fair value of each option award as of the date of grant using a closed form option valuation (Black-Scholes-Merton) model and the following assumptions. Expected volatilities are based on historical volatilities of our common stock commensurate with the expected term of the option. The "simplified" method described in the Securities and Exchange Commission's Staff Accounting Bulletin No. 110 is used to determine the expected term of the options due to the lack of sufficient historical data. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant with substantially the same term as the expected term of the option.

The fair value of options granted was determined using the following weighted average assumptions as of grant date.

	2023	2022
Risk-free interest rate	4.41%	2.93%
Expected term (yrs.)	6.25	5.44
Expected stock price volatility	31.43%	36.27%
Dividend yield	2.40%	1.60%

2003 Stock Option Plan: We adopted a qualified stock option plan (the "Option Plan") for employees, non-employee directors and Bank founders, under which a maximum of 1,000,404 shares of common stock was available be issued. The Option Plan calls for the exercise prices of the options to be equal to or greater than the fair market value of the stock at the time of grant. Options granted to Bank founders who are not also Bank directors or Bank officers were fully vested upon the date of grant. All other options granted have daily vesting over the first four years of the option contract. All director and employee option contracts have expiration dates on the earlier of termination of service or 10 years from the date of grant. The Option Plan expired during 2014 and was replaced with the 2014 Omnibus Plan (the "Omnibus Plan").

All options granted under the Option Plan have a 10-year term and have been issued with exercise prices at the fair market value of the underlying shares at the date of grant. The non-qualified stock option awards to the organizers vested 100% immediately, whereas regular stock option awards to directors and employees vest over a four-year period from the date the options were granted.

The following is a summary of the activity relating to the Option Plan for 2023 as presented below:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Options outstanding at beginning of year	320	$ 7.09		
Granted	–	–		
Exercised	(320)	7.09		
Expired	–	–		
Forfeited	–	–		
Options outstanding at end of year	–	$ –	0 years	$ –
Options fully vested and expected to vest	–			$ –
Exercisable at end of year	–	$ –	0 years	$ –

Information related to the stock option plan during each year follows:

	2023	2022
Intrinsic value of options exercised	$ 6	$ 18
Cash received from option exercises	$ 2	$ 7
Tax benefit realized from option exercises	$ –	$ –
Weighted average fair value of options granted	–	–

As of December 31, 2023, there was no unrecognized compensation cost related to non-vested stock options granted under the Option Plan. All shares issued under this plan fully vested during the year 2016.

2014 Omnibus Plan: We adopted the Omnibus Plan in May 2014 for employees and non-employee directors, which will continue in effect until February 19, 2024. The Omnibus Plan allows qualified stock option grants for employees and non-qualified restricted stock awards for officers and non-employee directors. The maximum number of shares of common stock that may be issued under this plan is 939,940 and 444,399 shares were available when the plan expired in February 2024. The Omnibus Plan was replaced with the 2024 Equity Based Compensation Plan.

The Omnibus Plan permits the grant of non-statutory options, incentive stock options and restricted stock awards to our directors and employees. Options granted under the Omnibus Plan may be incentive stock options or non-statutory stock options, as determined by the plan administrator at the time of grant of an option, however incentive stock options may be granted only to employees. In addition, restricted stock awards may be granted under the Omnibus Plan to directors and employees. On October 19, 2021, we declared a 10% stock dividend for shareholders of record as of November 8, 2021. Stock option awards and the related price per share amounts reflected in the table below have been restated to give retroactive effect to the 10% stock dividend declared in October 2021.

Stock Options: The per share exercise price for the shares to be issued upon exercise of any option shall be such price as is determined by the plan administrator, but no less than 100 percent of the fair market value per share on the date of grant. All option contracts have expiration dates on the earlier of termination of service or 10 years from the date of grant.

The following is a summary of the activity relating to the Omnibus Plan for 2023 as presented below:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Options outstanding at beginning of year	316,664	$ 20.43		
Granted	35,000	23.50		
Exercised	(22,392)	16.91		
Expired	(4,998)	21.32		
Forfeited	(11,102)	19.50		
Options outstanding at end of year	313,172	$ 21.43	6.73 years	$ 2,303
Options fully vested and expected to vest	221,155			$ 2,303
Exercisable at end of year	191,505	$ 20.62	6.13 years	$ 1,741

Information related to the stock option plan during each year follows:

	2023	2022
Intrinsic value of options exercised	$ 355	$ 102
Cash received from option exercises	$ 241	$ 211
Tax benefit realized from option exercises	$ 10	$ (5)
Weighted average fair value of options granted	$ 7.65	$ 8.21

As of December 31, 2023, there was $707,000 of total unrecognized compensation cost related to non-vested stock options granted under the plan. The cost is expected to be recognized over a weighted average period of 2.56 years.

Restricted Stock Awards: The following is a summary of the activity relating to non-vested shares under this plan for the year ended December 31, 2023 as presented below:

	Shares	Weighted Average Grant Date Fair Value
Non-vested awards at January 1, 2023	7,485	$ 22.86
Granted	27,775	$ 27.78
Vested	(11,226)	$ 24.81
Non-vested awards at December 31, 2023	24,034	$ 27.63

As of December 31, 2023, there was $618,000 in unrecognized compensation cost related to non-vested shares granted under the Omnibus Plan. The cost is expected to be recognized over a weighted average period of 4.06 years. The total fair value of shares vested during the years ended December 31, 2023 and 2022 was $284,000 and $247,000, respectively.

NOTE 15 - REGULATORY CAPITAL MATTERS

Regulatory Capital: We are subject to various regulatory capital adequacy requirements administered by the banking regulatory agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if not undertaken, would have a direct material effect on our financial statements. Management believes as of December 31, 2023, the Bank and Bancorp meet all capital adequacy requirements to which they are subject.

Prompt corrective action regulations define five classifications for regulated banks: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At December 31, 2023 and 2022, the most recent regulatory notifications categorized us well-capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the institution’s category.

The Board of Governors of the Federal Reserve also set regulatory capital requirements for bank holding companies like the Bancorp that generally follow similar minimum requirements set for banks for capital adequacy. However, the Federal Reserve also maintains a Small Bank Holding Company Policy Statement that generally applies to holding companies with less than $3.0 billion in assets and with non-complex operations. One element of this policy is that such holding companies are not subject to separate capital measurements and instead the Federal Reserve looks through the holding company to the bank level capital ratios. The Bancorp qualifies for the Policy Statement and currently is not subject to separate capital ratio measurements. Nevertheless, the following table shows the Bancorp’s capital ratios as if it were subject to separate capital measurement.

Actual and required capital amounts and ratios are presented below at December 31, 2023 and 2022 for both the Bank and Bancorp.

Capital Ratios for Bancorp	Actual		Required for Capital Adequacy Purposes including the Capital Conservation Buffer		To Be Well-Capitalized for the Bank Holding Company	
As of December 31, 2023						
Total capital to risk weighted assets	$ 231,856	14.98%	$ 162,545	10.50%	$ 154,805	10.00%
Tier 1 (Core) capital to risk weighted assets	$ 212,427	13.72%	$ 131,584	8.50%	$ 123,844	8.00%
Common Tier 1 (CET1) to risk weighted assets	$ 212,427	13.72%	$ 108,363	7.00%	$ 100,623	6.50%
Tier 1 (Core) capital to average assets	$ 212,427	12.09%	$ 70,271	4.00%	$ 87,838	5.00%

Capital Ratios for the Bank	Actual		Required for Capital Adequacy Purposes including the Capital Conservation Buffer		To Be Well-Capitalized Under Prompt Corrective Action Regulations	
As of December 31, 2023						
Total capital to risk weighted assets	$ 231,419	14.95%	$ 162,545	10.50%	$ 154,805	10.00%
Tier 1 (Core) capital to risk weighted assets	$ 211,990	13.69%	$ 131,584	8.50%	$ 123,844	8.00%
Common Tier 1 (CET1) to risk weighted assets	$ 211,990	13.69%	$ 108,363	7.00%	$ 100,623	6.50%
Tier 1 (Core) capital to average assets	$ 211,990	12.07%	$ 70,271	4.00%	$ 87,838	5.00%
As of December 31, 2022						
Total capital to risk weighted assets	$ 203,119	14.94%	$ 142,699	10.50%	$ 135,904	10.00%
Tier 1 (Core) capital to risk weighted assets	$ 186,071	13.69%	$ 115,519	8.50%	$ 108,723	8.00%
Common Tier 1 (CET1) to risk weighted assets	$ 186,071	13.69%	$ 95,133	7.00%	$ 88,338	6.50%
Tier 1 (Core) capital to average assets	$ 186,071	10.39%	$ 71,622	4.00%	$ 89,527	5.00%

Dividend Restrictions: The Board of Directors may, to the extent of such earnings and our net capital requirements and subject to the provisions of the California Financial Code, declare and pay a portion of such earnings to its shareholders as dividends. No cash dividend will be declared without a complete analysis of capital impact, current economic assessment, and current risk analysis.

Under the California Financial Code, payment of dividends by the Bank to the Bancorp without advance regulatory approval is restricted to the lesser of retained earnings or the amount of undistributed net profits of the Bank from the three most recent fiscal years. Under this restriction, approximately $85,667,000 of the Bank’s retained earnings balance was available for payment of dividends to the Bancorp as of December 31, 2023. The Bancorp received $1,830,000 in cash dividends from the Bank during fiscal year 2023.

Under the California Corporations Code, payment of dividends by the Bancorp to its shareholders is restricted to the amount of retained earnings immediately prior to the distribution or the amount of assets that exceeds the total liabilities immediately after the distribution. As of December 31, 2023, the Bancorp's retained earnings and amount of total assets that exceeds total liabilities were $117,263,000 and $230,036,000, respectively.

NOTE 16 - LOAN COMMITMENTS AND OTHER RELATED ACTIVITIES

Correspondent Banking: At times, we maintain deposit amounts at corresponding banks that exceed federally insured limits. Uninsured deposits totaled $14,382,000 and $8,952,000 at December 31, 2023 and 2022, respectively. We have not experienced any losses on amounts exceeding the insured limits.

Financial Investments with Off-Balance Sheet Exposure: In the normal course of business to meet the financing needs of our customers, we enter into various financial arrangements where the financial instruments are not recorded in our consolidated balance sheet. These financial instruments include commitments to extend credit, standby letters of credit, overdraft protection and financial guarantees. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheets. The contract amounts of those instruments reflect the extent of involvement we have in particular classes of financial instruments.

Our exposure to credit loss in the event of nonperformance by the other party for commitments to extend credit, standby letters of credit, and financial guarantees is represented by the contractual amount of those instruments. We use the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

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. We evaluate each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if we deemed necessary upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include cash, securities, accounts receivable, inventory, property, plant and equipment, residential real estate and income-producing commercial properties.

Standby letters of credit and financial guarantees written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

The contractual amounts of financial instruments with off-balance-sheet exposure as of December 31, 2023 and 2022 were as follows:

	December 31, 2023		December 31, 2022	
	Fixed Rate	Variable Rate	Fixed Rate	Variable Rate
Commitments to make loans	$ 15,994	$ 391,542	$ 4,112	$ 342,045
Unused lines of credit	503	68,218	496	57,618
Standby letters of credit	–	–	–	–
	$ 16,497	$ 459,760	$ 4,608	$ 399,663

Commitments to make loans are generally made for periods of 90 days or less.

NOTE 17 - EARNINGS PER SHARE

The factors used in the earnings per share computation follow:

	2023	2022
Basic earnings per share:		
Net income	$ 35,150	$ 30,944
Weighted average common shares outstanding	8,396,566	8,513,839
Basic earnings per common share	$ 4.19	$ 3.63
Diluted earnings per share:		
Net income	$ 35,150	$ 30,944
Weighted average common shares outstanding for basic earnings per common share	8,396,566	8,513,839
Add: Dilutive effects of assumed exercises of stock options	35,295	25,252
Weighted average outstanding and dilutive potential common shares	8,431,861	8,539,091
Diluted earnings per common share	$ 4.17	$ 3.62

Stock options for 112,000 and 164,000 shares of common stock were not considered in computing diluted earnings per common share as of December 31, 2023 and 2022, respectively, because they were anti-dilutive.

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