SANTA CRUZ COUNTY BANK

2020 ANNUAL REPORT

SANTA CRUZ COUNTY BANK

OUR MISSION

WE ARE COMMITTED TO OUR COMMUNITY
by building lasting relationships and being a trusted partner that together empowers growth, economic vitality, and community well-being.

Expanding to Meet our Clients

In 2020, we announced a new full-service office in Monterey and purchased a building on a high-traffic downtown corner. The new office has been beautifully remodeled inside and out. We opened for business in January 2021. Our staff of well-known, highly-experienced bankers will support our long-standing clients in the Monterey/Salinas region while developing new relationships in the region's diverse marketplace.

This region is familiar to us over many years of working with area clients and building long term relationships. Over nearly two decades, we have grown our presence in the Salinas/Monterey region as the result of natural progression to serve our many clients: farmers, growers and businesses whose operations span across several contiguous counties.

At Santa Cruz County Bank, we are proud to be a local community bank. We believe a region as unique as ours deserves an equally unique approach to banking.

With this in mind, the first Santa Cruz County Bank branch was opened in 2004 to serve the needs of Santa Cruz County businesses and individuals. Locally owned and operated, our bank has enjoyed success, thanks to our outstanding employees, our ever-growing suite of banking services, our relationship banking professionals, and of course, our loyal clients and customers.

Any bank can lend you money. Our unique advantage is in building relationships. We can provide our clients with informed and creative financial solutions, based on the details of their current situation and our understanding of their future plans.

As a community bank, we are motivated to help local businesses succeed.

Bottom line, we make loans when other banks make excuses. That's the beauty of working with Santa Cruz County Bank. Chalk it up to local knowledge and the entrepreneurial spirit that inspired us to start up a new bank in the first place.

We offer all the conveniences of remote banking from wherever you are, but we're always pleased when customers visit one of our branches to make a deposit, make a withdrawal, or simply to say hello.

APTOS
7775 Soquel Drive

CAPITOLA
819 Bay Avenue

CUPERTINO
19240 Stevens Creek Blvd.

MONTEREY
584 Munras Avenue

SANTA CRUZ
75 River Street
2020 N. Pacific Avenue

SCOTTS VALLEY
4604 Scotts Valley Drive

WATSONVILLE
595 Auto Center Drive

2020 RANKINGS & RECOGNITION

FINANCIAL PERFORMANCE

- Total assets over $1.4 billion
- Total deposits of $1.2 billion
- Net income exceeded $17 million
- Ranked 4th in overall deposit market share in Santa Cruz County
- Ranked 15th in overall deposit market share in Silicon Valley — *Silicon Valley Business Journal*

NATIONAL RECOGNITION

- Ranked 19th in *Independent Community Bankers of America's* Top Commercial Lenders
- *S & P Global* — Ranked in the Top 100 Community Banks in the nation for banks under $3 billion in assets
- Rated 5-Star "Superior" by *Bauer Financial* for every quarter in 2020

CALIFORNIA RECOGNITION

- Ranked in the "Top 10 Banks in California" for overall financial performance by *Financial Management Consulting Group*, 6th year
- Named a *Super Premier Performing Bank* by *Findley Reports*, 11th year

SBA LENDING 2020 FISCAL YEAR

- SBA Rank Silicon Valley — 11th by number of loans
- SBA Rank SF District — 10th by dollar amount

REGIONAL AWARDS AND RECOGNITION

- *Best Bank* in Santa Cruz County — *Good Times* "Best Of" Readers' Poll, 9th year
- *Best Bank* in Santa Cruz County — *Santa Cruz Sentinel* Readers' Choice, 6th year
- *Favorite Bank* in Santa Cruz County — *Santa Cruz Waves* magazine, Swellies Awards, 4th year
- *Platinum Award* — *Second Harvest Food Bank*

Dear Shareholders,

I am pleased to present the Bank's 2020 financial performance and report on our tenth consecutive year of record earnings and growth.

2020 — Our tenth successive record year.

As presented in the financial statements, we achieved record earnings and growth for the tenth consecutive year while reaching numerous financial milestones. In 2020 we recorded net income of $17.5 million or $4.56 earnings per share. Book value per share of common stock at year-end was $43.74, an 11% ($4.49) increase over 2019.

Our loan production through our SBA department continues to grow and rank us amongst the major national banks. For the 2020 fiscal year, we ranked 11th in the number of SBA loans generated in Silicon Valley, a region that spans throughout Santa Cruz, San Mateo and Santa Clara counties.

2020 will be remembered as one of the most challenging years for our Central Coast region due to the health and economic devastation of the Covid-19 Pandemic. The true value of community banking shines even brighter during times of crisis and Santa Cruz County Bank was a bright star. Community banks are part of the critical infrastructure that must continue operations while keeping the health of their customers and employees a priority. The pandemic was coupled with some of the worst wildfires in our state's history, the largest of which ravaged forests and homes in Santa Cruz, Santa Clara and Monterey counties — all within our market area.

When wildfires raged out of control and evacuations displaced one third of our workforce, Santa Cruz County Bank's team sprang into action donating clothing, housing and financial assistance through the Employee Wildfire Relief fund. In addition, the Bank made significant contributions to the Community Foundation's Covid-19 Relief Fund to help local families in need during this crisis and continued to support nonprofit organizations struggling to keep their doors open.

When the Paycheck Protection Program was established to help businesses survive the lockdowns it was all hands on deck at Santa Cruz County Bank. By the deadline, we completed three years worth of loan production in under two weeks. When PPP loans were awarded, we had secured funds for thousands of local businesses. Their doors remained opened and 36,000 of our community members remained employed. This was and continues to be your community bank at its best, caring for and supporting our business community and our neighbors

This past year we announced the retirement of our long-standing President and CEO David Heald. David served as our President and CEO for the past fourteen years as well as a Director of the Bank. David, while at the helm, navigated Santa Cruz County Bank through several unprecedented challenges including the collapse of the real estate market in 2008 and the ongoing Covid-19 Pandemic. David's leadership elevated Santa Cruz County Bank as a top performer among the nation's community banks. Our bank will continue to benefit from David's unique perspective and leadership. We wish David and his family the best in this new chapter of his life.

Looking ahead — 2021 Expansion and New Leadership

In January 2021 we opened our eighth full-service banking office in Monterey at 584 Munras Avenue. The Monterey branch has already exceeded expectations for loan and deposit growth as well as our goals for new business relationships.

On March 1, 2021 our Board and entire team welcomed Krista Snelling as President and CEO of Santa Cruz County Bank. Ms. Snelling brings over 25 years of strategic financial and operational expertise to the Bank. We look forward to continuing to execute on our strategic plan and community involvement under Krista's skilled leadership.

On behalf of the Board of Directors of Santa Cruz County Bank, I thank you, our clients, customers, community and shareholders for your ongoing loyalty, trust and support of community banking.

William J. Hansen
Chairman of the Board

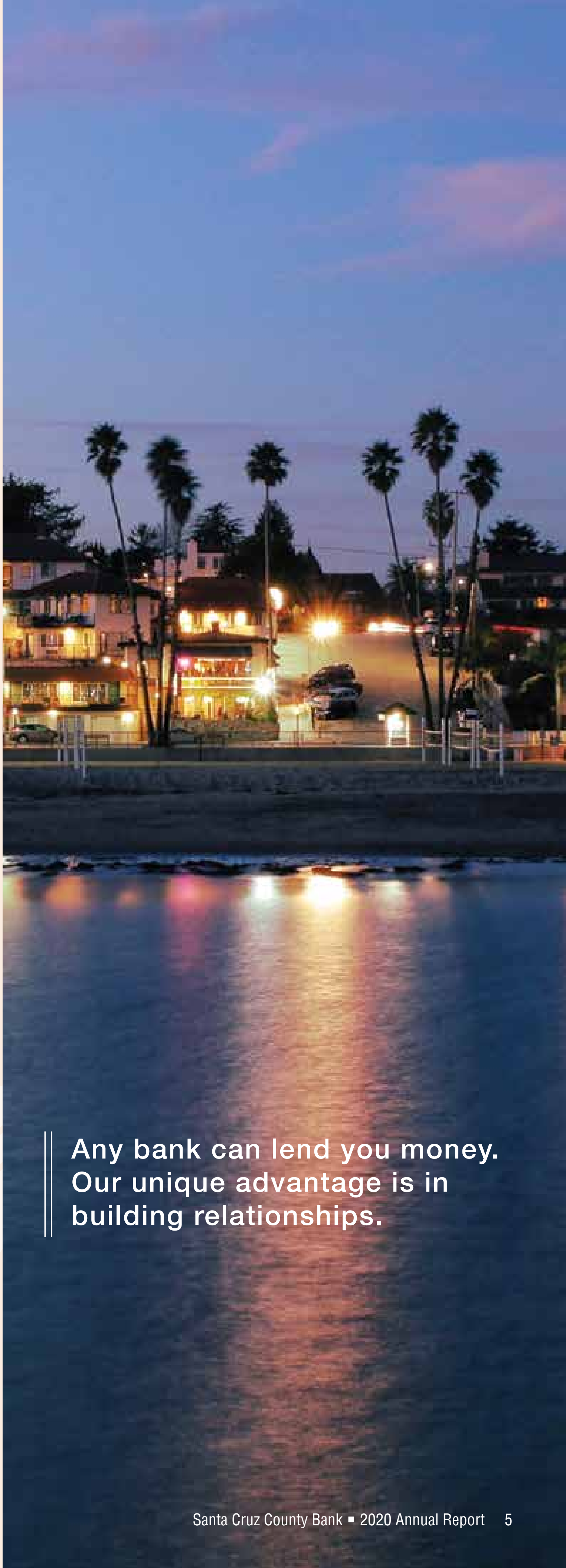
As your new President and CEO, I am humbled and inspired by the opportunity to be an integral part of this wonderful, top performing financial institution. I have followed and respected Santa Cruz County Bank for many years. I look forward to applying the experience I have gained throughout my career to build upon the Bank's legacy and to advance the positive presence of Santa Cruz County Bank in the Monterey Bay and Silicon Valley markets.

In hindsight, Santa Cruz County Bank accomplished some extremely important milestones in 2020. Together, channeling the strength and resiliency of our amazing employees and members of the communities we serve, we look forward to a brighter 2021. We are committed to making a positive impact on the communities we serve and helping lead the way to economic recovery in the months and years ahead.

Sincerely,

Krista Snelling

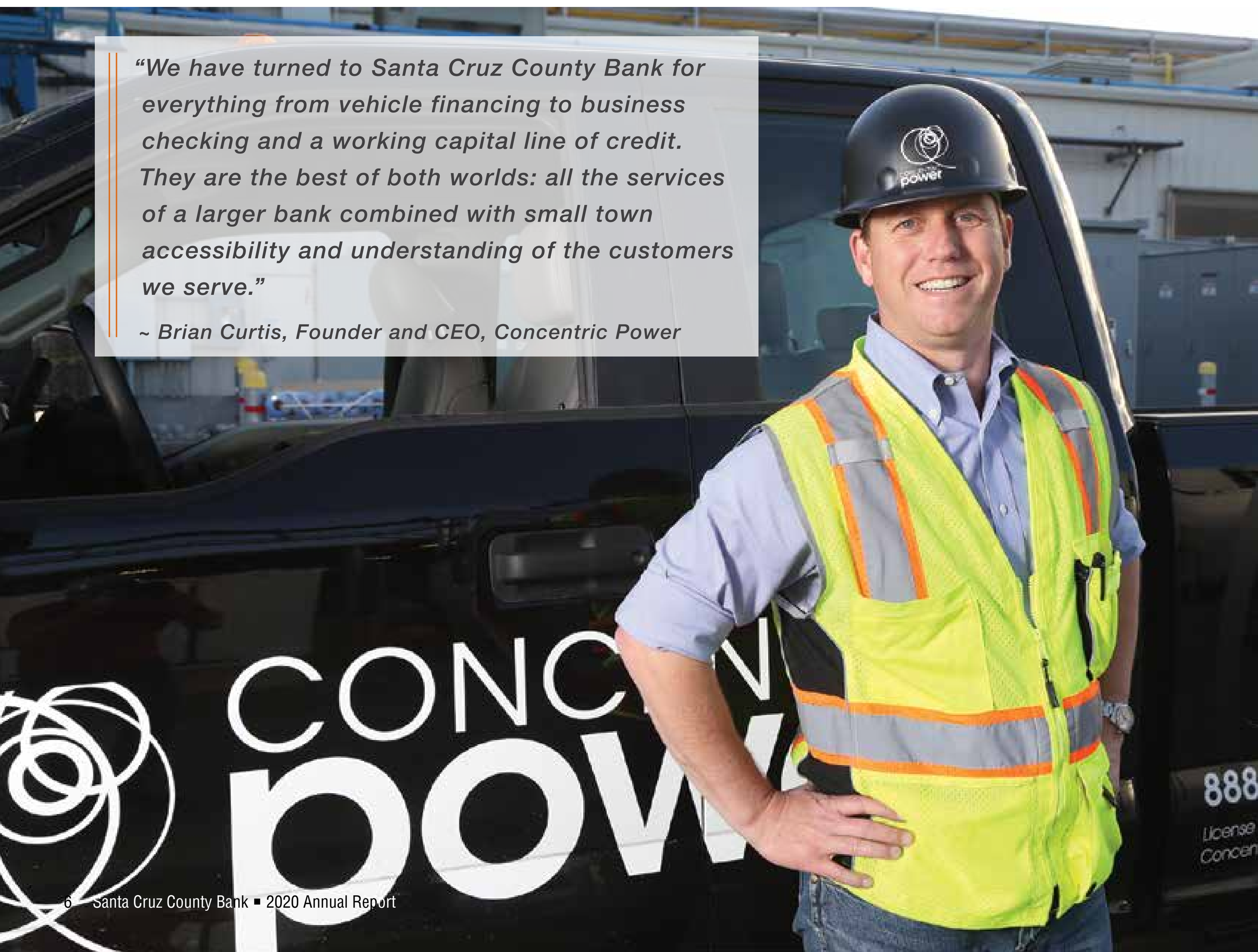
Krista Snelling
President and CEO



OUR CUSTOMERS SAY IT BEST

"The Don Chapin Company is pleased to have a strong relationship with Santa Cruz County Bank. They are a leader in understanding local businesses and our local economy. We give SCCB the highest rating for their commitment to our community, their timely responses, and their great customer service. SCCB truly understands the needs of those who live, work and play here."

~ Don Chapin Jr., President, Don Chapin Company, Inc.

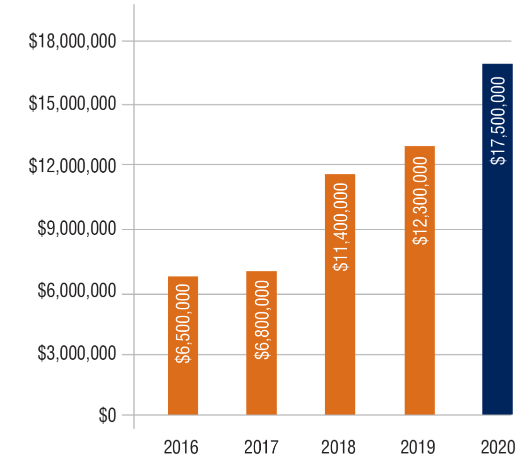


"We have turned to Santa Cruz County Bank for everything from vehicle financing to business checking and a working capital line of credit. They are the best of both worlds: all the services of a larger bank combined with small town accessibility and understanding of the customers we serve."

~ Brian Curtis, Founder and CEO, Concentric Power

FIVE YEAR HISTORICAL PERFORMANCE

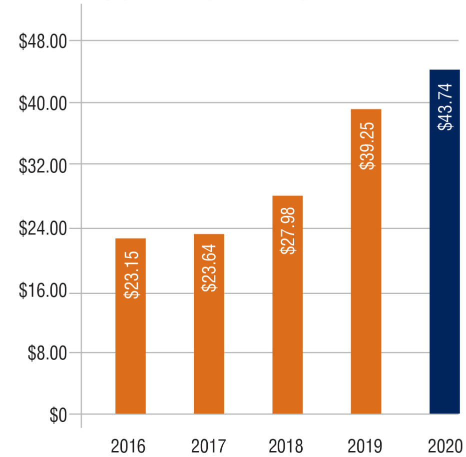
NET INCOME



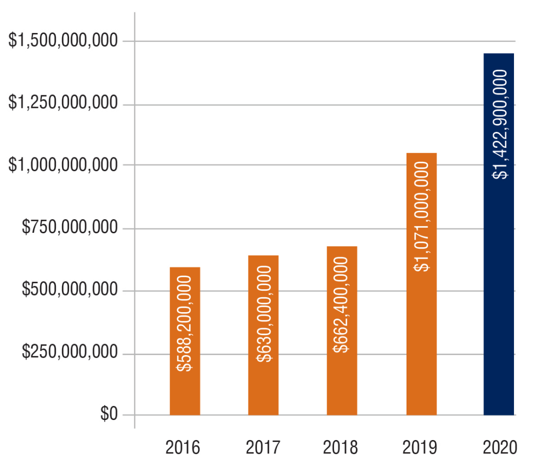
NET INCOME	$6,500,000	$6,800,000	$11,400,000	$12,300,000	$17,500,000
WACSO*	2,396,136	2,412,333	2,432,290	2,719,384	3,850,783
BASIC EARNINGS PER SHARE	$2.98	$2.80	$4.68	$4.51	$4.56

**Note: Weighted average common shares outstanding (basic).*
Lighthouse Bank merger closing date was October 18, 2019.

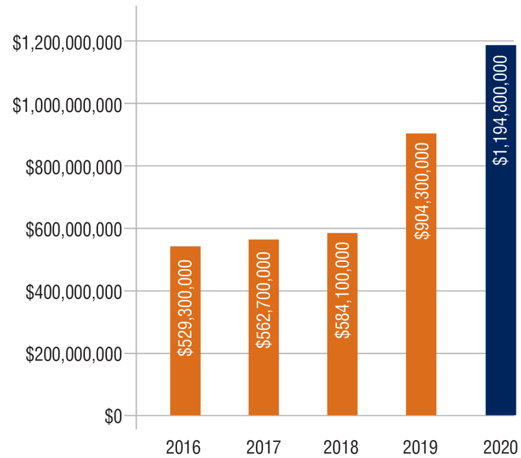
BOOK VALUE PER SHARE



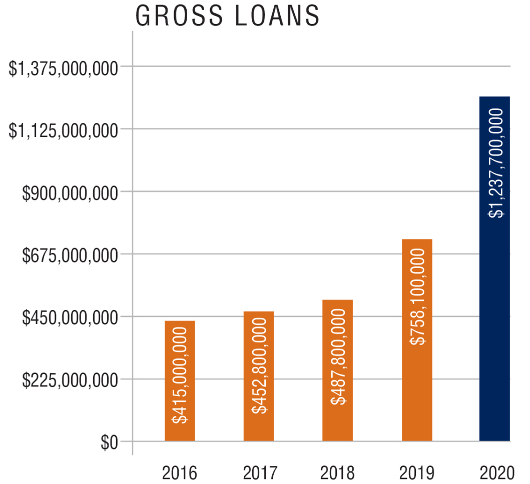
TOTAL ASSETS



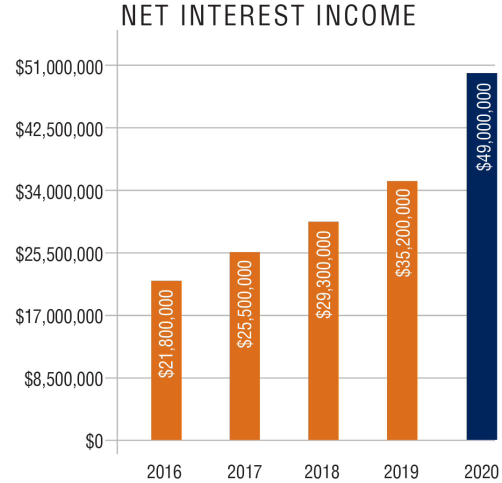
TOTAL DEPOSITS



GROSS LOANS



NET INTEREST INCOME

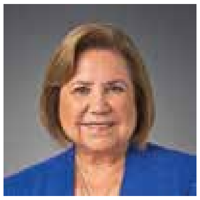


All numbers rounded to the nearest $100,000.

BOARD OF DIRECTORS

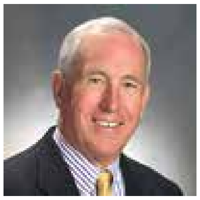
William J. Hansen
Chairman

John C. Burroughs
Vice Chairman



Tila Bañuelos

Kenneth R. Chappell



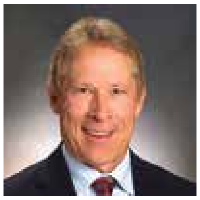
Craig French

George R. Gallucci
Former Founding Chairman

Thomas N. Griffin

Stephen D. Pahl

Krista Snelling
President and CEO Joined March 2021

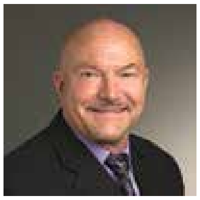


James L. Weisenstein

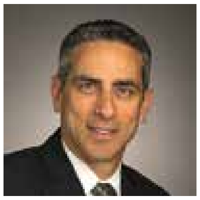
BANK MANAGEMENT TEAM

Krista Snelling
President and CEO Joined March 2021

Frederick L. Caiocca
EVP Regional Credit Manager



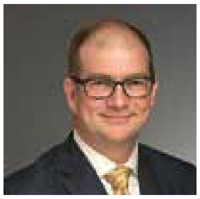
Vic Davis
EVP Chief Financial Officer & Cashier



Angelo DeBernardo, Jr.
EVP Chief Lending Officer

Heather La Fontaine
EVP Chief Administrative Officer

Jaime Manriquez
EVP CIO-CISO, Information Technology & Security



Creedence Shaw
EVP Chief Credit Officer

Jon P. Sisk
EVP Regional President

Mary Anne Carson
SVP Chief Marketing Officer

Susan Chandler
SVP SBA Department Manager

Douglas Fischer
SVP Relationship Manager

Tracy Ruelas-Hashimoto
SVP Assistant Chief Financial Officer

BANK FOUNDERS

A group of local business people joined to create a local, community bank focused on serving the residents and businesses of Santa Cruz County when it became apparent that the last of the local independent banks was soon to be taken over by a large out-of-area bank holding company. This group that we recognize as Founders all contributed time, money, and talent, not only to the Bank's organizing effort, but continue to be involved and support our Bank as customers, referring family, friends and business contacts, and serving as ambassadors of the Bank in our community.

Richard Alderson ▪ Joseph Anzalone[t] ▪ Tila Bañuelos* ▪ Victor Bogard ▪ Anthony & Rebecca Campos

Charles Canfield ▪ Kenneth R. Chappell* ▪ Kate & Fred Chen ▪ Marshall Delk ▪ George R. Gallucci*

Thomas N. Griffin* ▪ William J. Hansen* ▪ David V. Heald ▪ Mark Holcomb[t] ▪ Steven G. John****

Mateo Lettunich ▪ Robert Lockwood ▪ William Moncovich ▪ Stuart Mumm ▪ George Ow, Jr.

Louis Rittenhouse ▪ Frank Saveria ▪ Robert[t] & Bjorg Yonts

**denotes Bank Director **denotes former Bank Director t denotes deceased*

STOCK INFORMATION

Santa Cruz County Bank stock is publicly traded on the OTC marketplace under the stock symbol SCZC. Stock purchase orders may be placed through a brokerage firm or one of the Market Makers listed below.

D.A. Davidson & Co.
42605 Moonridge Road
Big Bear Lake, CA 92315
800.288.2811
Katy Ehlers
Michael Natzic

Monroe Financial Partners
100 North Riverside Plaza, Suite 1620
Chicago, IL 60606
312.506.8743
Steve Schroeder, CFA

Raymond James & Associates
One Embarcadero Center, Suite 650
San Francisco, CA 94111
888.317.8986
John Cavender

StockCross Financial Services, Inc. Equity Trading
15 Exchange Place, Suite 615
Jersey City, NJ 07302
800.993.2075
Tim Padala

Wedbush Securities
One SW Columbia Street, Suite 1000
Portland, OR 97258
866.662.0351
Joey Warmenhoven

SHAREHOLDER INFORMATION

Shareholders with questions regarding their account, stock transfers and registration, lost certificates or change of address should contact their broker, or if held directly, contact the Bank's transfer agent listed below:

Computershare Investor Services
P.O. Box 30170,
College Station, TX 77842-3170
800.962.4284 ▪ computershare.com

Crowe

Crowe LLP
Independent Member Crowe Global

INDEPENDENT AUDITOR'S REPORT

The Shareholders and Board of Directors
Santa Cruz County Bank
Santa Cruz, California

Report on the Financial Statements

We have audited the accompanying financial statements of Santa Cruz County Bank, which comprise the balance sheets as of December 31, 2020 and 2019, and the related 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.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Santa Cruz County Bank as of December 31, 2020 and 2019, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Other Legal and Regulatory Requirements

We also have audited in accordance with auditing standards generally accepted in the United States of America, Santa Cruz County Bank's internal control over financial reporting as of December 31, 2020, 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 16, 2021 expressed an unmodified opinion.

Crowe LLP

Crowe LLP

Sacramento, California
March 16, 2021

BALANCE SHEETS

December 31, 2020 and 2019

ASSETS	2020	2019
Cash and due from financial institutions	$ 12,530,234	$ 19,330,532
Federal funds sold	814	30,700,190
Cash and cash equivalents	12,531,048	50,030,722
Interest-bearing deposits in other financial institutions	55,235,000	135,786,000
Debt securities available-for-sale	49,850,414	52,344,896
Debt securities held-to-maturity (fair value 2020-$7,620,430; 2019 $15,444,362)	7,228,178	15,078,677
Loans held for sale	31,629,920	23,800,497
Loans, net of allowance of $13,021,249 in 2020; $10,296,230 in 2019	1,189,227,523	723,419,023
Federal Home Loan Bank stock, at cost	3,561,400	3,420,200
Bankers' Bank stock, at cost	456,215	456,215
Premises and equipment, net	10,371,574	7,647,742
Goodwill	25,761,654	25,761,654
Core deposit intangible asset, net	2,926,000	3,569,000
Bank owned life insurance	15,561,554	13,785,945
Accrued interest receivable and other assets	18,531,643	15,882,798
Total assets	$ 1,422,872,123	$ 1,070,983,369

LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits		
Noninterest-bearing	$ 552,645,185	$ 345,604,709
Interest-bearing	642,138,514	558,743,313
Total deposits	1,194,783,699	904,348,022
Federal Home Loan Bank advances and other borrowings	40,364,392	–
Accrued interest payable and other liabilities	19,238,144	15,536,979
Total liabilities	1,254,386,235	919,885,001
Commitments and contingencies - See Note 17		
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; 3,852,341 and 3,849,841 shares issued at December 31, 2020 and 2019	94,858,433	94,834,188
Additional paid-in capital	12,903,090	12,558,094
Retained earnings	60,098,549	43,704,318
Accumulated other comprehensive income	625,816	1,768
Total shareholders' equity	168,485,888	151,098,368
Total liabilities and shareholders' equity	$ 1,422,872,123	$ 1,070,983,369

See accompanying notes

STATEMENTS OF INCOME

Years ended December 31, 2020 and 2019

		2020		2019
Interest and dividend income				
Loans, including fees	$	48,276,908	$	32,891,233
Interest-bearing deposits in other financial institutions		1,961,186		2,547,132
Taxable securities		956,419		1,023,405
Tax-exempt securities		186,726		246,337
Dividends on FHLB, PCBB and TIB stock		209,807		192,373
Federal funds sold		104,587		472,807
Total interest and dividend income		51,695,633		37,373,287
Interest expense				
Deposits		2,584,312		2,187,596
Federal Home Loan Bank advances and other borrowings		125,408		387
Federal funds purchased		61		210
Total interest expense		2,709,781		2,188,193
Net interest income before provision for loan losses		48,985,852		35,185,094
Provision for loan losses		2,815,917		450,000
Net interest income after provision for loan losses		46,169,935		34,735,094
Noninterest income				
Service charges on deposits		473,752		602,711
Net gains on sales of loans		1,048,615		782,418
Loan servicing fees		600,334		612,460
ATM fee income		663,079		608,203
Other		1,426,851		840,763
Total noninterest income		4,212,631		3,446,555
Noninterest expense				
Salaries and employee benefits		15,002,551		10,795,030
Occupancy		1,842,892		1,312,189
Furniture and equipment		1,315,134		999,464
Marketing and business development		784,513		546,499
Data and item processing		1,096,682		910,127
Federal deposit insurance		269,541		196,547
Reduction of off balance sheet commitments		(30,080)		(9,614)
Amortization of core deposit intangibles		643,000		138,000
Acquisition expenses		351,055		3,341,558
Other		4,429,531		2,523,888
Total noninterest expense		25,704,819		20,753,688
Income before income taxes		24,677,747		17,427,961
Income tax expense		7,128,112		5,152,711
Net income	$	17,549,635	$	12,275,250
Earnings per share				
Basic	$	4.56	$	4.51
Diluted	$	4.54	$	4.47

See accompanying notes

STATEMENTS OF COMPREHENSIVE INCOME

Years ended December 31, 2020 and 2019

	2020	2019
Net income	$ 17,549,635	$ 12,275,250
Other comprehensive income		
Unrealized gains/losses on available-for-sale securities		
Unrealized holding gain/(loss) arising during the period	1,339,290	(24,659)
Tax effect	(395,943)	7,289
Net of tax	943,347	(17,370)
Unrealized frozen gains on securities transferred to held-to-maturity		
Amortization of unrealized frozen gain during the period	18,217	33,577
Tax effect	(5,386)	(9,927)
Net of tax	12,831	23,650
Defined benefit pension plans		
Actuarial net (loss)/gain arising during the period	(525,264)	261,770
Reclassification adjustment for amortization of prior service cost and net gain/loss included in net periodic pension cost	53,733	28,408
Tax effect	139,401	(85,787)
Net of tax	(332,130)	204,391
Total other comprehensive income	624,048	210,671
Comprehensive income	$ 18,173,683	$ 12,485,921

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

Years ended December 31, 2020 and 2019

	Shares	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance at December 31, 2018	2,448,594	$ 24,313,164	$ 12,083,645	$ 32,335,096	$ (208,903)	$ 68,523,002
Net income	–	–	–	12,275,250	–	12,275,250
Other comprehensive loss	–	–	–	–	210,671	210,671
Stock issued for acquisition	1,394,443	70,424,788	–	–	–	70,424,788
Cash dividends declared ($0.30 per share)	–	–	–	(839,357)	–	(839,357)
Stock-based compensation	–	–	474,449	–	–	474,449
Exercise of stock options	5,904	96,236	–	–	–	96,236
Restricted stock awards granted	900	–	–	–	–	–
Cumulative effect of right of use asset	–	–	–	(66,671)	–	(66,671)
Balance at December 31, 2019	3,849,841	94,834,188	12,558,094	43,704,318	1,768	151,098,368
Net income	–	–	–	17,549,635	–	17,549,635
Other comprehensive income	–	–	–	–	624,048	624,048
Cash dividends declared ($0.30 per share)	–	–	–	(1,155,404)	–	(1,155,404)
Stock-based compensation	–	–	344,996	–	–	344,996
Exercise of stock options	2,200	24,245	–	–	–	24,245
Restricted stock awards granted	300	–	–	–	–	–
Balance at December 31, 2020	3,852,341	$ 94,858,433	$ 12,903,090	$ 60,098,549	$ 625,816	$ 168,485,888

See accompanying notes

STATEMENTS OF CASH FLOWS

Years ended December 31, 2020 and 2019

	2020	2019
Cash flows from operating activities		
Net income	$ 17,549,635	$ 12,275,250
Adjustments to reconcile net income to net cash from operating activities		
Provision for loan losses	2,815,917	450,000
Depreciation and amortization of premises and equipment	803,858	609,992
Amortization of core deposit intangibles	643,000	138,000
Net amortization of securities	428,766	329,498
Net accretion of loans	(4,308,906)	(574,202)
Deferred income tax benefit	(1,160,846)	(225,053)
Net gain on sale of loans	(1,048,615)	(782,418)
Stock-based compensation expense	344,996	474,449
Earnings on bank owned life insurance	(375,609)	(283,975)
Originations of loans held for sale	(35,049,191)	(25,391,714)
Proceeds from loans held for sale	15,368,271	11,641,182
Net loss on sale/disposal of assets	–	1,773
Reduction of off balance sheet commitments	(30,080)	(9,614)
Non cash lease expense	53,837	47,854
Deferred benefit expense	548,824	368,599
Increase in deferred loan fees, net of costs	3,309,052	331,051
(Increase) decrease in accrued interest receivable and other assets	(901,661)	2,237,465
Increase (decrease) in accrued interest payable and other liabilities	363,027	(477,170)
Net cash (used in) from operating activities	(645,725)	1,160,967
Cash flows from investing activities		
Net cash and cash equivalents acquired in acquisition	–	55,286,309
Net change in interest-bearing deposits in other financial institutions	80,551,000	(20,981,000)
Available-for-sale securities		
Sales	–	12,363,815
Maturities, prepayments and calls	13,000,000	13,200,000
Purchases	(13,930,802)	(43,606,520)
Principal repayments	4,455,498	4,242,657

See accompanying notes

STATEMENTS OF CASH FLOWS

Years ended December 31, 2020 and 2019

	2020	2019
Held-to-maturity securities		
Maturities, prepayments and calls	2,475,000	3,615,000
Principal repayments	5,320,006	2,733,685
Loan originations and payments, net	(453,324,671)	(29,851,578)
Purchases of premises and equipment	(3,527,690)	(435,873)
Purchase of bank owned life insurance	(1,400,000)	–
Purchases of Federal Home Loan Bank stock	(141,200)	(155,800)
Net cash used in investing activities	(366,522,859)	(3,589,305)
Cash flows from financing activities		
Increase in deposits	290,435,677	36,279,698
Federal Home Loan Bank advances and other debt, net of repayments	40,364,392	–
Cash dividends paid	(1,155,404)	(839,357)
Proceeds from exercise of stock options, including tax benefit	24,245	96,236
Net cash from financing activities	329,668,910	35,536,577
Net change in cash and cash equivalents	(37,499,674)	33,108,239
Beginning cash and cash equivalents	50,030,722	16,922,483
Ending cash and cash equivalents	$ 12,531,048	$ 50,030,722
Supplemental cash flow information		
Interest paid	$ 2,623,515	$ 2,152,236
Income taxes paid	$ 6,110,000	$ 6,400,000
Supplemental noncash disclosures		
Transfer from loans held for sale to portfolio loans	$ 17,101,918	$ 8,026,849
Common stock issued in acquisition	$ –	$ 70,424,788
Operating lease right of use assets recognized	$ –	$ 4,836,176
Operating lease liabilities recognized	$ –	$ 4,903,172

See accompanying notes

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Santa Cruz County Bank, referred to as "the Bank", is a California state chartered bank, which offers a full range of commercial and personal banking services to residents and businesses in Santa Cruz County and contiguous counties, through its eight full-service offices located in Aptos, Capitola, Cupertino, Monterey, Santa Cruz, Scotts Valley, and Watsonville. The Bank was incorporated on September 10, 2003 as Santa Cruz County Bank (In Organization) and commenced banking operations on February 3, 2004 (Inception), upon receipt of final regulatory approval. The Bank is subject to regulations and undergoes periodic examinations by the Department of Financial Protection and Innovation ("DFPI") and the Federal Deposit Insurance Corporation ("FDIC"). The Bank's deposits are insured by the FDIC up to applicable legal limits.

The majority of the Bank's business is conducted with customers located in Santa Cruz County and adjacent counties. Its primary deposit products are checking, savings, and term certificate accounts, and its primary lending products are commercial, multi-family, agriculture, loans supported by single-family residential real estate, municipal loans, government guaranteed loans, and installment loans. Substantially all loans are secured by specific items of collateral including business assets, consumer assets, and commercial and residential real estate. Bank products are also supported by various government guarantee programs. Commercial loans are expected to be repaid from cash flow from operations of businesses. There are no significant concentrations of loans to any one industry or customer. However, the customers' ability to repay their loans is dependent on the real estate and general economic conditions in the area.

Subsequent Events

The Bank has evaluated subsequent events for recognition and disclosure from December 31, 2020 through March 16, 2021, 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. generally accepted accounting principles, 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. The Bank could experience a material adverse effect on its business as a result of the impact of the novel coronavirus pandemic ("COVID-19") and the resulting governmental actions to curtail its spread. It is at least reasonably possible that the estimates, based on information that was available at the date of the financial statements, will change in the near term due to the COVID-19 pandemic and that the effect of the change would be material to the financial statements, including the allowance for loan losses and the carrying value of goodwill. The extent to which the COVID-19 pandemic will impact our estimates and assumptions is highly uncertain and we are unable to make an estimate, at this time.

Cash Flows

For purposes of reporting cash flows, cash and cash equivalents include cash, deposits with other financial institutions with maturities fewer than 90 days, and Federal funds sold. 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, and Federal funds purchased.

Interest-Bearing Deposits in Other Financial Institutions

Interest-bearing deposits in other financial institutions mature within three years and are carried at 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, the Bank designates 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 without anticipating prepayments, except for mortgage backed securities where prepayments are anticipated. Gains and losses on sales are recorded on the settlement date and determined using the specific identification method.

Management evaluates securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the magnitude and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses the intent and ability of the Bank to retain its investment in the securities for a period of time sufficient to allow for an anticipated recovery in fair value. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis.

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.

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 Receivable

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 loan 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 non-accrual 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 non-accrual status in accordance with the Bank's policy, typically after 90 days of non-payment. In all cases, loans are placed on non-accrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. Non-accrual 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 non-accrual 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

Most of the Bank's business activity is with customers located within Santa Cruz County. Therefore, the Bank's exposure to credit risk is significantly affected by changes in the economy in the Santa Cruz County area.

Allowance for Loan Losses

The allowance for loan losses is a valuation allowance for probable credit losses in the Bank's loan portfolio that have been incurred as of the balance sheet date. The allowance is established through a provision for loan 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 the uncollectibility of a loan balance is confirmed. 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, 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 allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Generally, the Bank identifies loans to be reported as impaired when such loans are in non-accrual status or classified in part or in whole as either doubtful or loss. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings ("TDRs") and classified as impaired.

Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Commercial and commercial real estate loans over \$100,000 are individually evaluated for impairment. Typically, loans below \$100,000 from all class types are excluded from individual impairment analysis. When a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of expected future cash flows discounted at the loan's effective interest rate, except that as a practical expedient, it may measure impairment based on a loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. A loan is collateral dependent if the repayment of the loan is expected to be provided solely by the underlying collateral.

A restructuring of a debt constitutes a troubled debt restructuring ("TDR") if the Bank, for economic or legal reasons related to the debtor's financial difficulties, grants a concession to the debtor that it would not otherwise consider. Restructured workout loans typically present an elevated level of credit risk as the borrowers are not able to perform according to the original contractual terms. Loan modifications or concessions granted to borrowers resulting directly from the effects of the COVID-19 pandemic, who were otherwise in current payment status, are not considered to be TDRs. Additional details related to COVID and the CARES Act are available under the Adoption of New Accounting Standards. Troubled debt restructurings are individually evaluated for impairment and included in the separately identified impairment disclosures. TDRs are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a TDR is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral less estimated costs to sell. For TDRs that subsequently default, the Bank determines the amount of the allowance on that loan in accordance with the accounting policy for the allowance for loan losses on loans individually identified as impaired. The Bank incorporates recent historical experience related to TDRs including the performance of TDRs that subsequently default into the calculation of the allowance by loan portfolio segment.

The general reserve component covers loans that are collectively evaluated for impairment. Large groups of smaller balance homogeneous loans, such as consumer and residential real estate loans, are collectively evaluated for impairment, and accordingly, they are not separately identified for impairment disclosures. The general allowance component also includes loans that are not individually identified for impairment evaluation, such as commercial loans below the individual evaluation threshold, as well as those loans that are individually evaluated but are not considered impaired. The determination of the general reserve is based on estimates made by management, to include, but not limited to, consideration of historical loss experience adjusted for current factors. The historical loss experience is determined by portfolio segment and is based on considerations of both the Bank's actual historical loss history and losses of the peer group in which the Bank operates over the most recent 12 years. This is supplemented with other economic factors based on the risks present for each portfolio segment and internal asset classifications. These qualitative factors include economic trends in the Bank's service areas, industry experience and trends, geographic concentrations, estimated collateral values, the Bank's underwriting policies, the character of the loan portfolio, and probable losses inherent in the portfolio taken as a whole.

The Bank maintains a separate allowance for each portfolio segment (loan type). These portfolio segments include commercial real estate, land and construction, commercial and industrial, agricultural land, real estate and production, and consumer loans (principally home equity loans). Portfolio classes are not distinguished from segments for reporting purposes. The allowance for loan losses attributable to each portfolio segment, which includes both impaired loans and loans that are not impaired, is combined to determine the Bank's overall allowance, hence, is included on the balance sheet.

The general reserve component of the allowance for loan losses also consists of reserve factors that are based on management's assessment of the following for each portfolio segment: (1) inherent credit risk, (2) historical losses, and (3) other qualitative factors. These reserve factors are inherently subjective and are driven by the repayment risk associated with each portfolio segment described below.

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.

Land and Construction

Land and construction 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.

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.

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 secured by crop production and livestock are especially vulnerable to two risk factors that are largely outside the control of Bank 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.

Although management believes the allowance to be adequate, ultimate losses may vary from its estimates. 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. If the Board of Directors and management determine that changes are warranted based on those reviews, the allowance is adjusted. In addition, the Bank's primary regulators, FDIC and DFPI, as an integral part of their examination process, review the adequacy of the allowance. These regulatory agencies may require additions to the allowance based on their judgment about information available at the time of their examinations.

Allowance for Credit Losses on Off-Balance Sheet Credit Exposures

The Bank maintains a separate allowance for off-balance sheet commitments. Management estimates anticipated losses using historical data and utilization assumptions. The allowance for off-balance sheet commitments totaled $315,520 at December 31, 2020 and $345,600 at December 31, 2019, and is included in other liabilities on the balance sheet.

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 level of borrowings and other factors, and may invest in additional amounts. FHLB stock is carried at cost, classified as restricted security, 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 is redeemable at its par value of $100 per share at the discretion of the FHLB of San Francisco. The FHLB can suspend dividends and redemptions upon notification to its members.

Bankers' Bank Stock

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

Equity investments not using the equity method of accounting are measured at fair value with changes in fair value recognized in net income. Equity securities without readily determinable fair values are carried at cost, minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment. The carrying amount of equity securities without readily determinable fair values was $456,215 as of December 31, 2020 and December 31, 2019.

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 $658,399 and $529,270 at year-end 2020 and 2019 and were included in other assets on the 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 the Bank later determines 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 $600,334 and $612,460 for the years ended December 31, 2020 and 2019, respectively. Late fees and ancillary fees related to loan servicing are not material.

Premises and Equipment

Land is carried at cost. Bank 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. The Bank's 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. The Bank accounted for the acquisition of Lighthouse Bank 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. The Bank has selected December 31 as the date to perform the annual impairment test. 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.

Intangible Assets

The intangible assets at December 31, 2020 represent the estimated fair value of the core deposit relationships acquired in the business combination with Lighthouse Bank. Core deposit intangibles 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

The Bank has purchased life insurance policies on certain key 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.

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. The Bank estimates the fair value of each stock option award as of the date of grant using a Black-Scholes-Merton model, while the market price of the Bank's 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. The Bank's 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

The Bank uses 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.

The Bank recognizes 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 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 and unrealized gains and losses on securities available-for-sale, which are also recognized as separate components of equity.

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 Bank is subject to Federal Reserve Act Regulation D, which requires banks to maintain average reserve balances with the Federal Reserve Bank. Reserve requirements are offset by usable cash reserves. The Bank had no reserve requirement at December 31, 2020 and $1,800,000 at December 31, 2019 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 shareholders.

Fair Value of Financial Instruments

The Bank's estimated fair value amounts have been determined by the Bank 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 Bank's net income or shareholders' equity.

Adoption of New Accounting Standards

The following are descriptions of recently adopted accounting standards:

The CARES Act and Regulatory Changes on TDR's

During March and April of 2020, various regulatory agencies, including the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation, ("the agencies") issued regulatory guidance encouraging financial institutions to work with customers affected by the COVID-19 pandemic and providing additional information regarding loan modifications. The guidance clarifies the interaction between the interagency statement issued on March 22, 2020 and the temporary relief provided by Section 4013 of the Coronavirus Aid, Relief, and Economic Security ("CARES") Act signed into law on March 27, 2020. Section 4013 allows financial institutions to suspend the requirements to classify certain loan modifications as troubled debt restructurings (TDRs). The revised statement also provides supervisory interpretations on past due and nonaccrual regulatory reporting of loan modification programs and regulatory capital. Modifications under the revised statement have been applied by the bank related to the COVID-19 pandemic, as eligible and appropriate. The application of the guidance reduced the number of TDRs that were reported. In December, new legislation became effective extending the TDR relief under Section 4013 of the CARES Act to January 1, 2022 or the date that is 60 days after the date on which the COVID-19 emergency terminates. Future TDRs are indeterminable and will depend on future developments, which are highly uncertain and cannot be predicted, including the scope and duration of the pandemic and actions taken by governmental authorities and other third parties in response to the pandemic.

Newly Issued Not Effective Accounting Standards

ASU 2016-13, Financial Instruments - Credit Losses (Topic 326)

In June 2016, FASB issued guidance to replace the incurred loss model with an expected loss model, which is referred to as the current expected credit loss ("CECL") model. The CECL model is applicable to the measurement of credit losses on 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 cases recognized by a lessor. In addition, the amendments in this update require credit losses be presented as an allowance rather than as a write-down on available-for-sale debt securities. For the Bank, the standard will be effective for fiscal years beginning after December 31, 2022, including interim periods in those fiscal years.

For debt securities with other than temporary impairment ("OTTI"), the guidance will be applied prospectively. For all other assets within the scope of CECL, a cumulative effect adjustment will be recognized in retained earnings as of the beginning of the first reporting period in which the guidance is effective. The Bank is currently assessing data and system needs in order to evaluate the impact of adopting the new guidance. Management expects to recognize a one-time cumulative effect adjustment to the allowance for loan losses as of the first reporting period in which the new standard is effective, but cannot yet estimate the magnitude of the one-time adjustment or the overall impact of the new guidance on the Bank's financial position, results of operation, or cash flows.

ASU 2020-04, Reference Rate Reform (Topic 848)

In March 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 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. Under the guidance, the Bank could elect not to apply certain modification accounting requirements to contracts affected by reference rate transition, if certain criteria are met. A company that makes this election would not be required to re-measure the contracts at the modification date or reassess a previous accounting determination. This guidance also permits a company to elect various optional expedients that would allow it to continue applying hedge accounting for hedging relationships affected by reference rate transition, if certain criteria are met. The guidance is effective upon issuance and generally can be applied through December 31, 2022. The Bank is currently assessing the impact of this guidance on its financial statements.

NOTE 2 - BUSINESS COMBINATION

On October 18, 2019, the Bank completed the acquisition of Lighthouse Bank ("LHB") for an aggregate transaction value of $70,424,788. LHB was merged into the Bank and the Bank issued 1,394,443 shares of common stock to the former shareholders of LHB. Under the terms of the acquisition, LHB common shareholders received 0.5204 of a share of the Bank's common stock in exchange for each share of LHB common stock. With the LHB acquisition, the Bank added two full-service branches located in Santa Cruz and Cupertino. LHB's assets as of October 18, 2019 totaled $325,547,624. The fair value of the common shares issued as part of the consideration paid for LHB was determined in the basis of the closing price of the Bank's common shares on the acquisition date.

In accordance with GAAP guidance for business combinations, the Bank recorded $25,761,654 of goodwill and $3,707,000 of core deposit intangible assets on the acquisition date. The core deposit intangibles are being amortized using an accelerated basis method over a period of ten years with no significant residual value. For tax purposes, purchase accounting adjustments including goodwill are all non-taxable and/or non-deductible. Acquisition related costs of $351,055 and $3,341,558 are included in Noninterest Expense in the Bank's income statement for the years ended December 31, 2020 and 2019, respectively.

The acquisition was consistent with the Bank's strategy to expand the scale of our geographic footprint. The acquisition allows the Bank to deliver enhanced banking and lending services to our valued customers, added resources for our community and even greater efficiencies for the benefit of our shareholders. Goodwill arising from the acquisition consisted largely of synergies and the expected cost savings resulting from the combined operations.

The following table summarizes the consideration paid for LHB and the amounts of the assets and liabilities assumed recognized at the acquisition date:

		2019
Merger consideration		
Common stock issued	$	70,424,788
Fair value of total consideration transferred		70,424,788
Recognized amounts of identifiable assets acquired and liabilities assumed are as follows		
Cash and cash equivalents		55,286,309
Interest-bearing deposits in other financial institutions		19,600,000
Debt securities available-for-sale		12,363,815
Bankers' Bank stock		1,370,815
Loans, net		222,751,515
Premises and equipment		4,727,595
Core deposit intangibles		3,707,000
Deferred taxes and taxes receivable		41,265
Bank owned life insurance		4,972,759
Other assets		4,913,166
Total assets acquired		329,734,239
Deposits		283,587,359
Deposit premium		355,156
Other liabilities		1,128,590
Total liabilities assumed		285,071,105
Total identifiable net assets		44,663,134
Goodwill	$	25,761,654

The fair value of net assets acquired includes fair value adjustments to certain loans that were not considered impaired as of the acquisition date. The fair value adjustments were determined using discounted contractual cash flows. However, the Bank believes that all contractual cash flows related to these financial instruments will be collected. As such, those loans were not considered impaired at the acquisition date and were not subject to the guidance relating to purchased credit impaired ("PCI") loans, which have shown evidence of credit deterioration since origination. Loans acquired that were not subject to PCI requirements include non-impaired loans and customer receivables with a fair value and gross contractual amounts receivable of $222,751,515 and $226,502,607 respectively, on the date of acquisition.

NOTE 3 - DEBT SECURITIES

The fair value of securities available-for-sale reflected an unrealized gain of $1,083,627 at December 31, 2020 and unrealized loss of $255,663 at December 31, 2019. The unrealized gain/(loss) recorded is net of $320,631 and ($75,582) tax effect as accumulated other comprehensive income within shareholders' equity at December 31, 2020 and 2019, respectively.

The following tables summarize the carrying value and estimated fair value of securities available-for-sale and held-to-maturity at December 31, 2020 and 2019:

December 31, 2020	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale				
U.S. Treasury bonds	$ 2,001,406	$ 3,634	$ –	$ 2,005,040
U.S. government sponsored agencies	5,102,385	2,449	(10,080)	5,094,754
Mortgage backed securities: residential	7,267,485	2,960	(63,607)	7,206,838
Collateralized mortgage obligations	29,756,413	845,342	(4,558)	30,597,197
State and political subdivision	4,639,098	307,487	–	4,946,585
Total available-for-sale	$ 48,766,787	$ 1,161,872	$ (78,245)	$ 49,850,414
Held-to-maturity				
U.S. government sponsored agencies	$ 998,069	$ 5,561	$ –	$ 1,003,630
Mortgage backed securities: residential	858,341	57,239	(34)	915,546
Collateralized mortgage obligations	1,838,835	96,348	–	1,935,183
State and political subdivision	3,532,933	233,138	–	3,766,071
Total held-to-maturity	$ 7,228,178	$ 392,286	$ (34)	$ 7,620,430

December 31, 2019	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale				
U.S. Treasury bonds	$ 8,026,415	$ 10,353	$ (668)	$ 8,036,100
U.S. government sponsored agencies	5,008,147	925	(11,022)	4,998,050
Mortgage backed securities: residential	3,441,152	7,642	(21,714)	3,427,080
Collateralized mortgage obligations	31,471,869	42,080	(217,615)	31,296,334
State and political subdivision	4,652,976	7,870	(73,514)	4,587,332
Total available-for-sale	$ 52,600,559	$ 68,870	$ (324,533)	$ 52,344,896
Held-to-maturity				
U.S. government sponsored agencies	$ 988,636	$ 11,934	$ –	$ 1,000,570
Mortgage backed securities: residential	1,472,993	35,932	(85)	1,508,840
Collateralized mortgage obligations	6,629,432	70,647	(57)	6,700,022
State and political subdivision	5,987,616	247,314	–	6,234,930
Total held-to-maturity	$ 15,078,677	$ 365,827	$ (142)	$ 15,444,362

There were no transfers between available-for-sale and held-to-maturity during 2020 or 2019.

The proceeds from sales and calls of investment securities were $15,475,000 and $16,815,000 for the years ended December 31, 2020 and 2019, respectively. There were no gains or losses associated with these transactions.

The amortized cost and estimated fair value of debt securities at December 31, 2020 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, 2020	
	Amortized Cost	Estimated Fair Value
Available-for-sale		
Within one year	$ 2,237,410	$ 2,241,659
One to five years	4,349,099	4,351,831
Five to ten years	1,676,662	1,724,890
Beyond ten years	3,479,718	3,727,999
Mortgage-backed securities	7,267,485	7,206,838
Collateralized mortgage obligations	29,756,413	30,597,197
Total	$ 48,766,787	$ 49,850,414
Held-to-maturity		
Within one year	$ 1,590,214	$ 1,602,946
One to five years	1,141,675	1,223,666
Five to ten years	1,474,939	1,514,749
Beyond ten years	324,174	428,340
Mortgage-backed securities	858,341	915,546
Collateralized mortgage obligations	1,838,835	1,935,183
Total	$ 7,228,178	$ 7,620,430

Securities pledged at year-end 2020 and 2019 to secure public deposits had an amortized cost of $32,969,000 and $24,855,000, respectively and a fair value of $34,281,000 and $24,141,000, respectively.

At year-end 2020 and 2019, there were no holdings of securities of any one issuer, other than the U.S. Government and its agencies, in an amount greater than 10% of shareholders' equity.

The following table summarizes investment securities with unrealized and unrecognized losses at December 31, 2020 and December 31, 2019, aggregated by major security type and length of time in a continuous unrealized or unrecognized loss position:

December 31, 2020	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. government sponsored agencies	$ 2,985,100	$ (10,080)	$ –	$ –	$ 2,985,100	$ (10,080)
Mortgage backed securities: residential	4,305,660	(39,211)	1,917,390	(24,396)	6,223,050	(63,607)
Collateralized mortgage obligations	1,203,177	(4,558)	–	–	1,203,177	(4,558)
Total available-for-sale	$ 8,493,937	$ (53,849)	$ 1,917,390	$ (24,396)	$ 10,411,327	$ (78,245)
Held-to-maturity						
Mortgage backed securities: residential	$ 4,311	$ (34)	$ –	$ –	$ 4,311	$ (34)
Total held-to-maturity	$ 4,311	$ (34)	$ –	$ –	$ 4,311	$ (34)

December 31, 2019	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	$ 4,032,500	$ (668)	$ –	$ –	$ 4,032,500	$ (668)
U.S. government sponsored agencies	1,001,970	(380)	1,996,180	(10,642)	2,998,150	(11,022)
Mortgage backed securities: residential	2,344,971	(21,714)	–	–	2,344,971	(21,714)
Collateralized mortgage obligations	25,573,902	(209,933)	1,553,896	(7,682)	27,127,798	(217,615)
State and political subdivision	3,991,843	(73,514)	–	–	3,991,843	(73,514)
Total available-for-sale	$ 36,945,186	$ (306,209)	$ 3,550,076	$ (18,324)	$ 40,495,262	$ (324,533)
Held-to-maturity						
Mortgage backed securities: residential	$ –	$ –	$ 20,664	$ (85)	$ 20,664	$ (85)
Collateralized mortgage obligations	51,466	(57)	–	–	51,466	(57)
Total held-to-maturity	$ 51,466	$ (57)	$ 20,664	$ (85)	$ 72,130	$ (142)

As of December 31, 2020, the Bank performed an analysis of the investment portfolio to determine whether any of the investments held in the portfolio had an other-than-temporary impairment (“OTTI”). Management evaluated all investment securities with an unrealized loss at December 31, 2020 and identified those that had an unrealized loss for at least a consecutive 12-month period. There were no OTTI losses recorded during the twelve months ended December 31, 2020 or 2019.

As of December 31, 2020, the Bank’s security portfolio consisted of 84 investment securities, 7 of which were in an unrealized loss position for less than twelve months and 2 were in a loss position and had been in a loss position for twelve months or more.

All unrealized losses are related to the Bank's U.S. government sponsored agencies as discussed below.

U.S. Government Sponsored Agencies

At December 31, 2020, U.S. government or government-sponsored entities and agencies held by the Bank were issued by Small Business Administration, which the government has affirmed its commitment to support. The decline in fair value is attributable to changes in interest rates and not credit quality, and because the Bank does not have the intent to sell these mortgage backed securities and it is likely that it will not be required to sell the securities before their anticipated recovery, the Bank does not consider these securities to be other-than-temporarily impaired at December 31, 2020. The Bank's mortgage backed securities portfolio does not include non-agency collateralized mortgage obligations.

Mortgage Backed Securities: Residential

At December 31, 2020, residential mortgage-backed securities held by the Bank were issued by U.S. government sponsored entities such as the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac"), which the government has affirmed its commitment to support. The decline in fair value on the Bank's investments in U.S. Government sponsored entities collateralized by residential mortgage obligations is attributable to changes in interest rates and not credit quality, and because the Bank does not have the intent to sell these mortgage backed securities, and it is more likely than not that it will not be required to sell the securities before their anticipated recovery, the Bank does not consider these securities to be other-than-temporarily impaired at December 31, 2020.

NOTE 4 - LOANS RECEIVABLE

The outstanding loan portfolio balances at December 31, 2020 and 2019 were as follows:

	2020	2019
Commercial and industrial	$ 502,408,276	$ 159,978,860
Commercial real estate	548,092,169	402,560,300
Land and construction	84,213,865	100,693,621
Agricultural land, real estate and production	24,698,445	30,992,191
Consumer	46,705,353	40,050,565
Gross loans receivable	1,206,118,108	734,275,537
Net deferred loan fees	(3,869,336)	(560,284)
Allowance for loan losses	(13,021,249)	(10,296,230)
Loans receivable, net	$ 1,189,227,523	$ 723,419,023

At December 31, 2020 and 2019, loans held for sale that were originated under Small Business Administration ("SBA") programs totaled $31,629,920 and $23,800,497, respectively. During 2020, the bank originated Paycheck Protection Program ("PPP") covered loans totaling $371,421,546. PPP covered loans totaled $320,818,274 at December 31, 2020.

Salaries and employee benefits totaling $4,347,144 and $2,120,559 have been deferred as loan origination costs for the years ended December 31, 2020 and 2019, respectively.

The following table presents the activity in the allowance for loan losses by portfolio segment for each of the years ending December 31, 2020 and December 31, 2019:

December 31, 2020	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Unallocated	Total
Allowance for loan losses							
Beginning balance	$ 3,060,903	$ 2,916,944	$ 3,632,332	$ 296,083	$ 249,932	$ 140,036	$ 10,296,230
Provision for loan losses	400,697	1,711,923	857,223	(76,719)	62,829	(140,036)	2,815,917
Loans charged-off	(103,223)	–	–	–	–	–	(103,223)
Recoveries	8,800	3,525	–	–	–	–	12,325
Total ending allowance balance	$ 3,367,177	$ 4,632,392	$ 4,489,555	$ 219,364	$ 312,761	$ -	$ 13,021,249

December 31, 2019	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Unallocated	Total
Allowance for loan losses							
Beginning balance	$ 2,853,397	$ 3,124,492	$ 3,388,867	$ 205,861	$ 226,745	$ 37,369	$ 9,836,731
Provision for loan losses	198,007	(207,548)	243,465	90,222	23,187	102,667	450,000
Loans charged-off	–	–	–	–	–	–	-
Recoveries	9,499	–	–	–	–	–	9,499
Total ending allowance balance	$ 3,060,903	$ 2,916,944	$ 3,632,332	$ 296,083	$ 249,932	$ 140,036	$ 10,296,230

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of December 31, 2020 and 2019:

December 31, 2020	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Unallocated	Total
Allowance for loan losses							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	$ –	$ –	$ –	$ –	$ –	$ –	$ –
Collectively evaluated for impairment	3,367,177	4,632,392	4,489,555	219,364	312,761	–	13,021,249
Total ending allowance balance	$ 3,367,177	$ 4,632,392	$ 4,489,555	$ 219,364	$ 312,761	$ –	$ 13,021,249
Loans							
Loans individually evaluated for impairment	$ –	$ –	$ –	$ –	$ 31,462	$ –	$ 31,462
Loans collectively evaluated for impairment	502,408,276	548,092,169	84,213,865	24,698,445	46,673,891	–	1,206,086,646
Total ending loans balance	$ 502,408,276	$ $548,092,169	$ 84,213,865	$ 24,698,445	$ 46,705,353	$ –	$ 1,206,118,108

December 31, 2019	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Unallocated	Total
Allowance for loan losses							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	$ –	$ –	$ –	$ –	$ –	$ –	$ –
Collectively evaluated for impairment	3,060,903	2,916,944	3,632,332	296,083	249,932	140,036	10,296,230
Total ending allowance balance	$ 3,060,903	$ 2,916,944	$ 3,632,332	$ 296,083	$ 249,932	$ 140,036	$ 10,296,230
Loans							
Loans individually evaluated for impairment	$ –	$ –	$ –	$ –	$ –	$ –	$ –
Loans collectively evaluated for impairment	159,978,860	402,560,300	100,693,621	30,992,191	40,050,565	–	734,275,537
Total ending loans balance	$ 159,978,860	$ 402,560,300	$ $100,693,621	$ 30,992,191	$ 40,050,565	$ –	$ 734,275,537

The Bank had one consumer loan with a recorded investment of $31,462 impaired at the end of 2020. The impairment analysis indicated no specific reserve was required on the loan. The Bank did not have any impaired loans at the end of 2019.

Non-accrual loans and loans past due over 89 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans. The Bank had $31,462 and no loans in non-accrual as of December 31, 2020 and December 31, 2019.

The following table presents the recorded investment in loans past due over 89 days still on accrual by class of loans as of December 31, 2020 and December 31, 2019.

	Nonaccrual		Loans Past Due Over 90 Days and Still Accruing	
	2020	2019	2020	2019
Commercial and industrial	$ –	$ –	$ –	$ 739,606
Commercial real estate	–	–	–	–
Land and construction	–	–	–	–
Agricultural land, real estate and production	–	–	–	–
Consumer	31,462	–	–	–
Total	$ 31,462	$ –	$ –	$ 739,606

The following table presents the aging of the recorded investment in past due loans as of December 31, 2020 and 2019 by class of loans.

2020	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	$ –	$ –	$ –	$ –	$ 502,408,276	$ 502,408,276
Commercial real estate	–	–	–	–	548,092,169	548,092,169
Land and construction	–	–	–	–	84,213,865	84,213,865
Agricultural land, real estate and production	–	68,513	–	68,513	24,629,932	24,698,445
Consumer	–	–	31,462	31,462	46,673,891	46,705,353
Total	$ –	$ 68,513	$ 31,462	$ 99,975	$ 1,206,018,133	$ 1,206,118,108

2019	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	$ –	$ 149,710	$ 739,606	$ 889,316	$ 159,089,544	$ 159,978,860
Commercial real estate	659,051	–	–	659,051	401,901,249	402,560,300
Land and construction	–	–	–	–	100,693,621	100,693,621
Agricultural land, real estate and production	–	14,980	–	14,980	30,977,211	30,992,191
Consumer	9,656	–	–	9,656	40,040,909	40,050,565
Total	$ 668,707	$ 164,690	$ 739,606	$ 1,573,003	$ 732,702,534	$ 734,275,537

Troubled Debt Restructurings

As of December 31, 2020 and 2019, the Bank had no troubled debt restructurings.

The Bank is working with borrowers impacted by COVID-19 and providing modifications to include interest only deferral or principal and interest deferral. These modifications are excluded from troubled debt restructuring classification under the "Interagency Statement on Loan Modifications and Reporting for Financial Institutions Working with Customers Affected by the Coronavirus (Revised)." As of December 31, 2020, the Bank modified 173 loans with outstanding balances of $134,830,114. Of the 173 modified loans, 22 were still on deferral as of December 31, 2020 and had outstanding balances of $17,360,400.

Credit Quality Indicators

The Bank assigns 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. The Bank analyzes loans individually by classifying the loans as to credit risk. This analysis includes loans with an outstanding balance greater than $1,500,000 and non-homogeneous loans, such as commercial and commercial real estate loans. The analysis is performed on a semi-annual basis. These risk ratings are also subject to examination by independent specialists engaged by the Bank and the Bank's 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 the Bank's credit position at some future date. Special Mention loans are not adversely classified and do not expose the Bank 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 the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful

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

Loans not meeting the criteria above are analyzed individually as part of the above described process are considered to be pass-rated loans. Loans listed as not rated are either less than $300,000 or are included in groups of homogeneous loans.

The following table shows the risk category of the loan portfolio by class at December 31, 2020 and 2019:

December 31, 2020		Pass		Special Mention		Substandard		Doubtful		Total
Commercial and industrial	$	498,337,500	$	3,469,826	$	600,950	$	–	$	502,408,276
Commercial real estate		541,544,059		2,664,617		3,883,493		–		548,092,169
Land and construction		84,213,865		–		–		–		84,213,865
Agricultural land, real estate and production		24,629,932		68,513		–		–		24,698,445
Consumer		46,705,353		–		–		–		46,705,353
Total	$	1,195,430,709	$	6,202,956	$	4,484,443	$		$	1,206,118,108

December 31, 2019		Pass		Special Mention		Substandard		Doubtful		Total
Commercial and industrial	$	155,430,952	$	2,195,102	$	2,352,806	$	–	$	159,978,860
Commercial real estate		392,178,125		5,809,181		4,572,994		–		402,560,300
Land and construction		100,693,621		–		–		–		100,693,621
Agricultural land, real estate and production		29,184,248		1,807,943		–		–		30,992,191
Consumer		40,050,565		–		–		–		40,050,565
Total	$	717,537,511	$	9,812,226	$	6,925,800	$	–	$	734,275,537

NOTE 5 - 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. The Bank groups its 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.

The Bank 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 fixed rate loans is determined as the present value of expected future cash flows discounted at the current interest rate that represents a mix of residential and commercial real estate. The market rate is initially set at the 30-year mortgage rate resulting in a Level 3 classification. Variable rate loans that reprice frequently with changes in approximate market rates were valued using the outstanding principal balance resulting in a Level 3 classification. 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 incorporating discounts for credit, liquidity, and marketability factors.

Bankers' Bank Stock

Bankers' Bank Stock includes Federal Home Loan Bank Stock, TIB The Independent BankersBank Stock, and Pacific Coast Bankers Bank Stock. The Federal Home Loan Bank investment is carried at cost and is redeemable at par with certain restrictions. It is not practical to determine fair value of bank stock due to restrictions placed on its transferability.

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. The Bank does 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 the Bank has 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

The Bank's assets measured at fair value on a recurring basis as of December 31, 2020 and 2019 are summarized below:

	Fair Value Measurements at December 31, 2020 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	$ –	$ 2,005,040	$ –	$ 2,005,040
U.S. government sponsored agencies	–	5,094,754	–	5,094,754
Mortgage backed securities: residential	–	7,206,838	–	7,206,838
Collateralized mortgage obligations	–	30,597,197	–	30,597,197
State and political subdivision	–	4,946,585	–	4,946,585
Corporate	–	–	–	–
Total assets measured at fair value	$ –	$ 49,850,414	$ –	$ 49,850,414

	Fair Value Measurements at December 31, 2019 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	$ –	$ 8,036,100	$ –	$ 8,036,100
U.S. government sponsored agencies	–	4,998,050	–	4,998,050
Mortgage backed securities: residential	–	3,427,080	–	3,427,080
Collateralized mortgage obligations	–	31,296,334	–	31,296,334
State and political subdivision	–	4,587,332	–	4,587,332
Corporate	–	–	–	–
Total assets measured at fair value	$ –	$ 52,344,896	$ –	$ 52,344,896

There were no transfers between Level 1 and Level 2 during 2020 and 2019. There were no recurring Level 3 assets or liabilities measured at fair value during 2020 or 2019.

The Bank 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 at year-end 2020 or 2019.

Fair Value of Financial Instruments

The carrying amounts and estimated fair values of financial instruments not carried at fair value, at December 31, 2020 and 2019 are as follows:

		Fair Value Measurements at December 31, 2020 Using:			
Financial assets	Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Cash and cash equivalents	$ 12,531	$ 12,531	$ -	$ –	$ 12,531
Interest-bearing deposits in other financial institutions	55,235	–	55,235	–	55,235
Securities held-to-maturity	7,228	–	7,620	–	7,620
Loans held for sale	31,630	–	31,630	–	31,630
Loans, net	1,189,228	–	–	1,184,851	1,184,851
FHLB and Bankers' Bank stock	4,018	N/A	N/A	N/A	N/A
Accrued interest receivable	6,187	–	274	5,913	6,187
Financial liabilities					
Noninterest-bearing demand deposits	$ 552,645	$ 552,645	$ –	$ –	$ 552,645
Interest-bearing demand deposits	170,804	160,764	–	–	160,764
Savings and money market deposits	343,540	344,034	–	–	344,034
Time certificates of deposit	127,794	–	128,053	–	128,053
Accrued interest payable	154	70	84	–	154

		Fair Value Measurements at December 31, 2019 Using:			
Financial assets	Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Cash and cash equivalents	$ 50,031	$ 50,031	$ –	$ –	$ 50,031
Interest-bearing deposits in other financial institutions	135,786	–	135,786	–	135,786
Securities held-to-maturity	15,079	–	15,444	–	15,444
Loans held for sale	23,800	–	23,800	–	23,800
Loans, net	723,419	–	–	722,948	722,948
FHLB and Bankers' Bank stock	3,876	N/A	N/A	N/A	N/A
Accrued interest receivable	3,221	–	453	2,768	3,221
Financial liabilities					
Noninterest-bearing demand deposits	$ 345,605	$ 345,605	$ –	$ –	$ 345,605
Interest-bearing demand deposits	121,162	121,984	–	–	121,984
Savings and money market deposits	275,734	275,878	–	–	275,878
Time certificates of deposit	161,847	–	161,380	–	161,380
Accrued interest payable	193	9	184	–	193

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 2020 and 2019.

NOTE 6 - 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, 2020 and 2019:

	2020	2019
Land	$ 830,000	$ 830,000
Building	3,410,000	3,410,000
Furniture, fixtures and equipment	2,436,514	2,232,860
Software and capitalized data & item processing	291,910	185,448
Computer equipment	1,272,644	946,900
Automobile	16,215	16,215
Leasehold improvements	3,103,125	3,083,713
Construction-in-progress	3,068,058	195,640
Total premises and equipment	14,428,466	10,900,776
Less accumulated depreciation and amortization	(4,056,892)	(3,253,034)
Premises and equipment, net	$ 10,371,574	$ 7,647,742

Depreciation expense was $803,858 and $609,992 for 2020 and 2019, respectively.

NOTE 7 - LEASES

Lessee Arrangements

The Bank enters into leases in the normal course of business primarily for branches, back-office operations, and loan production offices. The Bank's leases have remaining terms ranging from 1 to 13 years, some of which include renewal options to extend the lease for up to 5 years and some of which include options to terminate the lease within 90 days. The Bank's leases do not include residual value guarantees or covenants.

The Bank leases 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.

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

In addition to the office building leases, the Bank has two leases for ATM and night depository kiosks. The operating leases had initial terms of five years each and various renewal options of three years each.

Building and kiosk rent expense for the years ended December 31, 2020 and 2019, was approximately

$874,445 and $662,578, respectively.

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.

The Bank uses its incremental borrowing rate at lease commencement to calculate the present value of lease payments when the rate implicit in a lease is not known. The Bank's 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:

	2020	2019
Right-of-use assets		
Operating leases	$ 5,488,707	$ 4,942,681
Total right-of-use assets	$ 5,488,707	$ 4,942,681
Lease liabilities		
Operating leases	$ 5,657,069	$ 5,057,206
Total lease liabilities	$ 5,657,069	$ 5,057,206

Right-of-use assets are included in accrued interest receivable and other assets. Lease liabilities are included in accrued interest payable and other liabilities. The components of total lease cost were as follows for the period ending:

	2020	2019
Operating lease cost	$ 832,445	$ 662,578
Short-term lease cost	42,000	–
Total lease cost, net	$ 874,445	$ 662,578

Future undiscounted lease payments for operating leases with initial terms of one year or more as of December 31, 2020 are as follows:

	Operating Leases
2021	$ 809,670
2022	715,409
2023	681,779
2024	616,470
2025	559,712
Thereafter	3,186,354
Total undiscounted lease payments	6,569,394
Less: imputed interest	912,325
Net lease liabilities	$ 5,657,069

NOTE 8 - GOODWILL AND INTANGIBLE ASSETS

The change in goodwill during the year is as follows:

	2020	2019
Balance at beginning of year	$ 25,761,654	$ –
Acquired goodwill	–	25,761,654
Impairment	–	–
Balance at end of year	$ 25,761,654	$ 25,761,654

Business combinations involving the Bank's acquisition of the equity interests or net assets of another enterprise give rise to goodwill. Total goodwill at December 31, 2020 and 2019 consisted of $25,761,654 representing the excess of the cost of LHB over the net of the amounts assigned to assets acquired and liabilities assumed in the transaction accounted for under the purchase method of accounting. The value of goodwill is ultimately derived from the Bank's ability to generate net earnings after the acquisition and is not deductible for tax purposes. A decline in net earnings could be indicative of a decline in the fair value of goodwill and result in impairment. For that reason, goodwill is assessed at least annually for impairment.

Acquired Intangible Assets

Acquired intangible assets were as follows at year-end:

	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets				
Core deposit intangibles	$ 3,707,000	$ 781,000	$ 3,707,000	$ 138,000
Total	$ 3,707,000	$ 781,000	$ 3,707,000	$ 138,000

The intangible assets at December 31, 2020 represents the estimated fair value of the core deposit relationships acquired in the acquisition of LHB 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, 2020, the weighted average remaining amortization period is 8.75 years. The carrying value of intangible assets at December 31, 2020 and 2019 was $2,926,000 and $3,569,000, net of accumulated amortization expense. Amortization expense recognized was $643,000 for 2020 and $138,000 for 2019.

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

Year Ending December 31	Estimated Core Deposit Intangible Amortization
2021	$ 486,000
2022	406,000
2023	363,000
2024	331,000
2025	312,000
Thereafter	1,028,000
Total	$ 2,926,000

NOTE 9 - DEPOSITS

Time deposits that meet or exceed the FDIC Insurance limit of $250,000 at year-end 2020 and 2019 were $64,358,130 and $78,792,989, respectively.

The scheduled maturities for all time deposits for the next five years were as follows:

2021	$	120,221,198
2022		3,958,896
2023		1,602,207
2024		1,009,570
2025		1,002,126
Total undiscounted lease payments	$	127,793,997

NOTE 10 - BORROWED FUNDS

At December 31, 2020, the Bank had unsecured lines of credit with its correspondent banks in an aggregate amount of $59,000,000, at interest rates that vary with market conditions. As of December 31, 2020, the Bank had no federal funds purchased.

The Bank has established a secured borrowing arrangement, secured by loans totaling approximately $469,741,733 with the Federal Home Loan Bank of San Francisco ("FHLB"). As of December 31, 2020, the Bank had a remaining borrowing capacity of $201,470,160 through the FHLB under which overnight and term advances were available. These advances are secured by assets including the Bank's ownership interest in the capital stock of the FHLB, securities and loans. The Bank's credit limit varies according to the amount and composition of the investments and loan portfolios pledged as collateral.

As of December 31, 2020, the Bank had a $5,000,000, Federal Home Loan Bank, FRC Recovery advance with a maturity date of May 24, 2021 and rate of 0% and $4,000,000 in Federal Home Loan Bank Overnight Advances with interest rates of 17 basis points.

In addition, $31,364,392 in loans was pledged to the Paycheck Protection Program Liquidity Facility ("PPPLF") at December 31, 2020. The loan advances all had rates of 35 basis points and 2 year terms. The Bank's credit limit varies according to the amount PPP loans pledged as collateral.

NOTE 11 -
PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS

The Bank established the Supplemental Executive Retirement Plan (SERP), an unfunded noncontributory defined benefit pension plan, to provide supplemental retirement benefits to a select group of key executives and senior officers. The Bank uses 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 for the years ended December 31, 2020 and 2019.

		2020		2019
Change in benefit obligation				
Beginning benefit obligation	$	3,174,263	$	3,273,567
Service cost		263,451		113,036
Interest cost		82,220		95,085
Actuarial gain (loss)		525,264		(261,770)
Benefits paid		(46,796)		(45,655)
Ending benefit obligation		3,998,402		3,174,263
Change in plan assets				
Beginning plan assets		–		–
Employer contributions		46,796		45,655
Benefits paid		(46,796)		(45,655)
Ending plan assets		–		–
Funded status at end of year	$	(3,998,402)	$	(3,174,263)

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

Change in benefit obligation	2020	2019
Unrecognized net actuarial (gain) loss	$ 136,102	$ (389,162)
Unrecognized prior service cost	53,733	107,466
	$ 189,835	$ (281,696)

The components of net periodic benefit cost and other amounts recognized in other comprehensive income at December 31 are as follows:

Components of net periodic benefit cost	2020	2019
Service cost	$ 263,451	$ 113,036
Interest cost	82,220	95,085
Amortization of prior service cost	53,733	53,733
Amortization of actuarial gains	–	(25,325)
Net periodic benefit cost	399,404	236,529
Other changes recognized in other comprehensive income		
Net loss (gain)	525,264	(261,770)
Amortization of gain	–	25,325
Amortization of prior service cost	(53,733)	(53,733)
Total recognized in other comprehensive income (loss)	471,531	(290,178)
Total recognized in net periodic benefit cost and other comprehensive income (loss)	$ 72,127	$ (526,707)

The 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.

Assumptions

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

	2020	2019
Discount rate used to determine net periodic benefit cost	2.38%	3.27%
Discount rate used to determine benefit obligations	2.23%	3.01%
Future salary increases	N/A	N/A

NOTE 12 - EMPLOYEE BENEFIT PLANS

401(k) Plan

All employees of the Bank are eligible to participate in the Bank's 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. The Bank matches 25% of contributions up to 6% of compensation. Total expense for the years ended December 31, 2020 and December 31, 2019 was $204,961 and $136,552, respectively.

Split-Dollar Life Insurance

The Bank accounts for split-dollar life insurance in accordance with ASC 715-60, Compensation - Nonretirement Postemployment Benefits, which requires that endorsement split-dollar life insurance arrangements which provide a postretirement benefit to an employee be recorded based on the substance of the agreement with the employee. If the employer has effectively agreed to provide the employee with a death benefit, the employer should accrue, over the service period, a liability for the actuarial present value of the future death benefit as of the employee's expected retirement date. The total liability recorded as of years ended December 31, 2020 and December 31, 2019 was $1,617,655 and $1,386,015, respectively. Total expense recognized during the years ended December 31, 2020 and December 31, 2019 was $231,640 and $201,830, respectively.

NOTE 13 - INCOME TAXES

The provision for income taxes is as follows for the years ended December 31, 2020 and 2019:

Current expense	2020	2019
Federal	$ 5,339,068	$ 3,400,622
State	2,949,890	1,977,142
Total current	8,288,958	5,377,764
Deferred expense		
Federal	(884,463)	(197,189)
State	(276,383)	(27,864)
Total deferred	(1,160,846)	(225,053)
Total provision	$ 7,128,112	$ 5,152,711

The effective tax rates differ from the federal statutory rate of 21% for 2020 and 2019 applied to income before income taxes due to the following:

	2020	2019
Federal statutory rate	21.00%	21.00%
State income tax, net of federal effect	8.54%	8.83%
Tax exempt interest	(0.68%)	(0.89%)
Acquisition related costs	0.00%	0.55%
Bank owned life insurance	(0.32%)	(0.34%)
Split dollar expense	0.20%	0.24%
Stock-based compensation	0.19%	0.09%
Other	(0.05%)	0.16%
Net	28.88%	29.64%

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 tax effects of temporary differences that gave rise to deferred tax assets and deferred tax liabilities at December 31, 2020 and 2019 are as follows:

Deferred tax assets	2020	2019
Allowance for loan losses	$ 3,849,550	$ 3,043,936
Deferred compensation	1,128,457	1,021,706
Accruals	1,001,484	1,145,611
Current state income tax	660,720	421,111
Fair value of loans and deposits	838,431	1,159,637
Lease liability	1,672,433	1,495,092
Other deferred tax assets	636,740	173,186
Gross deferred tax assets	9,787,815	8,460,279
Deferred tax liabilities		
Deferred loan costs	(1,754,993)	(1,541,698)
Core deposit intangibles	(865,031)	(1,055,125)
Premises and equipment	(377,107)	(386,311)
Right-of-use asset	(1,622,660)	(1,461,235)
Other deferred tax liabilities	(43,978)	(52,710)
Unrealized gain on available for sale securities and pension	(264,237)	(749)
Gross deferred tax liabilities	(4,928,006)	(4,497,828)
Net deferred tax asset	$ 4,859,809	$ 3,962,451

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, 2020 or December 31, 2019.

The Bank has no material unrecognized tax benefits at December 31, 2020 and 2019 and does not expect the total amount of unrecognized tax benefits to significantly increase or decrease within the next twelve months.

The Bank did not have any interest and penalties recorded in the income statement for the year ended December 31, 2020 and December 31, 2019 from unrecognized tax benefits.

The Bank is subject to U.S. federal income tax as well as income tax of the state of California. The Bank is no longer subject to examination by taxing authorities for years before 2017 and 2016, for federal and California purposes.

NOTE 14 - RELATED PARTY TRANSACTIONS

Loan related activity to principal officers, directors, and their affiliates during 2020 were as follows:

		2020
Beginning balance	$	13,350,062
New loans or disbursements		521,821
Principal repayments		(433,992)
Ending balance	$	13,437,891

At December 31, 2020 and 2019, no related party loans were on non-accrual or classified for regulatory reporting purposes. Deposits from principal officers, directors, and their affiliates at year-end 2020 and 2019 were $4,958,116 and $4,660,052, respectively.

NOTE 15 - STOCK-BASED COMPENSATION

The Bank has two share based compensation plans as described below. Total compensation cost that has been charged against income for those plans was $344,996 and $474,449 for 2020 and 2019, respectively. The total income tax benefit was $15,460 and $37,183 for 2020 and 2019, respectively.

The Bank estimates the fair value of each option award as of the date of grant using a closed form option valuation (Black-Scholes) model and the following assumptions. Expected volatilities are based on historical volatilities of the Bank's 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.

	2020	2019
Risk-free interest rate	0.74%	1.69%
Expected term (yrs.)	6.00	6.00
Expected stock price volatility	29.33%	26.72%
Dividend yield	0.74%	0.57%

2003 Stock Option Plan

The Bank adopted a qualified stock option plan (the "Option Plan") for employees, non-employee directors and Bank founders, under which a maximum of 500,202 shares of Bank's common stock may 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 shares granted have daily vesting over the first four years of the option contract. All option contracts for founders who are not also Bank directors or Bank officers have expiration dates of 10 years from the date of grant. 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 Bank's Option Plan for 2020 as presented below:

	December 31, 2020			
	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Options outstanding at beginning of year	11,050	$ 10.67		
Granted	–	–		
Exercised	(2,200)	11.02		
Expired	–	–		
Forfeited	–	–		
Options outstanding at end of year	8,850	$ 10.58	0.92 years	$ 264,859
Options fully vested and expected to vest	8,850			$ 264,859
Exercisable at end of year	8,850	$ 10.58	0.92 years	$ 264,859

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

	2020	2019
Intrinsic value of options exercised	$ 80,580	$ 133,554
Cash received from option exercises	$ 24,245	$ 48,382
Tax benefit realized from option exercises	$ 11,853	$ 25,784
Weighted average fair value of options granted	–	–

As of December 31, 2020, 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

The Bank 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 469,970 unless amended by the Board or the shareholders of the Bank.

The Omnibus Plan permits the grant of non-statutory options, incentive stock options and restricted stock awards to directors and employees of the Bank. 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.

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 Bank's Omnibus Plan for 2020 as presented below:

	December 31, 2020					
	Shares		Weighted Average Exercise Price	Weighted Average Remaining Contractual Life		Aggregate Intrinsic Value
Options outstanding at beginning of year	109,367	$	44.36			
Granted	24,000		37.44			
Exercised	-		-			
Expired	(923)		50.32			
Forfeited	(5,077)		50.44			
Options outstanding at end of year	127,367	$	42.77	7.65 years	$	517,620
Options fully vested and expected to vest	68,576				$	497,498
Exercisable at end of year	64,432	$	39.70	6.49 years	$	452,151

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

		2020		2019
Intrinsic value of options exercised	$	–	$	60,944
Cash received from option exercises	$	–	$	47,854
Tax benefit realized from option exercises	$	–	$	–
Weighted average fair value of options granted	$	11.26	$	13.64

As of December 31, 2020, there was $790,465 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 2.72 years.

Restricted Stock Awards

The following is a summary of the activity relating to the Bank's non-vested shares under this plan for the year ended December 31, 2020 as presented at right:

	Shares		Weighted Average Grant Date Fair Value
Non-vested awards at January 1, 2019	4,112	$	49.98
Granted	300		43.31
Vested	(4,412)		49.53
Forfeited	–		–
Non-vested awards at December 31, 2020	–	$	49.98

As of December 31, 2020, there was no unrecognized compensation cost related to non-vested shares granted under the Omnibus Plan. The total fair value of shares vested during the years ended December 31, 2020 and December 31, 2019 was $218,511 and $261,592.

NOTE 16 - REGULATORY CAPITAL MATTERS

Regulatory Capital

The Bank is 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 the Bank's financial statements. Management believes as of December 31, 2020, the Bank meets all capital adequacy requirements to which it is subject.

Prompt corrective action regulations define five classifications: 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 year-end 2020 and 2019, the most recent regulatory notifications categorized the Bank as 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.

Actual and required capital amounts (in thousands) and ratios are presented below at year-end.

	Actual		Required for Capital Adequacy Purposes		To Be Well-Capitalized Under Prompt Corrective Action Regulations	
As of December 31, 2020						
Total capital to risk weighted assets	$ 151,320	15.59%	$ 101,916	10.50%	$ 97,063	10.00%
Tier 1 (Core) capital to risk weighted assets	$ 139,172	14.34%	$ 82,504	8.50%	$ 77,651	8.00%
Common Tier 1 (CET1) to risk weighted assets	$ 139,172	14.34%	$ 67,944	7.00%	$ 63,091	6.50%
Tier 1 (Core) capital to average assets	$ 139,172	10.27%	$ 54,196	4.00%	$ 67,745	5.00%

	Actual		Required for Capital Adequacy Purposes		To Be Well-Capitalized Under Prompt Corrective Action Regulations	
As of December 31, 2019						
Total capital to risk weighted assets	$ 131,913	16.26%	$ 85,186	10.50%	$ 81,130	10.00%
Tier 1 (Core) capital to risk weighted assets	$ 121,766	15.01%	$ 68,960	8.50%	$ 64,904	8.00%
Common Tier 1 (CET1) to risk weighted assets	$ 121,766	15.01%	$ 56,791	7.00%	$ 52,734	6.50%
Tier 1 (Core) capital to average assets	$ 121,766	11.85%	$ 41,088	4.00%	$ 51,359	5.00%

Dividend Restrictions

The Board of Directors may, to the extent of such earnings and the Bank's 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.

NOTE 17 - LOAN COMMITMENTS AND OTHER RELATED ACTIVITIES

Correspondent Banking

At times, the Bank maintains deposit amounts at corresponding banks that exceed federally insured limits. Uninsured deposits totaled $9,588,732 at December 31, 2020. The Bank has not experienced any losses on amounts exceeding the insured limits.

Financial Investments With Off-Balance Sheet Risk

The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, 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 the Bank has in particular classes of financial instruments.

The Bank's 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. The Bank uses 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. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank 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 risk at year-end December 31, were as follows:

	December 31, 2020		December 31, 2019	
	Fixed Rate	Variable Rate	Fixed Rate	Variable Rate
Commitments to make loans	$ 3,218,346	$ 269,138,604	$ 27,256,734	$ 156,258,958
Unused lines of credit	499,038	42,663,673	462,204	47,672,666
Standby letters of credit	–	130,000	–	514,000
	$ 3,717,384	$ 311,932,277	$ 27,718,938	$ 204,445,624

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

NOTE 18 - EARNINGS PER SHARE

The factors used in the earnings per share computation follow:

	2020	2019
Basic earnings per share		
Net income	$ 17,549,635	$ 12,275,250
Weighted average common shares outstanding	3,850,783	2,719,384
Basic earnings per common share	$ 4.56	$ 4.51
Diluted earnings per share		
Net income	$ 17,549,635	$ 12,275,250
Weighted average common shares outstanding for basic earnings per common share	3,850,783	2,719,384
Add: Dilutive effects of assumed exercises of stock options	18,604	25,400
Weighted average outstanding and dilutive potential common shares	3,869,387	2,744,784
Diluted earnings per common share	$ 4.54	$ 4.47

Stock options for 107,000 and 89,000 shares of common stock were not considered in computing diluted earnings per common share for the years ended December 31, 2020 and December 31, 2019, respectively, because they were anti-dilutive.

SANTA CRUZ COUNTY BANK

Put your money where your life is.