open bank

OP BANCORP

ANNUAL REPORT

2017

OP BANCORP

OP Bancorp is the holding company of Open Bank with $901 million in total assets as of December 31, 2017. Open Bank is headquartered in Los Angeles and has been serving the banking needs of small-and medium-sized businesses, professionals, and residents with a particular emphasis on Korean and other ethnic minority communities. The Bank currently operates with eight full branch offices in Downtown Los Angeles, Los Angeles Fashion District, Los Angeles Koreatown, Gardena, Buena Park, and Santa Clara. The Bank also has three loan production offices in Seattle, Washington, Dallas, Texas, and Atlanta, Georgia.

The Bank commenced its operations on June 10, 2005 as First Standard Bank and changed its name to Open Bank in October 2010. OP Bancorp common stock is quoted on the Nasdaq Global Market under the ticker symbol, “OPBK.”

DEAR SHAREHOLDER, CLIENTS, AND COMMUNITIES

Open Bank continues to be your steward to serve our clients, shareholders, employees, and communities… to grow our relationships together.

We continued to demonstrate strong performance in 2017. We are very pleased to report record earnings of $9.2 million and finished the year with total assets of over $900 million on a consolidated basis. We had strong growth in both loans and deposits and continue to strive to maintain a net interest margin higher than our peers. We continue to find new opportunities for growth and opened a loan production office in Duluth, Georgia in 2017 and a new branch in Santa Clara, Northern California in the first quarter 2018.

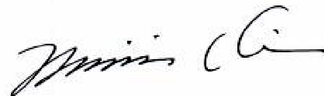
We believe that our strong growth is the result of our strategic goals, excellent service, experienced management team, and enduring efforts in building relationships with new and existing clients in our communities we serve.

We have a commitment to contribute 10% of our net income after taxes to the Open Stewardship Foundation and other community events. In 2017 we made a total contribution to Open Stewardship of around $920,000. The funds were used to support 62 civic organizations, schools, and other eligible charitable non-profit organizations, as well as community events that provide public benefit services in the communities we serve.

In the first quarter of 2018 we completed our initial public offering raising net proceeds of $22.6 million. This was a wonderful step for our Company and we are very excited to have our common stock listed on the Nasdaq Global Market.

Looking ahead, we benefit from our financial strength, our commitment to our communities, and staying true to our vision… as we continue to grow, our contribution to our communities will grow…hand-in-hand.

BRIAN CHOI
Chairman of the Board
OP Bancorp



MIN KIM
President & Chief Executive Officer
OP Bancorp
Open Bank

FINANCIAL HIGHLIGHT

As of or for the year ended December 31,

(dollars in thousands, except per share data)	2017	2016	2015
Income Statement Data			
Interest income	$ 40,283	$ 31,701	$ 25,192
Interest expense	4,573	3,371	2,689
Net interest income	35,710	28,330	22,503
Provision for loan losses	1,311	1,682	553
Non-interest income	8,986	9,007	7,978
Non-interest expense	26,257	23,334	19,795
Income before taxes	17,128	12,320	10,133
Provision for income taxes	7,892	4,894	4,170
Net income	9,236	7,425	5,963
Per Share Data			
Basic income per share	$ 0.68	$ 0.55	$ 0.44
Diluted income per share	$ 0.66	$ 0.53	$ 0.43
Book value per share (at period end)	$ 6.94	$ 6.30	$ 5.71
Shares of common stock outstanding	13,190,527	12,896,548	12,682,510
Weighted average diluted shares	13,485,791	13,158,155	12,944,867
Balance Sheet Data			
Loans held for investment	$ 748,024	$ 674,227	$ 507,286
Loans held for sale	15,739	1,646	5,579
Allowance for loan losses	9,139	7,910	6,390
Total assets	900,999	761,250	617,350
Deposits	773,306	661,784	519,721
Shareholders’ equity	91,480	81,284	72,479

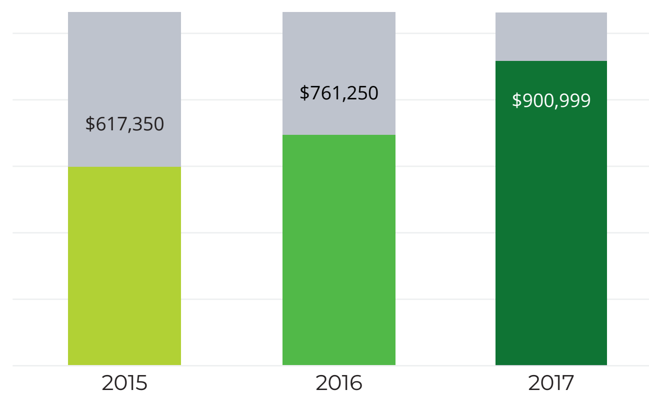
As of or for the year ended December 31,

(dollars in thousands, except per share data)	2017	2016	2015
Performance Ratio			
Return on average assets	1.13%	1.08%	1.05%
Return on average equity	10.63	9.69	8.63
Yield on total loans	5.48	5.20	5.18
Yield on average earning assets	5.20	4.85	4.70
Cost of average interest bearing liabilities	0.97	0.83	0.79
Cost of deposits	0.62	0.56	0.55
Net interest margin	4.61	4.34	4.20
Efficiency ratio (1)	58.74	62.50	64.94
Asset Quality Data (at Period End)			
Net charge-offs to average loans held for investment	0.01%	0.03%	(0.02)%
Nonperforming assets to loans held for investment plus OREO	0.14	0.09	0.20
ALL to nonperforming loans	881.29	1,373.26	615.01
ALL to loans held for investment	1.22	1.17	1.26
Balance Sheet and Capital Ratios			
Loans held for investment to deposits	96.73%	101.88%	97.61%
Noninterest bearing deposits to deposits	37.43	37.38	29.85
Average equity to average total assets	10.59	11.18	12.20
Leverage ratio	10.46	10.89	11.70
Common equity tier 1 ratio	12.26	12.20	14.28
Tier 1 risk-based capital ratio	12.26	12.20	14.28
Total risk-based capital ratio	13.49	13.40	15.53
Non-owner occupied CRE to total risk-based capital	296.69	293.56	233.83

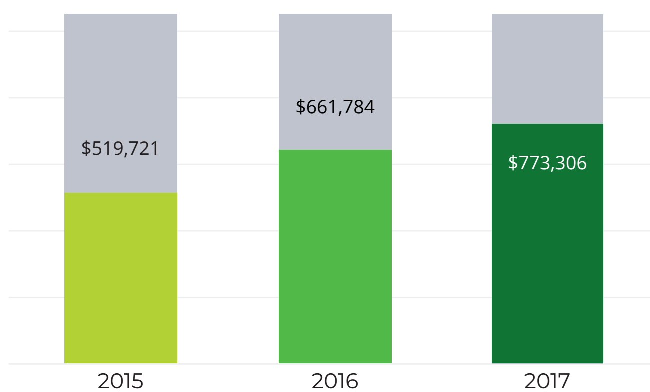
(1) Represents non-interest expense divided by the sum of net interest income plus non-interest income.

FINANCIAL HIGHLIGHT

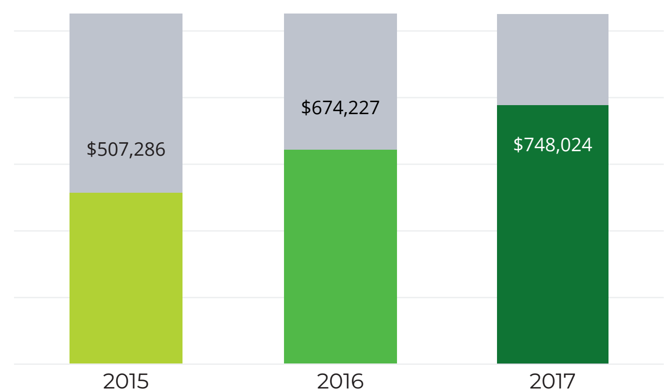
TOTAL ASSET
dollars in thousands



TOTAL DEPOSIT
dollars in thousands

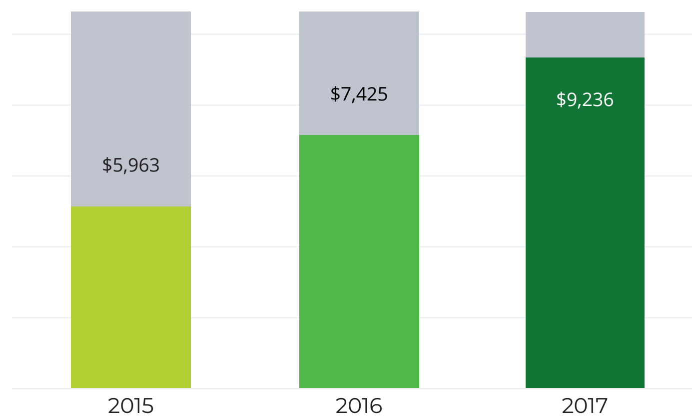


LOAN HELD FOR INVESTMENT
dollars in thousands

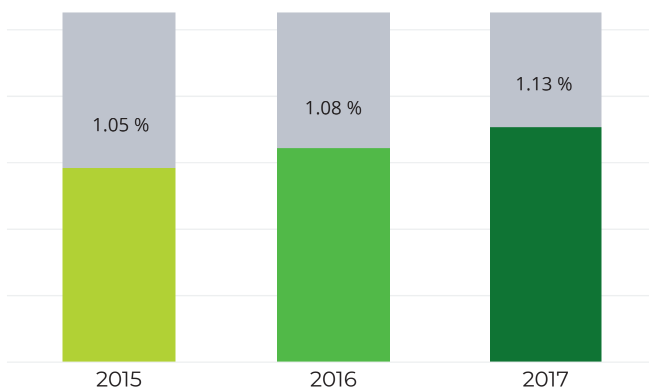


NET INCOME

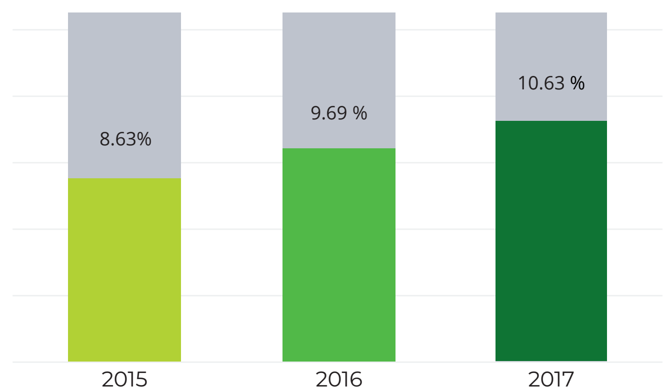
dollars in thousands



RETURN ON AVERAGE ASSETS



RETURN ON AVERAGE EQUITY



CORPORATE INFORMATION

Board of Directors

BRIAN CHOI
Chairman of the Board
Chairman and CEO
Universal Financing Corporation
Ehese Investments, LLC

MIN J. KIM
President & Chief Executive Officer
OP Bancorp and Open Bank

SOO HUN JUNG
Medical Doctor

JASON HWANG
Certified Public Accountant
Jason Hwang, CPA

ERNEST E. DOW
Principal
Dow & Sohn CPAs

OCK HEE KIM
Former President
Lily's Dress Company

MYUNG JA PARK
President
LP Royal Import LLC
Park and Park Inc.

YONG SIN SHIN
President
CJS Groups Inc

Executive Officers

MIN J. KIM
President &
Chief Executive Officer
OP Bancorp and Open Bank

CHRISTINE OH
Executive Vice President &
Chief Financial Officer
OP Bancorp and Open Bank

STEVE PARK
Executive Vice President &
Chief Credit Officer
Open Bank

KI WON YOON
Executive Vice President &
Chief Lending Officer
Open Bank

KATHRINE DUNCAN
Executive Vice President &
Chief Risk Officer
Open Bank

INDEPENDENT AUDITOR
Crowe LLP
Sherman Oaks, CA

CORPORATE COUNSEL
Buchalter, A Professional Corporation
Los Angeles, CA

TRANSFER AGENT
Computershare Trust Company

Corporate Office

Headquarters
1000 Wilshire Blvd., Suite 500
Los Angeles, CA 90017
213.892.9999

Commercial Loan I
1000 Wilshire Blvd., Suite 100
Los Angeles, CA 90017
213.593.4820

Commercial Loan II
1000 Wilshire Blvd., Suite 100
Los Angeles, CA 90017
213.593.4823

Commercial Loan III
1000 Wilshire Blvd., Suite 100
Los Angeles, CA 90017
213.593.4830

Commercial Loan IV
1000 Wilshire Blvd., Suite 100
Los Angeles, CA 90017
213.593.4828

SBA Department
1000 Wilshire Blvd., Suite 500
Los Angeles, CA 90017
213.892.1164

Home Loan Center
550 S. Western Ave.
Los Angeles, CA 90020
877.296.6736

Branches

Aroma Office
3680 Wilshire Blvd., Suite 101
Los Angeles, CA 90010
213.401.3500

Buena Park Office
5141 Beach Blvd., Suite E
Buena Park, CA 90621
714.735.5900

Fashion District Office
747 E. 10th St., Suite 310
Los Angeles, CA 90021
213.443.9333

Gardena Office
15435 S. Western Ave., Suite 100-D
Gardena, CA 90249
310.354.6000

Olympic Office
3030 W. Olympic Blvd., Suite 110
Los Angeles, CA 90006
323.200.2100

Santa Clara Office
2998 E. El Camino Real
Santa Clara, CA 95051
669.212.8800

Western Office
550 S. Western Ave.
Los Angeles, CA 90020
213.401.1200

Wilshire Office
1000 Wilshire Blvd., Suite 100
Los Angeles, CA 90017
213.266.4100

Loan Production Office

Washington LPO, Seattle
11900 NE 1st St., Suite 300
Bellevue, WA 98005
425.454.3700

Texas LPO,Dallas
11498 Luna Rd., Suite 100
Farmers Branch, TX 75234
469.420.9400

Georgia LPO, Atlanta
3700 Crestwood Pkwy., Suite 205
Duluth, GA 30096
470.375.2435

THE COMPLETE ANNUAL REPORT IS SAVED IN THE ATTACHED USB

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Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the "Selected Historical Consolidated Financial Data" and our consolidated financial statements and related notes included elsewhere in this report. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Certain risks, uncertainties and other factors, including but not limited to those set forth under "Cautionary Note Regarding Forward-Looking Statements," "Risk Factors" and elsewhere in our registration statement or Form S-1, may cause actual results to differ materially from those projected in the forward looking statements. We assume no obligation to update any of these forward-looking statements.

Overview

We are a bank holding company headquartered in Los Angeles, California. Our commercial community banking activities are operated through Open Bank, our banking subsidiary. We offer commercial banking services to small and medium-sized businesses, their owners and retail customers primarily in the Korean-American community.

Our lending activities are diversified and include commercial real estate, Small Business Administration ("SBA") guaranteed, commercial and industrial, home mortgage, and consumer loans. We generally lend in markets where we have a physical presence through our branch and loan production offices, and attract deposits throughout our market area through a wide range of deposit products for business banking and retail markets. We offer a multitude of other products and services to our customers to complement our lending and deposit business.

We derive our income primarily from interest received on our loan portfolio, and fee income we receive in connection with our deposits and the sale and service of SBA loans. Our major operating expenses are the interest we pay on deposits, the salaries and related benefits we pay our management and staff and the rent we pay on our leased properties. We rely primarily on locally-generated deposits, mostly from the Korean-American market within California, to fund our loan activities. We currently operate seven branches in Los Angeles County and Orange County. We have three loan production offices in Dallas, Texas, Seattle, Washington and Atlanta, Georgia.

As of December 31, 2017, we had total assets of $901.0 million, gross loans of $748.0 million, total deposits of $773.3 million, and total consolidated shareholders' equity of $91.5 million. For the years ended December 31, 2017, 2016 and 2015, we recorded net income of $9.2 million, $7.4 million, and $6.0 million, respectively.

Critical Accounting Policies and Estimates

Our accounting and reporting policies conform to accounting principles generally accepted in the United States of America ("GAAP") and conform to general practices within the industry in which we operate. To prepare financial statements in conformity with GAAP, management makes estimates, assumptions and judgments based on available information. These estimates, assumptions and judgments affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions and judgments are based on information available as of the date of the financial statements and, as this information changes, actual results could differ from the estimates, assumptions and judgments reflected in the financial statement. In particular, management has identified several accounting policies that, due to the estimates, assumptions and judgments inherent in those policies, are critical in understanding our financial statements.

The following is a discussion of the critical accounting policies and significant estimates that require us to make complex and subjective judgments. Additional information about these policies can be found in Note 2 of our consolidated financial statements as of December 31, 2017, included elsewhere in this prospectus.

Allowance for Loan Losses

The allowance for loan losses ("ALL") is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. 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 ALL is maintained at a level that management believes is appropriate to provide for known and inherent incurred loan losses as of the date of the consolidated balance sheet and we have established methodologies for the determination of its adequacy. The methodologies are set forth in a formal policy and take into consideration the need for an overall general valuation allowance as well as specific allowances that are determined on an individual loan basis.

The evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available. While management uses available information to recognize losses on loans, changes in economic or other conditions may necessitate revision of the estimate in future periods.

Servicing Assets

Servicing assets are recognized separately when loans are sold and the rights to service loans are retained. When loans are sold, servicing assets are recorded at fair value in accordance with ASC Topic 860, *Transfers and Servicing* ("ASC 860"). Fair value is based on market prices for comparable servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. The fair value of servicing rights is highly sensitive to changes in underlying assumptions. Changes in the prepayment speed and discount rate assumptions have the most significant impact on the fair value of servicing assets.

Servicing fee income, which is reported on the income statement as other income, is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal and are recorded as income when earned. The amortization of servicing assets is netted against loan servicing fee income. Late fees and ancillary fees related to loan servicing are not material.

Fair Value of Financial Instruments

ASC Topic 820, *Fair Value Measurement* ("ASC 820"), defines fair value as the price that would be received to sell a financial asset or paid to transfer a financial liability in an orderly transaction between market participants at the measurement date. The degree of management judgment involved in determining the fair value of assets and liabilities is dependent upon the availability of quoted market prices or observable market parameters. For financial instruments that trade actively and have quoted market prices or observable market parameters, there is minimal subjectivity involved in measuring fair value. When observable market prices and parameters are not available, management judgment is necessary to estimate fair value. In addition, changes in market conditions may reduce the availability of quoted prices or observable date. See Note 13 of our consolidated financial statements as of December 31, 2017, included elsewhere in this prospectus, for a complete discussion of fair value of financial assets and liabilities and their related measurement practices.

Stock-Based Compensation

We grant stock options to purchase our common stock and restricted stock to our employees and directors under the 2010 Equity Incentive Plan. Additionally, we have outstanding options that were granted under option

plans from which we no longer make grants. The benefits provided under all of these plans are subject to the provisions of accounting guidance related to share based payments. Our results of operations for the calendar years ended December 31, 2017, 2016 and 2015 were impacted by the recognition of non-cash expense related to the fair value of our share based compensation awards.

The determination of fair value of stock-based payment awards on the date of grant using the Black Scholes model is affected by our stock price, as well as the input of other subjective assumptions. These assumptions include, but are not limited to, the expected term of stock options and our stock price volatility. Our stock options have characteristics significantly different from those of traded options, and changes in the assumptions can materially affect the fair value estimates.

Current accounting guidance requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. If actual forfeitures vary from our estimates, we will recognize the difference in compensation expense in the period the actual forfeitures occur.

Income Taxes

We use the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. If current available information raises doubt as to the realization of the deferred tax assets, a valuation allowance may be established. We consider the determination of this valuation allowance to be a critical accounting policy because of the need to exercise significant judgment in evaluating the amount and timing of recognition of deferred tax liabilities and assets, including projections of future taxable income. These judgments and estimates are reviewed on a continual basis as regulatory and business factors change. See Note 9 of our consolidated financial statements as of December 31, 2017, included elsewhere in this prospectus, for additional information. A valuation allowance for deferred tax assets may be required in the future if the amounts of taxes recoverable through loss carry backs decline, if we project lower levels of future taxable income, or we project lower levels of tax planning strategies. Such valuation allowance would be established through a charge to income tax expense that would adversely affect our operating results.

Results of Operations—Comparison of Results of Operations for the Years Ended December 31, 2017 and 2016

The following discussion of our results of operations compares the year ended December 31, 2017 to the year ended December 31, 2016.

We reported net income for the year ended December 31, 2017 of $9.2 million compared to net income of $7.4 million for the year ended December 31, 2016. The increase was due to a $7.4 million increase in net interest income and a $371,000 decrease in provision for loan losses, offset by a $2.9 million increase in noninterest expense and a $3.0 million increase in provision for income taxes, which included a revaluation of deferred tax assets of $1.3 million.

Net Interest Income

The management of interest income and expense is fundamental to our financial performance. Net interest income, the difference between interest income and interest expense, is the largest component of the Company's total revenue. Management closely monitors both total net interest income and the net interest margin (net interest income divided by average earning assets). We seek to maximize net interest income without exposing the Company to an excessive level of interest rate risk through our asset and liability policies. Interest rate risk is

managed by monitoring the pricing, maturity and repricing options of all classes of interest-bearing assets and liabilities. Our net interest margin is also adversely impacted by the reversal of interest on nonaccrual loans and the reinvestment of loan payoffs into lower yielding investment securities and other short-term investments.

The following table presents, for the periods indicated, information about: (i) weighted average balances, the total dollar amount of interest income from interest-earning assets and the resultant average yields; (ii) average balances, the total dollar amount of interest expense on interest-bearing liabilities and the resultant average rates; (iii) net interest income; (iv) the interest rate spread; and (v) the net interest margin.

	Year Ended December 31,					
	2017			2016		
(Dollars in thousands)	**Average Balance**	**Interest and Fees**	**Yield / Rate**	**Average Balance**	**Interest and Fees**	**Yield / Rate**
Earning assets:						
Federal funds sold and other investments (1)	$ 22,926	$ 495	2.16%	$ 26,213	$ 507	1.93%
Securities available for sale	37,620	676	1.80	40,159	664	1.65
Total investments	60,546	1,171	1.93	66,372	1,171	1.76
Real estate	384,462	18,721	4.87	315,244	14,046	4.46
SBA	123,822	9,430	7.62	103,313	7,414	7.18
C & I	98,455	5,346	5.43	73,803	3,845	5.21
Home Mortgage	103,191	5,344	5.18	88,282	4,694	5.32
Consumer	4,385	271	6.18	5,986	531	8.87
Loans (2)	714,315	39,112	5.48	586,628	30,530	5.20
Total earning assets	774,861	40,283	5.20	653,000	31,701	4.85
Noninterest-earning assets	45,499			32,617		
Total assets	820,360			685,617		
Interest-bearing liabilities:						
NOW and savings deposits	6,137	15	0.24%	4,058	10	0.25%
Money market deposits	258,019	2,344	0.91	202,737	1,736	0.86
Time deposits	196,831	2,111	1.07	181,191	1,540	0.85
Total interest-bearing deposits	460,987	4,470	0.97	387,986	3,286	0.85
Borrowings	9,302	103	1.11	16,986	85	0.50
Total interest-bearing liabilities	470,289	4,573	0.97	404,972	3,371	0.83
Noninterest-bearing liabilities:						
Noninterest-bearing deposits	256,267			198,413		
Other noninterest-bearing liabilities	6,895			5,585		
Total noninterest-bearing liabilities	263,162			203,998		
Shareholders' equity	86,909			76,647		
Total liabilities and shareholders' equity	$820,360			$685,617		
Net interest income / interest rate spreads		$35,710	4.23%		$28,330	4.02%
Net interest margin			4.61%			4.34%

(1) Includes income and average balances for FHLB and Pacific Coast Bankers Bank ("PCBB") stock, term federal funds, interest-earning time deposits and other miscellaneous interest-earning assets.

(2) Average loan balances include non-accrual loans and loans held for sale.

Increases and decreases in interest income and interest expense result from changes in average balances (volume) of interest-earning assets and interest-bearing liabilities, as well as changes in average interest rates.

The following tables set forth the effects of changing rates and volumes on our net interest income during the period shown. Information is provided with respect to (i) effects on interest income attributable to changes in volume (change in volume multiplied by prior rate) and (ii) effects on interest income attributable to changes in rate (changes in rate multiplied by prior volume). Change applicable to both volume and rate have been allocated to volume.

	Year Ended December 31, 2017 over 2016		
	Change due to:		
(Dollars in thousands)	Volume	Rate	Interest Variance
Earning assets:			
Federal funds sold and other investments	$ (68)	$ 56	$ (12)
Securities available for sale	(47)	59	12
Total investments	(115)	115	—
Real estate	3,295	1,380	4,675
SBA	1,540	476	2,016
C & I	1,333	168	1,501
Home Mortgage	776	(126)	650
Consumer	(122)	(138)	(260)
Loans	6,822	1,760	8,582
Total earning assets	6,707	1,875	8,582
NOW and savings deposits	5	—	5
Money market deposits	501	107	608
Time deposits	143	428	571
Total interest-bearing deposits	649	535	1,184
Borrowings	(51)	69	18
Total interest-bearing liabilities	598	604	1,202
Net interest income	$6,109	$1,271	$7,380

Net interest income for the year ended December 31, 2017 was $35.7 million compared to $28.3 million for the year ended December 31, 2016, an increase of $7.4 million, or 26.1%. This increase was primarily due to an 18.7% increase in the average balance of interest-earning assets, coupled with a 35 basis point improvement in the average yield on interest-earning assets, offset by a 14 basis point increase in the average rate paid on interest-bearing liabilities. The increase in the average balance of interest-earning assets was primarily due to an increase in average loans outstanding. The increase in the average yield on interest-earning assets was primarily due to cumulative market rate increases by the Federal Reserve of 100 basis points through four rate increases in each of December 2016, March 2017, June 2017 and December 2017.

Total interest income was $40.3 million in 2017 compared to $31.7 million in 2016, an increase of $8.6 million, or 27.1%. This increase was primarily due to an increase in interest earned on our loan portfolio. Interest and fees on loans was $39.1 million in 2017 compared to $30.5 million in 2016, an increase of $8.6 million, or 28.1%. This increase in interest income on loans was primarily due to a 21.8% increase in the average balance of loans outstanding and a 28 basis point improvement in the average yield on loans.

Interest income on total investments was $1.2 million in 2017 and 2016. Interest income on the securities portfolio increased $12,000, or 1.8%, to $676,000 in 2017 compared to $664,000 in 2016. The increase in interest

income on the securities portfolio was primarily due to a 15 basis point increase in the average yield on the securities portfolio. Interest income on federal funds sold and other investments decreased $12,000, or 2.4%, to $495,000 in 2017 from $507,000 in 2016, due to a 12.5% decrease in the average balance of federal funds sold, offset by a 23 basis point increase in the average yield on federal fund sold and other investments.

Total interest expense was $4.6 million in 2017 compared to $3.4 million in 2016, an increase of $1.2 million, or 35.7%. The increase was primarily due to increases in interest expense on deposits. Interest expense on deposits was $4.5 million in 2017 compared to $3.3 million in 2016, an increase of $1.2 million, or 36.0%. This increase was primarily due to an 18.8% increase in the average balance of interest-bearing deposits, coupled with a 12 basis point increase in the average interest rate paid.

Net interest margins for the years ended December 31, 2017 and 2016 were 4.61% and 4.34%, respectively.

Provision for Loan Losses

Credit risk is inherent in the business of making loans. We establish an allowance for loan losses through charges to earnings, which are shown in the statements of operations as the provision for loan losses. Specifically identifiable and quantifiable known losses are promptly charged off against the allowance. The provision for loan losses is determined by conducting a quarterly evaluation of the adequacy of our allowance for loan losses and charging the shortfall or excess, if any, to the current quarter's expense. This has the effect of creating variability in the amount and frequency of charges to earnings. The provision for loan losses and level of allowance for each period are dependent upon many factors, including loan growth, net charge-offs, changes in the composition of the loan portfolio, delinquencies, management's assessment of the quality of the loan portfolio, the valuation of problem loans and the general economic conditions in our market area.

The provision for loan losses for the year ended December 31, 2017 was $1.3 million compared to $1.7 million for the year ended December 31, 2016, a decrease of $371,000, or 22.1%. The decrease was primarily due to slower growth in our loan portfolio in 2017 compared to in 2016. Our gross loans increased 11% in 2017 compared to 33% in 2016.

The allowance for loan losses as a percentage of loans held for investment was 1.22% at December 31, 2017 and 1.17% at December 31, 2016.

Noninterest Income

While interest income remains the largest single component of total revenues, noninterest income is also an important component. A portion of our noninterest income is associated with SBA lending activity, consisting of gains on the sale of loans sold in the secondary market and servicing income from loans sold with servicing retained. Other sources of noninterest income include loan servicing fees, service charges and fees, and gains on the sale of securities.

Noninterest income for the year ended December 31, 2017 was $9.0 million, a decrease of $21,000, or 0.2%, compared to $9.0 million for the year ended December 31, 2016.

The following table sets forth the various components of our noninterest income for the years ended December 31, 2017 and 2016:

	Year Ended December 31,		
(Dollars in thousands)	**2017**	**2016**	**Increase (decrease)**
Noninterest income:			
Service charges on deposit accounts	$ 1,656	$ 1,275	$ 381
Loan servicing fees, net of amortization	1,127	1,313	(186)

(Dollars in thousands)	2017	2016	Increase (decrease)
	Year Ended December 31,		
Gain on sale of loans	4,939	5,507	(568)
Other income and fees	1,264	912	352
Total noninterest income	$ 8,986	$ 9,007	$ (21)

Total gain on sale of loans was $4.9 million in the year ended December 31, 2017 compared to $5.5 million for the same period of 2016, a decrease of $568,000 or 10.3%.

Gain on sale of SBA loans totaled $4.8 million in the year ended December 31, 2017 compared to $5.4 million for the same period of 2016. We sold $66.2 million in SBA loans with an average premium of 9.30% in the year ended December 31, 2017 compared to the sale of $83.4 million in SBA loans with an average premium of 8.93% in the same period of 2016, primarily due to a lower production in SBA loans in 2017 compared to 2016. We originated $99.7 million of SBA loans in 2017 compared to $111.5 million in 2016. Other loans sold by us during both periods were immaterial.

Loan servicing income, net of amortization decreased by $186,000 to $1.1 million in 2017 compared to $1.3 million in 2016. The decrease in loan servicing income was due, in part, to a $521,000 increase in servicing asset amortization expense, offset by a $335,000 increase in servicing fees. Our total SBA loan servicing portfolio was $309.3 million as of December 31, 2017 compared to $303.8 million as of December 31, 2016. The increase in the servicing portfolio reflects the sales of SBA loans in 2017.

The servicing assets that result from the sales of SBA loans with servicing retained are amortized over the expected term of the loans using a method approximating the interest method. Servicing income generally declines as the respective loans are repaid.

Noninterest Expense

Noninterest expense for the year ended December 31, 2017 was $26.3 million compared to $23.3 million for the year ended December 31, 2016, an increase of $2.9 million, or 12.5%. The following table sets forth the major components of our noninterest expense for the years ended December 31, 2017 and 2016:

(Dollars in thousands)	2017	2016	Increase (decrease)
	Year Ended December 31,		
Noninterest expense:			
Salaries and employee benefits	$ 16,474	$ 14,556	$1,918
Occupancy and equipment	3,918	3,616	302
Data processing and communication	1,323	1,087	236
Professional fees	589	684	(95)
FDIC insurance and regulatory assessments	377	369	8
Promotion and advertising	631	557	74
Directors' fees and stock-based compensation	796	758	38
Foundation donation and other contributions	954	745	209
Other expenses	1,195	962	233
Total noninterest expense	26,257	23,334	2,923

Salaries and employee benefits expense for the year ended December 31, 2017 was $16.5 million compared to $14.6 million for the year ended December 31, 2016, an increase of $1.9 million, or 13.2%. This increase was attributable to an increase in the number of employees to support continued growth, annual salary adjustments,

increased bonus and incentives and increased benefit costs. The average number of full-time equivalent employees was 130.4 in 2017 compared to 125.0 in 2016.

Occupancy and equipment expense for 2017 was $3.9 million compared to $3.6 million for 2016, an increase of $302,000, or 8.4%. This increase was primarily due to the commencement of the lease for the Santa Clara office in mid-2017 which will open in the first quarter of 2018, and the increased rental expense from the lease renewals of the Fashion District and Gardena Offices in 2017.

Data processing and communication expense for 2017 was $1.3 million compared to $1.1 million for 2016, an increase of $236,000, or 21.7%. This increase was primarily due a continued growth in our loans and deposits.

Professional fees for 2017 were $589,000 compared to $684,000 for 2016, a decrease of $95,000, or 13.9%. This decrease was primarily due to the costs incurred in 2016 associated with the formation of OP Bancorp as a bank holding company and the completion of the transactions under which Open Bank became a wholly-owned subsidiary of OP Bancorp, offset by the professional fees incurred in the fourth quarter of 2017 attributable to this offering.

FDIC insurance and regulatory assessment expense for 2017 was $377,000 compared to $369,000 for 2016, an increase of $8,000 or 2.2%. This increase was primarily due to an increase in our FDIC insurance and DBO regulatory assessment as the size of our assets continued to grow.

Promotion and advertising expense for 2017 was $631,000 compared to $557,000 for 2016, an increase of $74,000 or 13.3%. The increase was consistent with a continued growth of our loans and deposits.

Directors' fees and expenses for 2017 were $796,000 compared to $758,000 for 2016, an increase of $38,000 or 5.0%. Directors' fees and expenses include a monthly retainer fee, reimbursement for travel and other expenses, and stock-based expenses relating to equity awards granted in prior years under our equity plans to our directors. Directors' fees and expenses (not including stock-based expenses) for 2017 was $365,000 compared to $327,000 in 2016, an increase of $38,000, or 11.5%. The increase was due to the increase in directors' monthly retainer fees in 2017. Directors' stock-based expenses for 2017 and 2016 were $431,000.

Our aggregate donations to the Foundation and other charitable and community contributions for 2017 were $954,000 compared to $745,000 for 2016, an increase of $209,000, or 28.1%. The increase was due to increased donation accruals for Open Stewardship Foundation, which is directly proportionate to the growth in our after tax income. On an annual basis, we donate 10% of our consolidated net income after taxes to the Foundation.

Other expenses for 2017 were $1.2 million compared to $964,000 in 2016, an increase of $232,000, or 24.1%. The increase was primarily due to increased operating expenses and customer service expenses.

Income Tax Expense

Income tax expense was $7.9 million in 2017 compared to $4.9 million in 2016. The increase in income tax expense was related to growth in pre-tax income and a revaluation of deferred tax assets of $1.3 million, as discussed below. Effective tax rates were 46.1% and 39.7% in 2017 and 2016, respectively.

On December 22, 2017, H.R.1, commonly known as the Tax Cuts and Jobs Act (the "Tax Act"), was signed into law, which among other items reduces the federal corporate tax rate to 21% from 34%, effective January 1, 2018. U.S. generally accepted accounting principles require companies to revalue certain tax-related assets as of the date of enactment of the new legislation with resulting tax effects accounted for in the reporting period of enactment. As a result, we performed an analysis to determine the impact of the revaluation of the net deferred tax asset. The value of the deferred tax asset was reduced by $1.3 million, and recorded as tax expense for the year ended December 31, 2017.

Some items of income and expense are recognized in different years for tax purposes than when applying generally accepted accounting principles leading to timing differences between our actual tax liability, and the amount accrued for this liability based on book income. These temporary differences comprise the "deferred" portion of our tax expense or benefit, which accumulates on our books as a deferred tax asset or deferred tax liability until such time as they reverse.

Realization of deferred tax assets is primarily dependent upon us generating sufficient future taxable income to obtain benefit from the reversal of net deductible temporary differences and the utilization of tax credit carry forwards and the net operating loss carry forwards for Federal and California state income tax purposes. The amount of deferred tax assets considered realizable is subject to adjustment in future periods based on estimates of future taxable income. Under generally accepted accounting principles a valuation allowance is required to be recognized if it is "more likely than not" that the deferred tax assets will not be realized. The determination of the realizability of the deferred tax assets is highly subjective and dependent upon judgment concerning management's evaluation of both positive and negative evidence, including forecasts of future income, cumulative losses, applicable tax planning strategies, and assessments of current and future economic and business conditions.

We had net deferred tax assets of $3.4 million and $3.3 million at December 31, 2017, and December 31, 2016, respectively.

After consideration of the matters in the preceding paragraph, we have determined that it is more likely than not that net deferred tax assets at December 31, 2017 and December 31, 2016 will be fully realized in future years.

Results of Operations—Comparison of Results of Operations for the Years Ended December 31, 2016 and 2015

The following discussion of our results of operations compares the year ended December 31, 2016 to the year ended December 31, 2015.

We reported net income for the year ended December 31, 2016 of $7.4 million compared to net income of $6.0 million for the year ended December 31, 2015. The increase was due to a $5.8 million increase in net interest income and a $1.0 million increase in noninterest income offset by a $3.5 million increase in noninterest expense and a $1.1 million increase in provision for loan losses and a $700,000 increase in provision for income taxes.

Net Interest Income

The following table presents, for the periods indicated, information about our: (i) weighted average balances, the total dollar amount of interest income from interest-earning assets and the resultant average yields; (ii) average balances, the total dollar amount of interest expense on interest-bearing liabilities and the resultant average rates; (iii) net interest income; (iv) the interest rate spread; and (v) the net interest margin.

	Year Ended December 31,					
	2016			2015		
(Dollars in thousands)	**Average Balance**	**Interest and Fees**	**Yield / Rate**	**Average Balance**	**Interest and Fees**	**Yield / Rate**
Earning assets:						
Federal funds sold and other investments (1)	$ 26,213	$ 507	1.93%	$ 36,963	$ 383	1.04%
Securities available for sale	40,159	664	1.65	28,577	480	1.68
Total investments	66,372	1,171	1.76	65,540	863	1.32
Real estate	315,244	14,046	4.46	243,621	10,963	4.50
SBA	103,313	7,414	7.18	84,751	6,088	7.18
Commercial & Industrial	73,803	3,845	5.21	64,702	3,066	4.74
Home Mortgage	88,282	4,694	5.32	68,979	3,698	5.36
Consumer	5,986	531	8.87	7,774	514	6.61

(Dollars in thousands)	2016 Average Balance	2016 Interest and Fees	2016 Yield / Rate	2015 Average Balance	2015 Interest and Fees	2015 Yield / Rate
	Year Ended December 31,					
Loans (2)	586,628	30,530	5.20	469,827	24,329	5.18
Total earning assets	653,000	31,701	4.85	535,367	25,192	4.70
Noninterest-earning assets	32,617			30,800		
Total assets	685,617			566,167		
Interest-bearing liabilities:						
NOW and savings deposits	4,058	10	0.25%	3,276	8	0.24%
Money market deposits	202,737	1,736	0.86	163,887	1,505	0.92
Time deposits	181,191	1,540	0.85	151,715	1,092	0.72
Total interest-bearing deposits	387,986	3,286	0.85	318,878	2,605	0.82
Borrowings	16,986	85	0.50	20,001	84	0.42
Total interest-bearing liabilities	404,972	3,371	0.83	338,879	2,689	0.79
Noninterest-bearing liabilities:						
Noninterest-bearing deposits	198,413			153,435		
Other noninterest-bearing liabilities	5,585			4,784		
Total noninterest-bearing liabilities	203,998			158,219		
Shareholders' equity	76,647			69,069		
Total liabilities and shareholders' equity	$685,617			$566,167		
Net interest income / interest rate spreads		$28,330	4.02%		$22,503	3.91%
Net interest margin			4.34%			4.20%

(1) Includes income and average balances for FHLB and PCBB stock, term federal funds, interest-earning time deposits and other miscellaneous interest-earning assets.
(2) Average loan balances include non-accrual loans and loans held for sale.

Increases and decreases in interest income and interest expense result from changes in average balances (volume) of interest-earning assets and interest-bearing liabilities, as well as changes in average interest rates. The following tables set forth the effects of changing rates and volumes on our net interest income during the period shown. Information is provided with respect to (i) effects on interest income attributable to changes in volume (change in volume multiplied by prior rate) and (ii) effects on interest income attributable to changes in rate (changes in rate multiplied by prior volume). Change applicable to both volume and rate have been allocated to volume.

	Year Ended December 31, 2016 over 2015		
	Increase (Decrease) Due to Change due in:		
(Dollars in thousands)	Average Volume	Average Rate	Net Interest Variance
Earning assets:			
Federal funds sold and other investments	$ (135)	$ 259	$ 124
Securities available for sale	194	(10)	184
Total investments	59	249	308
Real estate	3,182	(99)	3,083
SBA	1,326	—	1,326
Commercial & Industrial	457	322	779
Home Mortgage	1,024	(28)	996
Consumer	(134)	151	17
Total loans	5,855	346	6,201
Total earning assets	5,914	595	6,509
Expense from interest-bearing liabilities			
NOW and savings deposits	$ 2	$ —	$ 2
Money market deposits	335	(104)	231
Time deposits	232	216	448
Total interest-bearing deposits	569	112	681
Borrowings	(14)	15	1
Total interest-bearing liabilities	555	127	682
Net interest income	$5,359	$ 468	$5,827

Net interest income for the year ended December 31, 2016 was $28.3 million compared to $22.5 million for the year ended December 31, 2015, an increase of $5.8 million, or 25.9%. This increase was primarily due to a 22.0% increase in the average balance of interest-earning assets, coupled with a 15 basis point improvement in the average yield on interest-earning assets. The increase in the average balance of interest-earning assets was primarily due to an increase in average loans outstanding. The increase in the average yield on interest-earning assets was primarily due to an increase in the federal funds rate of 25 basis points in December 2015.

Total interest income was $31.7 million in 2016 compared to $25.2 million in 2015, an increase of $6.5 million, or 25.8%. This increase was primarily due to an increase in interest earned on our loan portfolio. Interest and fees on loans was $30.5 million in 2016 compared to $24.3 million in 2015, an increase of $6.2 million, or 25.5%. This increase in interest income on loans was primarily due to a 24.9% increase in the average balance of loans outstanding. The increase in the average balance of loans outstanding was primarily due to continued organic growth in most of our loan categories.

Interest income on total investments increased $308,000, or 35.7%, to $1.2 million in 2016 compared to $864,000 in 2015. Interest income on the securities portfolio increased $184,000, or 38.3%, to $664,000 in 2016

compared to $480,000 in 2015. The increase in interest income on the securities portfolio was primarily due to a $11.6 million, or 40.5%, increase in the average balance of our securities portfolio. We purchased $30.1 million of home mortgage-backed securities and collateralized mortgage obligations in 2015. Interest income on federal funds sold, cash equivalents and other investments increased $124,000, or 32.0%, to $507,000 in 2016 from $383,000 in 2015 primarily due to an increase of $95,000 in FHLB stock dividend in 2016.

Total interest expense was $3.4 million in 2016 compared to $2.7 million in 2015, an increase of $700,000, or 25.4%. The increase was primarily due to increases in interest expense on deposits. Interest expense on deposits was $3.3 million in 2016 compared to $2.6 million in 2015, an increase of $700,000, or 26.1%. This increase was primarily due to a 21.7% increase in the average balance of interest-bearing deposits, coupled with a three basis point increase in the average interest rate paid.

Net interest margins for the years ended December 31, 2016 and 2015 were 4.34% and 4.20%, respectively.

Provision for Loan Losses

The provision for loan losses for the year ended December 31, 2016 was $1.7 million compared to $553,000 for the year ended December 31, 2015, an increase of $1.1 million, or 204%, which was primarily due to the growth of our loan portfolio. The allowance for loan losses as a percentage of loans was 1.17% at December 31, 2016 and 1.26% at December 31, 2015.

Noninterest Income

Noninterest income for the year ended December 31, 2016 was $9.0 million compared to $8.0 million for the year ended December 31, 2015, an increase of $1.0 million, or 12.9%. The following table sets forth the various components of our noninterest income for the years ended December 31, 2016 and 2015:

	Year Ended December 31,		
(Dollars in thousands)	**2016**	**2015**	**Increase (decrease)**
Noninterest Income:			
Service charges on deposit accounts	$ 1,275	$ 1,278	$ (3)
Loan servicing fees, net of amortization	1,313	1,131	182
Gain on sale of loans	5,507	4,669	838
Other income and fees	912	900	12
Total noninterest income	$ 9,007	$ 7,978	$1,029

Total gain on sale of loans during 2016 was $5.5 million in the year ended December 31, 2016 compared to $4.7 million for the same period of 2015, an increase of $800,000 or 17.9%.

Gain on sale of SBA loans totaled $5.4 million in the year ended December 31, 2016 compared to $4.6 million for the same period of 2015. We sold $83.4 million in SBA loans with an average premium of 8.93% in the year ended December 31, 2016 compared to the sale of $64.8 million with an average premium of 9.46% in the same period of 2015. Other loans sold by us during the period were immaterial.

Loan servicing income, net of amortization increased by $200,000 to $1.3 million in 2016 compared to $1.1 million in 2015. The increase in loan servicing income was due to an increase in SBA loans being serviced. Our total SBA loan servicing portfolio was $303.8 million as of December 31, 2016 compared to $260.5 million as of December 31, 2015. The increase in the servicing portfolio reflects the growth in our originations and sales of SBA loans in 2016.

Noninterest Expense

Noninterest expense for the year ended December 31, 2016 was $23.3 million compared to $19.8 million for the year ended December 31, 2015, an increase of $3.5 million, or 17.9%. The following table sets forth the various components of our noninterest expense for the years ended December 31, 2016 and 2015:

	Year Ended December 31,		
(Dollars in thousands)	**2016**	**2015**	**Increase (decrease)**
Noninterest expense:			
Salaries and employee benefits	$ 14,556	$ 12,253	$2,303
Occupancy and equipment	3,616	3,162	454
Data processing and communication	1,087	784	303
Professional fees	684	413	271
FDIC insurance and regulatory assessments	369	307	62
Promotion and advertising	557	532	25
Directors' fees and stock-based compensation	758	784	(26)
Foundation donation and other contributions	745	602	143
Other expenses	962	958	4
Total noninterest expense	23,334	19,795	3,539

Salaries and employee benefits expense for the year ended December 31, 2016 was $14.6 million compared to $12.3 million for the year ended December 31, 2015, an increase of $2.3 million, or 18.8%. This increase was attributable to an increase in the number of employees to support continued growth, annual salary adjustments, increased bonus and incentives and increased benefit costs. The number of full-time equivalent employees was 129.5 at December 31, 2016 compared to 115.5 at December 31, 2015.

Occupancy and equipment expense for 2016 was $3.6 million compared to $3.2 million for 2015, an increase of $454,000, or 14.4%. This increase was mainly due to the opening of the Western office in mid-2015 and the three loan production offices in 2016.

Data processing and communication expense for 2016 was $1.1 million compared to $784,000 for 2015, an increase of $303,000, or 38.6%. This increase was primarily due a continued growth in operations.

Professional fees for 2016 was $684,000 compared to $413,000 for 2015, and increase of $271,000, or 65.6%. This increase was primarily due to higher costs associated with the PCAOB standards audit conducted during 2016 for years 2016 and 2015 and the costs incurred in 2016 associated with the formation of OP Bancorp as a bank holding company and completion of the transactions under which Open Bank became a wholly-owned subsidiary of OP Bancorp.

FDIC insurance and regulatory assessment expense for 2016 was $369,000 compared to $307,000 for 2015, an increase of $62,000 or 20.2%. This increase was primarily due to an increase in our FDIC insurance and DBO regulatory assessment as we continued to grow in assets.

Promotion and advertising expense for 2016 was $557,000 compared to $532,000 for 2015, an increase of $25,000 or 4.7%. The increase was consistent with a continued growth of our loans and deposits.

Directors' fees and expenses for 2016 were $758,000 compared to $784,000 for 2015, a decrease of $26,000 or 3.3%. Directors' fees and expenses include a monthly retainer fee, reimbursement for traveling and other expenses, and stock-based expenses relating to equity awards granted in prior years under our equity plans to our directors. Directors' fees and expenses (not including stock-based expenses) for 2016 was $327,000 compared to

$282,000 for 2015, an increase of $45,000, or 16.0%. The increase was due to the increase in directors' monthly retainer fees in 2016. Director's stock-based expenses for 2016 was $431,000 compared to $502,000 for 2015, a decrease of $71,000, or 14.1%. The decrease was the result of more stock options vesting in 2015 compared to 2016.

Our aggregate donations to the Foundation and other charitable and community contributions for 2016 were $745,000 compared to $602,000 for 2015, an increase of $143,000, or 23.8%.

Income Tax Expense

Income tax expense was $4.9 million in 2016 compared to $4.2 million in 2015. The increase in income tax expense was consistent with the related growth in our pre-tax income. Our effective tax rates were 39.7% and 41.2% in 2016 and 2015, respectively. The lower effective tax rate in 2016 was primarily due to benefits recognized from the change in tax accounting associated with the treatment of our stock options.

Financial Condition

Total assets increased $139.7 million, or 18.4%, to $901.0 million at December 31, 2017 as compared to $761.3 million at December 31, 2016. This increase primarily resulted from an increase of $73.8 million, or 10.9%, in gross loans and an increase of $43.1 million in cash and cash equivalents. We funded our asset growth primarily with an increase of $111.5 million in deposits and additional advances from FHLB of $15.0 million.

Investment portfolio

The securities portfolio is the second largest component of our interest earning assets, and the structure and composition of this portfolio is important to an analysis of our financial condition. The portfolio serves the following purposes: (i) it provides a source of pledged assets for securing certain deposits and borrowed funds, as may be required by law or by specific agreement with a depositor or lender; (ii) it provides liquidity to even out cash flows from the loan and deposit activities of customers; (iii) it can be used as an interest rate risk management tool, because it provides a large base of assets, the maturity and interest rate characteristics of which can be changed more readily than the loan portfolio to better match changes in the deposit base and our other funding sources; and (iv) it is an alternative interest-earning use of funds when loan demand is weak or when deposits grow more rapidly than loans.

We classify our securities as either available-for-sale or held-to-maturity at the time of purchase. Accounting guidance requires available-for-sale securities to be marked to fair value with an offset to accumulated other comprehensive income (loss), a component of shareholders' equity. Monthly adjustments are made to reflect changes in the fair value of our available-for-sale securities.

All of the securities in our investment portfolio were classified as available-for-sale at December 31, 2017. There were no held-to-maturity or trading securities in our investment portfolio at December 31, 2017. All available-for-sale securities are carried at fair value. Securities available-for-sale consist primarily of US government-sponsored agency securities, home mortgage-backed securities and collateralized mortgage obligations.

Securities available-for-sale increased $6.0 million, or 16.9%, to $41.5 million at December 31, 2017 from $35.5 million at December 31, 2016. Securities available-for-sale decreased $8.4 million to $35.5 million at December 31, 2016 from $43.9 million at December 31, 2015. No issuer of the available-for-sale securities, other than FNMA and FHLMC, comprised more than ten percent of our shareholders' equity as of December 31, 2017, 2016, or 2015.

The following table summarizes the fair value of the available-for-sale securities portfolio as of the dates presented.

(Dollars in thousands)	December 31, 2017			December 31, 2016			December 31, 2015		
	Amortized Cost	Fair Value	Unrealized Gain/(Loss)	Amortized Cost	Fair Value	Unrealized Gain/(Loss)	Amortized Cost	Fair Value	Unrealized Gain/(Loss)
Available for sale:									
U.S. Government agencies	$ 6,989	$ 6,932	$ (57)	$ 6,984	$ 6,977	$ (7)	$ 7,978	$ 7,949	$ (29)
Mortgage-backed securities—residential	14,109	13,941	(168)	17,721	17,556	(165)	22,615	22,444	(171)
Collateralized mortgage obligations	18,459	18,113	(346)	11,124	10,930	(194)	13,690	13,496	(194)
Other securities	2,518	2,486	(32)	—	—	—	—	—	—
Total available for sale	$42,075	$41,472	$ (603)	$35,829	$35,463	$ (366)	$44,283	$43,889	$ (394)

Certain securities have fair values less than amortized cost and, therefore, contain unrealized losses. At December 31, 2017, we evaluated the securities which had an unrealized loss for other than temporary impairment (OTTI) and determined all decline in value to be temporary. We anticipate full recovery of amortized cost with respect to these securities by maturity, or sooner in the event of a more favorable market interest rate environment. We do not intend to sell these securities and it is not more likely than not that we will be required to sell them before recovery of the amortized cost basis, which may be at maturity.

The following table sets forth certain information regarding contractual maturities and the weighted average yields of our investment securities as of the dates presented. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties. We have no securities with contractual maturities due in one year or less as of December 31, 2017.

(Dollars in thousands)	As of December 31, 2017					
	Due after One Year Through Five Years		Due after Five Years Through Ten Years		Due after Ten Years	
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield
Available for sale:						
U.S. Government agencies	$6,989	1.68%	$ —	—	$ —	—
Mortgage-backed securities—residential	—	—	5,545	1.98%	8,564	1.89%
Collateralized mortgage obligations	—	—	—	—	18,459	2.03%
Other securities	—	—	—	—	2,518	—
Total available for sale	6,989	1.68%	$ 5,545	1.98%	$29,541	1.82%

We have not used interest rate swaps or other derivative instruments to hedge fixed rate loans or securities to otherwise mitigate interest rate risk.

Loans

Our loans represent the largest portion of our earning assets, substantially greater than the securities portfolio or any other asset category, and the quality and diversification of the loan portfolio is an important consideration when reviewing our financial condition.

At December 31, 2017, gross loans including deferred costs totaled $748.0 million compared to $674.2 million at December 31, 2016 and $507.3 million at December 31, 2015.

The loan distribution table that follows sets forth our gross loans outstanding, and the percentage distribution in each category as of the dates indicated:

(Dollars in thousands)	As of December 31, 2017 Amount	2017 % of Total	2016 Amount	2016 % of Total	2015 Amount	2015 % of Total
Real estate:						
Commercial real estate	$420,760	56%	$362,585	54%	$272,394	54%
SBA loans—real estate	106,924	14%	97,411	14%	75,641	15%
Total real estate	527,684	70%	459,996	68%	348,035	69%
SBA loan—non-real estate	8,635	1%	6,875	1%	6,814	1%
Commercial and industrial	103,681	14%	97,660	14%	70,629	14%
Home mortgage	104,068	13.9%	104,809	16%	76,866	15%
Consumer	3,955	1%	4,887	1%	4,942	1%
Gross loans	748,023	100%	674,227	100%	507,286	100%
Allowance for loan losses	(9,139)		(7,910)		(6,390)	
Net loans	$738,884		$666,317		$500,896	

Gross loans increased $73.8 million, or 10.9%, to $748.0 million as of December 31, 2017 compared to $674.2 million as of December 31, 2016. The increase in our gross loans resulted from organic growth in most of our loan categories.

The following tables presents the maturity distribution of our loans as of December 31, 2017 and 2016. The table shows the distribution of such loans between those loans with predetermined (fixed) interest rates and those with variable (floating) interest rates.

	As of December 31, 2017						
	Due in One Year or Less		Due after One Year Through Five Years		Due after Five Years		
(Dollars in thousands)	Fixed Rate	Adjustable Rate	Fixed Rate	Adjustable Rate	Fixed Rate	Adjustable Rate	Total
Real estate:							
Commercial real estate	$24,364	$38,629	$171,457	$ 88,328	$ 39,120	$ 58,862	$420,760
SBA loans—real estate	—	—	—	—	—	106,924	106,924
Total real estate	24,364	38,629	171,457	88,328	39,120	165,786	527,684
SBA loan—non-real estate	—	—	—	764	—	7,871	8,635
Commercial and industrial	—	58,900	2,188	25,876	—	16,717	103,681
Home mortgage	—	—	—	—	104,068	—	104,068
Consumer	—	1,821	11	1,202	—	921	3,955
Gross loans	$24,364	$99,350	$173,656	$116,170	$143,188	$191,295	$748,023

(Dollars in thousands)	As of December 31, 2016						
	Due in One Year or Less		Due after One Year Through Five Years		Due after Five Years		
	Fixed Rate	Adjustable Rate	Fixed Rate	Adjustable Rate	Fixed Rate	Adjustable Rate	Total
Real estate:							
Commercial real estate	$ 4,541	$26,034	$183,869	$41,074	$ 62,842	$ 44,225	$362,585
SBA loans—real estate	—	—	—	—	—	97,411	97,411
Total real estate	4,541	26,034	183,869	41,074	62,842	141,636	459,996
SBA loan—non-real estate	—	15	—	701	—	6,159	6,875
Commercial and industrial	75	46,933	2,908	25,248	—	22,496	97,660
Home mortgage	—	—	—	—	104,809	—	104,809
Consumer	—	2,548	—	1,419	—	920	4,887
Gross loans	$ 4,616	$75,530	$186,777	$68,442	$167,651	$171,211	$674,227

Our loan portfolio is concentrated in commercial real estate, commercial (primarily manufacturing, wholesale, and services oriented entities), SBA loans (unguaranteed portion) with the remaining balance in home mortgage, and consumer loans. We do not have any material concentrations by industry or group of industries in the loan portfolio. However, 84.5% of our gross loans was secured by real property as of December 31, 2017, compared to 83.8% as of December 31, 2016.

We have established concentration limits in the loan portfolio for commercial real estate loans, commercial and industrial loans, and unsecured lending, among others. All loan types are within established limits. We use underwriting guidelines to assess the borrowers' historical cash flow to determine debt service, and we further stress test the debt service under higher interest rate scenarios. Financial and performance covenants are used in commercial lending agreements to allow us to react to a borrower's deteriorating financial condition, should that occur.

Commercial real estate loans include owner-occupied and non-occupied commercial real estate. We originate both fixed and adjustable rate loans. Adjustable rate loans are based on the *Wall Street Journal* prime rate. At December 31, 2017, approximately 56% of the commercial real estate portfolio consisted of fixed-rate loans. Our policy maximum loan-to-value, or LTV, is 70% for commercial real estate loans. At December 31, 2017, our average loan to value for commercial real estate loans was 72.1%. Our commercial real estate loan portfolio totaled $420.8 million at December 31, 2017 compared to $362.6 million at December 31, 2016.

We are designated an SBA Preferred Lender under the SBA Preferred Lender Program. We offer mostly SBA 7(a) variable-rate loans. We generally sell the 75% guaranteed portion of the SBA loans that we originate. Our SBA loans are typically made to small-sized manufacturing, wholesale, retail, hotel/motel and service businesses for working capital needs or business expansions. SBA loans have maturities up to 25 years. Typically, non-real estate secured loans mature in less than 10 years. Collateral may also include inventory, accounts receivable and equipment, and may include personal guarantees. Our unguaranteed SBA loans collateralized by real estate are monitored by collateral type and included in our CRE Concentration Guidance.

As of December 31, 2017 our SBA portfolio totaled $115.6 million compared to $104.3 million as of December 31, 2016. These increases were primarily due to continued growth of our SBA loan portfolio partially offset by the sales of those loans. We originated $99.7 million and $111.5 million during the years ended December 31, 2017 and 2016, respectively. We sold $66.2 million and $83.4 million of SBA loans during the years ended December 31, 2017 and 2016, respectively.

From our total SBA loan portfolio, $106.9 million is secured by real estate and $8.6 million is unsecured or secured by business assets at December 31, 2017.

Commercial and industrial loans totaled $103.7 million at December 31, 2017 compared to $97.7 million at December 31, 2016 and $70.6 million at December 31, 2015. The increase resulted primarily from organic loan growth.

We originate mainly non-qualified, alternative documentation single-family home mortgage loans ("home mortgage") primarily through broker relationships, but also through our branch network. The loan product is a five-year or seven-year hybrid adjustable rate mortgage which reprices after five years to the one-year LIBOR plus certain spreads. We originate the non-qualified single-family home mortgage loans held by us for investment.

Home mortgage loans totaled $104.1 million at December 31, 2017 compared to $104.8 million at December 31, 2016, a decrease of $700,000, or 0.7%. The decrease was primarily due to lower loan origination and higher loan payoffs in 2017 compared to 2016. During the year ended December 31, 2017, we originated $42.1 million and sold $9.5 million in home mortgage loans. Payoffs and paydowns for the same period were $31.2 million and $2.8 million, respectively. During the same period in 2016, we originated $53.3 million and sold $5.8 million in home mortgage loans. Payoffs and paydowns for the same period were $17.3 million and $2.3 million, respectively.

Loan Servicing

As of December 31, 2017, 2016, and 2015, we serviced $309.3 million, $303.8 million, and $260.5 million respectively, of SBA loans for others. Activity for loan servicing rights was as follows:

	Year Ended December 31,		
(Dollars in thousands)	**2017**	**2016**	**2015**
Beginning balance	$ 6,783	$ 5,551	$ 4,670
Additions	1,923	2,645	2,148
Amortized to expense	(1,935)	(1,413)	(1,267)
Ending balance	$ 6,771	$ 6,783	$ 5,551

Loan servicing rights are included in accrued interest receivable and other assets on our consolidated balance sheets and reported net of amortization.

Allowance for loan losses

The allowance for loan losses is an estimate of probable incurred losses in the loan portfolio. Loans are charged-off against the allowance when management believes a loan balance is uncollectible. Subsequent recoveries, if any, are credited to the allowance for loan losses. Management's methodology for estimating the allowance balance consists of several key elements, which include specific allowances on individual impaired loans and the formula driven allowances on pools of loans with similar risk characteristics. 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 for loan losses is determined on a quarterly basis and reflects management's estimate of probable incurred credit losses inherent in the loan portfolio. We also rely on internal and external loan review procedures to further assess individual loans and loan pools, and economic data for overall industry and geographic trends. The computation includes element of judgment and high levels of subjectivity.

A loan is considered impaired when it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. Impaired loans include loans on non-accrual status and performing restructured loans. Income from loans on non-accrual status is recognized to the extent cash is

received and when the loan's principal balance is deemed collectible. Depending on a particular loan's circumstances, we measure impairment of a loan based upon either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price, or the fair value of the collateral less estimated costs to sell if the loan is collateral dependent. A loan is considered collateral dependent when repayment of the loan is based solely on the liquidation of the collateral. Fair value, where possible, is determined by independent appraisals, typically on an annual basis. Between appraisal periods, the fair value may be adjusted based on specific events, such as if deterioration of quality of the collateral comes to our attention as part of our problem loan monitoring process, or if discussions with the borrower lead us to believe the last appraised value no longer reflects the actual market value for the collateral. The impairment amount on a collateral-dependent loan is charged-off to the allowance if deemed not collectible and the impairment amount on a loan that is not collateral-dependent is set up as a specific reserve.

In cases where a borrower experiences financial difficulties and we make certain concessionary modifications to contractual terms, the loan is classified as a troubled debt restructuring. These concessions may include a reduction of the interest rate, principal or accrued interest, extension of the maturity date or other actions intended to minimize potential losses. Loans restructured at a rate equal to or greater than that of a new loan with comparable risk at the time the loan is modified may be excluded from restructured loan disclosures in years subsequent to the restructuring if the loans are in compliance with their modified terms. A restructured loan is considered impaired despite its accrual status and a specific reserve is calculated based on the present value of expected cash flows discounted at the loan's effective interest rate or the fair value of the collateral less estimated costs to sell if the loan is collateral dependent. Interest income on impaired loans is accrued as earned, unless the loan is placed on non-accrual status.

The allowance for loan losses was $9.1 million at December 31, 2017 compared to $7.9 million at December 31, 2016, an increase of $1.2 million, or 15.5%. The increase was primarily due to the overall growth in the size of our gross loan portfolio, which grew $73.8 million, or 10.9%, to $748.0 million at December 31, 2017 from $674.2 million at December 31, 2016.

In determining the allowance and the related provision for loan losses, we consider three principal elements: (i) valuation allowances based upon probable losses identified during the review of impaired commercial and industrial, commercial real estate, construction and land development loans, (ii) allocations, by loan classes, on loan portfolios based on historical loan loss experience and qualitative factors and (iii) review of the credit discounts in relationship to the valuation allowance calculated for purchased loans. Provisions for loan losses are charged to operations to record changes to the total allowance to a level deemed appropriate by us.

It is the policy of management to maintain the allowance for loan losses at a level adequate for risks inherent in the loan portfolio. The Federal Reserve Board and the California Department of Business Oversight also review the allowance for loan losses as an integral part of their examination process. Based on information currently available, management believes that our allowance for loan losses is adequate. However, the loan portfolio can be adversely affected if California economic conditions and the real estate market in our market area were to weaken. The effect of such events, although uncertain at this time, could result in an increase in the level of nonperforming loans and increased loan losses, which could adversely affect our future growth and profitability. No assurance of the ultimate level of credit losses can be given with any certainty.

Analysis of the Allowance for Loan Losses.

The following table provides an analysis of the allowance for loan losses, provision for loan losses and net charge-offs, by category, for the years ended December 31, 2017, 2016 and 2015.

	As of and For the Year Ended December 31, 2017			As of and For the Year Ended December 31, 2016			As of and For the Year Ended December 31, 2015		
(Dollars in thousands)	Provision	Net Charge-offs	ALL Balance	Provision	Net Charge-offs	ALL Balance	Provision	Net Charge-offs	ALL Balance
Real estate:									
Commercial real estate	$ 584	$ —	$ 4,801	$ 985	$ —	$ 4,217	$ 751	$ —	$ 3,232
SBA loans—real estate	189	—	1,082	189	—	893	(42)	1	704
Total real estate	773	—	5,883	1,174	—	5,110	709	1	3,936
SBA loan—non-real estate	633	155	538	(50)	20	59	(7)	(7)	129
Commercial and industrial	(57)	—	1,265	130	142	1,322	(336)	(70)	1,334
Home mortgage	44	(73)	1,408	427	—	1,364	227	—	937
Consumer	(83)	—	45	1	—	55	(40)	(4)	54
Total	$ 1,310	$ 82	$ 9,139	$ 1,682	$162	$ 7,910	$ 553	$ (80)	$ 6,390
Gross loans			$ 748,023			$ 674,227			$ 507,286
Average gross loans			705,748			578,262			462,870
Net charge-offs to average loans(1)			0.01%			0.03%			(0.02)%
Allowance for loans losses to gross loans			1.22%			1.17%			1.26%

(1) Net charge-offs are loan charge-offs net of loan recoveries.

Non-performing Loans

Loans are considered delinquent when principal or interest payments are past due 30 days or more. Delinquent loans may remain on accrual status between 30 days and 90 days past due. Loans on which the accrual of interest has been discontinued are designated as non-accrual loans. Typically, the accrual of interest on loans is discontinued when principal or interest payments are past due 90 days or when, in the opinion of management, there is a reasonable doubt as to collectability in the normal course of business. When loans are placed on non-accrual status, all interest previously accrued but not collected is reversed against current period interest income. Income on non-accrual loans is subsequently recognized only to the extent that cash is received and the loan's principal balance is deemed collectible. Loans are restored to accrual status when loans become well-secured and management believes full collectability of principal and interest is probable.

Real estate we acquire as a result of foreclosure or by deed-in-lieu of foreclosure is classified as OREO until sold, and is initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. We had no OREO at December 31, 2017, 2016 and 2015.

Non-performing loans include loans 90 days past due and still accruing, loans accounted for on a non-accrual basis and accruing restructured loans. Non-performing assets consist of non-performing loans plus OREO.

Non-performing loans were $1.0 million at December 31, 2017 compared to $576,000 at December 31, 2016 and $1.0 million at December 31, 2015. The increase in the year ended December 31, 2017 was primarily due to two non-accrual home mortgage loans which were non-performing. The decrease in the year ended December 31, 2016 was primarily due to one large principal paydown on one of the non-performing loans. We did not recognize any interest income on non-accrual loans during the years ended December 31, 2017, 2016 and 2015 while the loans were in non-accrual status. Additional interest income that we would have recognized on these loans had they been current in accordance with their original terms was $10,000 in the year ended December 31, 2016 and $5,000 for the same period of 2015. There was no such additional interest income in the year ended December 31, 2017.

We recognized interest income on loans modified under troubled debt restructurings of $9,000 in the year ended December 31, 2017, $25,000 in the year ended December 31, 2016, and $34,000 in the year ended December 31, 2015.

The following table sets forth the allocation of our non-performing assets among our different asset categories as of the dates indicated. Non-performing loans include non-accrual loans, loans past due 90 days or more and still accruing interest, and loans modified under troubled debt restructurings.

	As of December 31,		
(Dollars in thousands)	**2017**	**2016**	**2015**
Non-accrual loans	$ 683	$ 209	$ 657
Past due loans 90 days or more and still accruing	—	—	—
Accruing troubled debt restructured loans	354	367	382
Total non-performing loans	1,037	576	1,039
Other real estate owned	—	—	—
Total non-performing assets	$1,037	$ 576	$1,039
Non-performing loans to gross loans	0.14%	0.09%	0.20%
Non-performing assets to total assets	0.12%	0.08%	0.17%
Allowance for loan losses to non-performing loans	881%	1373%	615%

In addition to the nonperforming assets described above we have a lending relationship with two companies that are affiliated with each other comprised of two loans to a retail company and one loan to a related online company totaling $1.9 million. These loans were current at December 31, 2017 and accordingly, they were not included in the nonperforming asset categories above. In March 2018, even though the loans were current, the retail company with a $1.4 million loan outstanding filed for reorganization under Chapter 11 of the federal bankruptcy laws. We will reassess the risk ratings and potential loss exposure of these loans on a prospective basis as we continue to work with the borrower and obtain further information. The $500,000 loan to the online company, representing the balance of the borrowing relationship, is current and remains a performing loan.

Deposits

We gather deposits primarily through our branch locations. We offer a variety of deposit products including demand deposits accounts, interest-bearing products, savings accounts and certificate of deposits. We put continued effort into gathering noninterest demand deposits accounts through marketing to our existing and new loan customers, customer referrals, our marketing staff and various involvement with community networks.

Total deposits at December 31, 2017 were $773.3 million, representing an increase of $111.5 million, or 16.9%, compared to $661.8 million at December 31, 2016. As of December 31, 2017, 37.4% of total deposits were comprised of noninterest-bearing demand accounts, 32.5% of interest-bearing transaction accounts and 30.1% of time deposits.

Total deposits at December 31, 2016 were $661.8 million, representing an increase of $142.1 million, or 27.3%, compared to $519.7 million at December 31, 2015. As of December 31, 2016, 37.4% of total deposits were comprised of noninterest-bearing demand accounts, 35.2% of interest-bearing transaction accounts and 27.4% of time deposits.

The following table summarizes our average deposit balances and weighted average rates for the years ended December 31, 2017, 2016 and 2015:

	As of December 31,					
	2017		2016		2015	
(Dollars in thousands)	Average Balance	Weighted Average Rate	Average Balance	Weighted Average Rate	Average Balance	Weighted Average Rate
Noninterest-bearing demand	$256,267	—%	$198,413	—%	$153,435	—%
Interest-bearing:						
NOW and Savings deposits	6,137	0.25	4,058	0.25	3,276	0.25
Money market	258,019	0.91	202,737	0.86	163,888	0.92
Time deposits ($250,000 or less)	106,676	1.08	108,912	0.94	58,882	0.74
Time deposits (more than $250,000)	90,155	1.06	72,279	0.71	92,832	0.71
Total interest-bearing	460,987	0.97	387,986	0.85	318,878	0.82
Total deposits	$717,254	0.62	$586,399	0.56	$472,313	0.55

The following tables set forth the maturity of time deposits as of December 31, 2017 and 2016:

	As of December 31, 2017 Maturity Within:				
(Dollars in thousands)	Three Months	Three to Six Months	Six to 12 Months	After 12 Months	Total
Time deposits ($250,000 or less)	$ 49,491	$28,128	$37,414	$ 8,748	$123,781
Time deposits (more than $250,000)	52,245	13,673	36,832	6,202	108,952
Total time deposits	$101,736	$41,801	$74,246	$14,950	$232,733

	As of December 31, 2016 Maturity Within:				
(Dollars in thousands)	Three Months	Three to Six Months	Six to 12 Months	After 12 Months	Total
Time deposits ($250,000 or less)	$14,302	$15,801	$31,060	$10,441	$ 71,604
Time deposits (more than $250,000)	35,699	53,235	15,497	5,600	110,031
Total time deposits	$50,001	$69,036	$46,557	$16,041	$181,635

Borrowed Funds

Other than deposits, we also utilized FHLB advances as a supplementary funding source to finance our operations. The advances from the FHLB are collateralized by residential and commercial real estate loans. At December 31, 2017, 2016 and 2015, we had maximum borrowing capacity from the FHLB of $308.5 million, $248.3 million and $211.3 million, respectively. We had $25 million of advances from FHLB at December 31, 2017, compared to $10 million at December 31, 2016 and $20 million at December 31, 2015.

Liquidity

Liquidity refers to the measure of our ability to meet the cash flow requirements of depositors and borrowers, while at the same time meeting our operating, capital and strategic cash flow needs, all at a reasonable cost. We continuously monitor our liquidity position to ensure that assets and liabilities are managed in a manner that will meet all short-term and long-term cash requirements. We manage our liquidity position to meet the daily cash flow needs of customers, while maintaining an appropriate balance between assets and liabilities to meet the return on investment objectives of our shareholders.

Our liquidity position is supported by management of liquid assets and access to alternative sources of funds. Our liquid assets include cash, interest-bearing deposits in correspondent banks, federal funds sold, and fair value of unpledged investment securities. Other available sources of liquidity include wholesale deposits, and additional borrowings from correspondent banks, FHLB advances, and the Federal Reserve discount window.

Our short-term and long-term liquidity requirements are primarily met through cash flow from operations, redeployment of prepaying and maturing balances in our loan and investment portfolios, and increases in customer deposits. Other alternative sources of funds will supplement these primary sources to the extent necessary to meet additional liquidity requirements on either a short-term or long-term basis.

As of December 31, 2017, 2016 and 2015, we had $9.5 million of unsecured federal funds lines with no amounts advanced. In addition, on such dates we had lines of credit from the Federal Reserve discount window of $92.8 million, $84.0 million and $45.1 million, respectively. The Federal Reserve discount window lines were collateralized by a pool of commercial real estate loans and commercial and industrial loans totaling $156.2 million, $152.9 million and $92.3 million as of December 31, 2017, 2016 and 2015, respectively. We did not have any borrowings outstanding with the Federal Reserve at December 31, 2017, 2016 or 2015, and our borrowing capacity is limited only by eligible collateral.

At December 31, 2017 we had a $25 million advance from the FHLB which had an overnight borrowing interest rate of 1.41%. We had a $10 million FHLB advance outstanding at December 31, 2016 which was an overnight borrowing at an interest rate of 0.55%. At December 31, 2015, we had an aggregate of $20 million of outstanding advances from FHLB of which $10 million was a one year advance maturing on June 2, 2016 at an interest rate of 0.49% and $10 million was a one year advance maturing on August 8, 2016 at an interest rate of 0.57%. Based on the values of loans pledged as collateral, we had $145.8 million of additional borrowing availability with the FHLB as of December 31, 2017. We also maintain relationships in the capital markets with brokers to issue certificates of deposit and money market accounts.

Capital Requirements

We are subject to various regulatory capital requirements administered by the federal and state banking regulators. Failure to meet regulatory capital requirements may result in certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on our financial statements. Under capital adequacy guidelines and the regulatory framework for “prompt corrective action” (described below), we must meet specific capital guidelines that involve quantitative measures of our assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting policies. The capital amounts and classifications are subject to qualitative judgments by the federal banking regulators about components, risk weightings and other factors. Qualitative measures established by regulation to ensure capital adequacy required us to maintain minimum amounts and ratio of CET1 capital, Tier 1 capital and total capital to risk-weighted assets and of Tier 1 capital to average consolidated assets, referred to as the “leverage ratio.” For further information, see “Supervision and Regulation—Regulatory Capital Requirements” and “Supervision and Regulation—Prompt Corrective Action Framework.”

In the wake of the global financial crisis of 2008 and 2009, the role of capital has become fundamentally more important, as banking regulators have concluded that the amount and quality of capital held by banking

organizations was insufficient to absorb losses during periods of severely distressed economic conditions. The Dodd-Frank Act and new banking regulations promulgated by the U.S. federal banking regulators to implement the Basel III Capital Rules have established strengthened capital standards for banks and bank holding companies and require more capital to be held in the form of common stock. These provisions, which generally became applicable to us on January 1, 2015, impose meaningfully more stringent regulatory capital requirements than those applicable to us prior to that date. In addition, the Basel III Capital Rules will implement a concept known as the "capital conservation buffer." In general, banks and bank holding companies will be required to hold a buffer of common equity Tier 1 capital equal to 2.5% of risk-weighted assets over each minimum capital ratio to avoid being subject to limits on capital distributions (e.g., dividends, stock buybacks, etc.) and certain discretionary bonus payments to executive officers. For community banks, the capital conservation buffer requirement commenced on January 1, 2016, with a gradual phase-in. Full compliance with the capital conservation buffer will be required by January 1, 2019.

The table below also summarizes the capital requirements applicable to us and the Bank in order to be considered "well-capitalized" from a regulatory perspective, as well as our and the Bank's capital ratios as of December 31, 2017 and 2016. We and the Bank exceeded all regulatory capital requirements under the Basel III Capital Rules and were considered to be "well-capitalized" as of the dates reflected in the table below. As of December 31, 2017, the FDIC categorized us as well-capitalized under the prompt corrective action framework. There have been no conditions or events since December 31, 2017 that management believes would change this classification.

	Actual		Regulatory Capital Ratio Requirements		Minimum To be Considered "Well Capitalized"		Regulatory Capital Ratio Requirements, including fully phased in Capital Conservation Buffer	
(Dollars in thousands)	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
As of December 31, 2017:								
Total capital (to risk-weighted assets)								
Consolidated	$100,713	13.49%	$59,729	8.00%	N/A	N/A	$78,394	10.50%
Bank	100,648	13.48%	59,726	8.00%	74,658	10.00%	78,391	10.50%
Tier 1 capital (to risk-weighted assets)								
Consolidated	91,510	12.26%	44,797	6.00%	N/A	N/A	63,462	8.50%
Bank	91,445	12.25%	44,795	6.00%	59,726	8.00%	63,459	8.50%
CET1 capital (to risk-weighted assets)								
Consolidated	91,510	12.26%	33,597	4.50%	N/A	N/A	52,263	7.00%
Bank	91,445	12.25%	33,596	4.50%	48,528	6.50%	52,260	7.00%
Tier 1 capital (to average assets)								
Consolidated	91,510	10.46%	35,009	4.00%	N/A	N/A	35,009	4.00%
Bank	91,445	10.45%	35,007	4.00%	43,759	5.00%	35,007	4.00%

	Actual		Regulatory Capital Ratio Requirements		Minimum To be Considered "Well Capitalized"		Regulatory Capital Ratio Requirements, including fully phased in Capital Conservation Buffer	
(Dollars in thousands)	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
As of December 31, 2016:								
Total capital (to risk-weighted assets)								
Consolidated	$89,286	13.40%	$53,311	8.00%	N/A	N/A	$69,970	10.50%
Bank	89,225	13.39%	53,306	8.00%	66,632	10.00%	69,964	10.50%
Tier 1 capital (to risk-weighted assets)								
Consolidated	81,304	12.20%	39,983	6.00%	N/A	N/A	56,643	8.50%
Bank	81,244	12.19%	39,979	6.00%	53,306	8.00%	56,637	8.50%

(Dollars in thousands)	Actual		Regulatory Capital Ratio Requirements		Minimum To be Considered "Well Capitalized"		Regulatory Capital Ratio Requirements, including fully phased in Capital Conservation Buffer	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
CET1 capital (to risk-weighted assets)								
Consolidated	81,304	12.20%	29,987	4.50%	N/A	N/A	46,647	7.00%
Bank	81,244	12.19%	29,985	4.50%	43,311	6.50%	46,643	7.00%
Tier 1 capital (to average assets)								
Consolidated	81,304	10.89%	29,859	4.00%	N/A	N/A	29,859	4.00%
Bank	81,244	10.88%	29,857	4.00%	37,321	5.00%	29,857	4.00%

Contractual Obligations

The following tables contain supplemental information regarding our total contractual obligations at December 31, 2017 and 2016:

(Dollars in thousands)	Payments Due at December 31, 2017				
	Within One Year	One to Three Years	Three to Five Years	After Five Years	Total
Deposits without a stated maturity	$540,573	$ —	$ —	$ —	$540,573
Time deposits	217,783	14,768	182	—	232,733
Operating lease commitments	1,630	3,251	3,378	3,763	12,022
Advances from FHLB	25,000				25,000
Total contractual obligations	$784,986	$18,019	$3,560	$3,763	$810,328

(Dollars in thousands)	Payments Due at December 31, 2016				
	Within One Year	One to Three Years	Three to Five Years	After Five Years	Total
Deposits without a stated maturity	$480,149	$ —	$ —	$ —	$480,149
Time deposits	165,594	16,041	—	—	181,635
Operating lease commitments	1,459	2,775	2,806	4,572	11,612
Advances from FHLB	10,000				10,000
Total contractual obligations	$657,202	$18,816	$2,806	$4,572	$683,396

We believe that we will be able to meet our contractual obligations as they come due through the maintenance of adequate cash levels. We expect to maintain adequate cash levels through profitability, loan and securities repayment and maturity activity and continued deposit gathering activities. We have in place various borrowing mechanisms for both short-term and long-term liquidity needs.

Off-Balance Sheet Arrangements

We are a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of our customers. These financial instruments include commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in our consolidated balance sheet. The contractual or notional amounts of those instruments reflect the extent of involvement we have in particular classes of financial 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 amount does not necessarily represent future cash requirements. We evaluate each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if we deem collateral is necessary upon extension of credit, is based on management's credit evaluation of the counterparty.

Standby letters of credit are conditional commitments issued by us to guarantee the performance of a customer to a third party. They are intended to be disbursed, subject to certain condition, upon request of the borrower.

The following table summarized commitments as of the dates presented.

	December 31,		
(Dollars in thousands)	**2017**	**2016**	**2015**
Commitments to extend credit	$62,356	$55,689	$53,013
Standby letters of credit	1,627	1,499	3,166
Total	$63,983	$57,188	$56,179

Quantitative and Qualitative Disclosures about Market Risk

Market risk represents the risk of loss due to changes in market values of assets and liabilities. We incur market risk in the normal course of business through exposures to market interest rates, equity prices, and credit spreads. We have identified interest rate risk as our primary source of market risk.

Interest Rate Risk

Interest rate risk is the risk to earnings and value arising from changes in market interest rates. Interest rate risk arises from timing differences in the repricings and maturities of interest-earning assets and interest-bearing liabilities (repricing risk), changes in the expected maturities of assets and liabilities arising from embedded options, such as borrowers' ability to prepay home mortgage loans at any time and depositors' ability to redeem certificates of deposit before maturity (option risk), changes in the shape of the yield curve where interest rates increase or decrease in a nonparallel fashion (yield curve risk), and changes in spread relationships between different yield curves, such as U.S. Treasuries and LIBOR (basis risk).

Our board's asset liability committee, or ALM, establishes broad policy limits with respect to interest rate risk. Our management's asset liability committee, or ALCO, establishes specific operating guidelines within the parameters of the policies set by the ALM. In general, we seek to minimize the impact of changing interest rates on net interest income and the economic values of assets and liabilities. Our ALCO monitors the level of interest rate risk sensitivity on a quarterly basis to ensure compliance with the ALM-approved risk limits. The policy requires a periodic review of all key assumptions used, such as identifying appropriate interest rate scenarios, setting loan prepayment rates based on historical analysis, and noninterest-bearing and interest-bearing deposit durations based on historical analysis.

Interest rate risk management is an active process that encompasses monitoring loan and deposit flows complemented by investment and funding activities. Effective management of interest rate risk begins with understanding the dynamic characteristics of assets and liabilities and determining the appropriate interest rate risk posture given business forecasts, management objectives, market expectations, and policy constraints.

An asset sensitive position refers to a balance sheet position in which an increase in short-term interest rates is expected to generate higher net interest income, as rates earned on our interest-earning assets would reprice upward more quickly than rates paid on our interest-bearing liabilities, thus expanding our net interest margin. Conversely, a liability sensitive position refers to a balance sheet position in which an increase in short-term interest

rates is expected to generate lower net interest income, as rates paid on our interest-bearing liabilities would reprice upward more quickly than rates earned on our interest-earning assets, thus compressing our net interest margin.

Interest rate risk measurement is calculated and reported to the ALCO and ALM at least quarterly. The information reported includes period-end results and identifies any policy limits exceeded, along with an assessment of the policy limit breach and the action plan and timeline for resolution, mitigation, or assumption of the risk.

Evaluation of Interest Rate Risk

We use a net interest income simulation model to measure and evaluate potential changes in our net interest income. We run various hypothetical interest rate scenarios at least quarterly and compare these results against a scenario with no changes in interest rates. We use two approaches to model interest rate risk: Earnings at Risk, or EAR, and Economic Value of Equity, or EVE. Under EAR, net interest income is modeled utilizing various assumptions for assets and liabilities. EVE measures the period end market value of assets minus the market value of liabilities and the change in this value as rates change. EVE is a period end measurement.

Our simulation model incorporates various assumptions, which we believe are reasonable but which may have a significant impact on results such as: (i) the timing of changes in interest rates; (ii) shifts or rotations in the yield curve; (iii) re-pricing characteristics for market-rate-sensitive instruments; (iv) varying loan prepayment speeds for different interest rate scenarios; and (v) the overall growth and mix of assets and liabilities. Because of limitations inherent in any approach used to measure interest rate risk, simulation results are not intended as a forecast of the actual effect of a change in market interest rates on our results but rather as a means to better plan and execute appropriate asset-liability management strategies and manage our interest rate risk.

Potential changes to our net interest income in hypothetical rising and declining rate scenarios calculated as of December 31, 2017, 2016 and 2015 are presented in the following table. The projections assume (1) immediate, parallel shifts downward of the yield curve of 100 basis points and (2) immediate, parallel shifts upward of the yield curve of 100, 200, 300 and 400 basis points over 12 months. In the current interest rate environment, a downward shift of the yield curve of 200, 300 and 400 basis points does not provide us with meaningful results. In a downward parallel shift of the yield curve, interest rate at the short-end of the yield curve are not modeled to decline any further than 0%.

	Net Interest Income Sensitivity			Economic Value of Equity Sensitivity		
	December 31,			December 31,		
	2017	2016	2015	2017	2016	2015
+400 basis points	11.58%	9.95%	2.49%	6.28%	(4.63)%	(14.04)%
+300 basis points	9.14%	7.57%	3.23%	5.85%	(2.15)%	(9.36)%
+200 basis points	6.42%	5.58%	2.58%	4.90%	(0.02)%	(5.69)%
+100 basis points	3.43%	3.19%	1.66%	4.09%	1.65%	(2.02)%
-100 basis points	(2.24)%	(1.47)%	(2.70)%	(3.06)%	(6.42)%	(1.29)%

We are within board-established policy limits for the all rate scenarios. The EAR reported at December 31, 2017 projects that our earnings are expected to be sensitive to changes in interest rates over the next year. In recent periods, the amount of fixed rate assets decreased resulting in a position shift to be slightly more asset sensitive.

MARKET PRICE OF COMMON STOCK

The common stock of the Company was quoted on the OTCQB Market until March 28, 2018, under the symbol "OPBK." The following table shows the high and low bid quotations of the common stock in each of the previous eight quarters as quoted on the OTCQB. There may also have been transactions at prices other than those shown during that time. The market for our common stock is sporadic and at times very limited.

The Historical Bid Quotations of the Common Stock

Quarters Ending	High	Low
December 31, 2017	$9.95	$9.11
September 30, 2017	$9.30	$7.75
June 30, 2017	$7.90	$7.30
March 31, 2017	$7.70	$6.95
December 31, 2016	$7.70	$6.10
September 30, 2016	$6.40	$5.95
June 30, 2016	$6.10	$5.65
March 31, 2016	$6.55	$5.64

On December 31, 2017, we had approximately 390 record holders of our common stock. There has been no regular and liquid trading market for the common stock. Our common stock became listed for trading on the Nasdaq Global Market in March 2018, and at that time the quoting of our shares on the OTCQB Market was discontinued.

The Company has not paid dividends on its common stock.

Independent Auditors' Report

Crowe Horwath LLP
Independent Member Crowe Horwath Inter

Report of Independent Registered Public Accounting Firm

Shareholders and the Board of Directors of OP Bancorp
Los Angeles, California

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of OP Bancorp (the "Company") as of December 31, 2017 and 2016, the related consolidated statements of income and comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2017, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting in accordance with the standards of the PCAOB. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion in accordance with the standards of the PCAOB.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Crowe Horwath LLP

Crowe Horwath LLP

We have served as the Company's auditor since 2010.

Los Angeles, California
March 5, 2018

Consolidated Balance Sheets

	December 31, 2017	December 31, 2016
ASSETS		
Cash and cash equivalents	$ 63,249,952	$ 20,126,028
Securities available for sale, at fair value	41,471,711	35,463,451
Loans held for sale	15,739,305	1,646,250
Loans receivable, net of allowance of $9,139,488 at December 31, 2017 and $7,909,682 at December 31, 2016	738,884,413	666,317,092
Premises and equipment, net	4,480,792	5,067,095
Accrued interest receivable	2,463,486	2,001,488
Federal Home Loan Bank and Pacific Coast Bankers Bank stock, at cost	4,286,500	3,437,600
Servicing assets	6,771,097	6,782,555
Company owned life insurance	11,089,718	10,769,627
Deferred tax assets	3,383,365	3,276,063
Other assets	9,178,491	6,363,171
Total assets	$ 900,998,830	$ 761,250,420
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Deposits:		
Noninterest bearing	$ 289,409,876	$ 247,376,244
Interest bearing:		
Savings	3,838,353	3,206,538
Money market and others	247,324,292	229,566,160
Time deposits greater than $250,000	108,952,059	79,056,290
Other time deposits	123,781,434	102,578,668
Total deposits	773,306,014	661,783,900
Federal Home Loan Bank advances	25,000,000	10,000,000
Accrued interest payable	423,239	321,753
Other liabilities	10,789,627	7,860,980
Total liabilities	809,518,880	679,966,633
Shareholders' equity		
Preferred stock – no par value; 10,000,000 shares authorized; no shares issued or outstanding at December 31, 2017 and 2016	-	-
Common stock – no par value; 50,000,000 shares authorized; 13,190,527 and 12,896,548 shares issued and outstanding at December 31, 2017 and 2016, respectively	67,925,860	67,499,310
Additional paid-in capital	5,279,991	4,611,973
Retained earnings	18,623,952	9,387,470
Accumulated other comprehensive loss	(349,853)	(214,966)
Total shareholders' equity	91,479,950	81,283,787
Total liabilities and shareholders' equity	$ 900,998,830	$ 761,250,420

Consolidated Statements of Income and Comprehensive Income

	Years Ended December 31,		
	2017	2016	2015
Interest income			
Interest and fees on loans	$ 39,111,439	$ 30,529,892	$ 24,328,811
Interest on investment securities	675,948	664,121	480,305
Other interest income	495,153	507,042	383,042
Total interest income	40,282,540	31,701,055	25,192,158
Interest expense			
Interest on deposits	4,469,689	3,286,147	2,605,140
Interest on borrowed funds	103,067	85,290	83,974
Total interest expense	4,572,756	3,371,437	2,689,114
Net interest income	35,709,784	28,329,618	22,503,044
Provision for loan losses	1,310,932	1,682,301	552,843
Net interest income after provision for loan losses	34,398,852	26,647,317	21,950,201
Noninterest income			
Service charges on deposits	1,656,252	1,274,726	1,277,879
Loan servicing fees, net of amortization	1,127,017	1,313,036	1,130,650
Gain on sale of loans	4,938,760	5,507,238	4,669,042
Other income	1,264,333	911,624	900,417
Total noninterest income	8,986,362	9,006,624	7,977,988
Noninterest expense			
Salaries and employee benefits	16,473,500	14,555,542	12,252,708
Occupancy and equipment	3,918,219	3,615,843	3,162,047
Data processing and communication	1,322,955	1,086,764	783,657
Professional fees	588,850	683,531	412,859
FDIC insurance and regulatory assessments	376,886	368,557	306,769
Promotion and advertising	630,683	556,805	532,482
Directors' fees	796,206	758,423	783,602
Foundation donation and other contributions	953,900	745,300	601,577
Other expenses	1,195,544	963,350	959,270
Total noninterest expense	26,256,743	23,334,115	19,794,971
Income before income taxes	17,128,471	12,319,826	10,133,218
Income tax expense	7,891,989	4,894,455	4,169,873
Net income	$ 9,236,482	$ 7,425,371	$ 5,963,345
Earnings per share - Basic	$ 0.68	$ 0.55	$ 0.44
Earnings per share - Diluted	$ 0.66	$ 0.53	$ 0.43
Other comprehensive income/(loss):			
Change in unrealized gain/(loss) on securities available for sale, net of tax effects of ($103,553), $11,932, and ($100,453) in 2017, 2016 and 2015, respectively	(134,887)	17,065	(143,663)
Total other comprehensive income/(loss)	(134,887)	17,065	(143,663)
Comprehensive income	$ 9,101,595	$ 7,442,436	$ 5,819,682

Consolidated Statements of Changes in Shareholders' Equity

	Common Stock		Additional Paid-in Capital	Retained Earnings / (Accumulated Deficit)	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	Shares Outstanding	Amount				
Balance at January 1, 2015	12,411,089	$66,993,270	$2,538,412	$ (4,001,246)	$ (88,368)	$65,442,068
Net income	-	-	-	5,963,345	-	5,963,345
Stock issued under stock-based compensation plans	271,421	349,090	-	-	-	349,090
Stock-based compensation	-	-	868,444	-	-	868,444
Change in unrealized loss on securities available for sale net of reclassifications and tax effects	-	-	-	-	(143,663)	(143,663)
Balance at December 31, 2015	12,682,510	$67,342,360	$3,406,856	$ 1,962,099	$ (232,031)	$72,479,284
Net income	-	-	-	7,425,371	-	7,425,371
Stock issued under stock-based compensation plans	214,038	156,950	-	-	-	156,950
Stock-based compensation	-	-	1,205,117	-	-	1,205,117
Change in unrealized gain on securities available for sale net of reclassifications and tax effects	-	-	-	-	17,065	17,065
Balance at December 31, 2016	12,896,548	$67,499,310	$4,611,973	$ 9,387,470	$ (214,966)	$81,283,787
Net income	-	-	-	9,236,482	-	9,236,482
Stock issued under stock-based compensation plans	293,979	426,550	-	-	-	426,550
Stock-based compensation	-	-	668,018	-	-	668,018
Change in unrealized loss on securities available for sale net of reclassifications and tax effects	-	-	-	-	(134,887)	(134,887)
Balance at December 31, 2017	13,190,527	$67,925,860	$5,279,991	$ 18,623,952	$ (349,853)	$91,479,950

Consolidated Statements of Cash Flows

	2017	2016	2015
Cash flows from operating activities			
Net income	$ 9,236,482	$ 7,425,371	$ 5,963,345
Adjustments to reconcile net income to net cash and cash equivalents provided by operating activities:			
Provision for loan losses	1,310,932	1,682,301	552,843
Depreciation and amortization of premises and equipment	1,007,736	1,084,071	940,404
Amortization of net premiums on securities	282,969	385,410	268,598
Stock-based compensation	668,018	1,205,117	868,444
Gain on sales of loans	(4,938,760)	(5,507,238)	(4,669,042)
Gain on called securities	-	-	(1,383)
Earnings on company owned life insurance	(320,091)	(334,666)	(353,082)
Origination of loans held for sale	(83,423,426)	(84,065,452)	(68,291,494)
Proceeds from sales of loans held for sale	72,345,672	90,860,166	70,944,759
Amortization of servicing assets	1,934,917	1,413,698	1,267,603
Net change in:			
Accrued interest receivable	(461,998)	(439,675)	(386,967)
Other assets	(2,819,069)	(6,159,670)	926,048
Accrued interest payable	101,486	(25,383)	214,968
Other liabilities	2,928,647	3,058,493	703,632
Net cash from operating activities	(2,146,485)	10,582,543	8,948,676
Cash flows from investing activities			
Net change in loans receivable	(73,878,253)	(167,103,293)	(93,676,619)
Proceeds from calls of securities held to maturity	-	-	3,000,000
Proceeds from calls of securities available for sale	6,168,924	8,069,010	5,580,479
Purchase of securities available for sale	(12,698,593)	-	(30,117,837)
Purchase of premises and equipment, net	(421,433)	(259,033)	(1,879,464)
Purchase of Federal Home Loan Bank stock	(848,900)	(782,300)	(755,200)
Net cash from investing activities	(81,678,255)	(160,075,616)	(117,848,641)
Cash flows from financing activities			
Net change in deposits	111,522,114	142,062,833	91,202,151
Cash received from stock option exercises	426,550	156,950	349,090
Borrowings/(Repayment) of Federal Home Loan Bank advances	15,000,000	(10,000,000)	(10,000,000)
Net cash from financing activities	126,948,664	132,219,783	81,551,241
Net change in cash and cash equivalents	43,123,924	(17,273,290)	(27,348,724)
Cash and cash equivalents at beginning of period	20,126,028	37,399,318	64,748,042
Cash and cash equivalents at end of period	$ 63,249,952	$ 20,126,028	$ 37,399,318
Supplemental cash flow information			
Cash paid during the year for:			
Income taxes	$ 7,741,894	$ 5,432,000	$ 2,695,000
Interest	4,471,270	3,396,820	2,474,146

Notes to Consolidated Financial Statements

NOTE 1—BUSINESS DESCRIPTION

OP Bancorp is a California corporation whose common stock is quoted on the OTCQB under the ticker symbol, "OPBK." OP Bancorp was formed to acquire 100% of the voting equity of Open Bank (the "Bank") and commenced operation as a bank holding company on June 1, 2016. This transaction was treated as an internal reorganization as all shareholders of the Bank became shareholders of OP Bancorp. OP Bancorp has no operations other than ownership of the Bank. The Bank is a California state-chartered and FDIC-insured financial institution, which began its operations on June 10, 2005. Headquartered in downtown Los Angeles, California, OP Bancorp operates primarily in the traditional banking business arena that includes accepting deposits and making loans and investments. OP Bancorp's primary deposit products are demand and time deposits, and the primary lending products are commercial business loans to small to medium sized businesses. OP Bancorp is operating with seven full service branches. There are no significant concentrations of loans to any one industry or customer. However, OP Bancorp's customers' ability to repay their loans is dependent on the real estate and general economic conditions in OP Bancorp's market area.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation: The consolidated financial statements include OP Bancorp and its wholly owned subsidiary, the Bank, together referred to as the "Company." Intercompany transactions and balances are eliminated in consolidation. The consolidated financial statements of the Company have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP"). Certain reclassifications have been made to the prior year's financial statements to conform to the current year's presentation.

Use of Estimates: To prepare financial statements in conformity with GAAP, management makes 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.

Concentration of Risk: Most of the Company's customers are located within Los Angeles County and the surrounding area. The concentration of loans originated in this area may subject the Company to the risk of adverse impacts of economic, regulatory or other developments that could occur in Southern California.

The Company has significant concentration in commercial real estate loans. The Company obtains what it believes to be sufficient collateral to secure potential losses. The extent and value of the collateral obtained varies based upon the details underlying each loan agreement.

Cash Flows: Cash and cash equivalents include cash, deposits with other financial institutions with original maturities less than 90 days, and federal funds sold. Net cash flows are reported for customer loan and deposit transactions.

Securities: 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. 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.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized on the level-yield method without anticipating prepayments. Gains and losses on sales are recorded on the trade 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 extent and duration of the unrealized loss, and the financial condition and near- term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. 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.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Federal Home Loan Bank ("FHLB") Stock: The Bank is a member of the FHLB system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. FHLB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income.

Pacific Coast Bankers Bank ("PCBB") Stock : The Bank is a member of PCBB. PCBB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income.

Loans Held for Sale: Certain Small Business Administration ("SBA") loans that may be sold prior to maturity are designated as held for sale at origination and are recorded at the lower of their cost or fair value less costs to sell, determined on an aggregate basis. A valuation allowance is established if the market value of such loans is lower than their cost, and operations are charged or credited for valuation adjustments. Origination fees on loans held for sale, net of certain costs of processing and closing the loans, are deferred until the time of sale and are included in the computation of the gain or loss from the sales of the related loans. A portion of the premium on sale of SBA loans is recognized as gains on sales of loans at the time of the sale. These loans are generally sold with servicing retained.

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 principal balance outstanding, net of deferred loan fees and costs and an allowance for loan losses. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the level-yield method without anticipating prepayments. The recorded investment in loans includes accrued interest receivable, deferred loan fees and costs, and unearned income.

The accrual of interest income on commercial real estate and other commercial and industrial loans is discontinued at the time the loan is 90 days delinquent unless the loan is well-secured and in process of collection. Consumer loans are typically charged off no later than 120 days past due. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual status or charged-off at an earlier date if collection of principal or interest is considered doubtful. Nonaccrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

All interest accrued but not received for loans placed on nonaccrual status is reversed against interest income. Interest received on such loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Loan Losses: The allowance for loan losses is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. 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. A loan is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement.

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 and classified as impaired. Troubled debt restructurings are separately identified for impairment disclosures and are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a troubled debt restructuring is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral. For troubled debt restructurings that subsequently default, the Company determines the amount of reserve in accordance with the accounting policy for the allowance for loan losses.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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. Impairment is measured on a loan-by-loan basis for commercial real estate and construction loans. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Income recognition on impaired loans materially conforms to the method the Company uses for income recognition on nonaccrual loans.

Allowance for impaired loans is determined based on the present value of the estimated cash flows or on the fair value of the collateral if the loan is collateral dependent, less costs to sell. If the measured fair value is less than the recorded investment in the loan, the deficiency will be charged off against the allowance for loan losses, or alternatively, a specific allocation will be established. For consumer loans, management will generally charge off the balance if the loan is 90 days or more past due.

The general component of the allowance covers non- impaired loans and is based on historical loss experience adjusted for current factors. The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the most recent two years. For those portfolio segments that the Company does not have sufficient historical data available to track the loss migration, the loss factors are based on the actual loss history experienced by the Company over the most recent five years. This actual loss experience is supplemented with other economic factors based on the risks present for each portfolio segment. These economic factors include consideration of the following: levels of and trends in delinquencies and impaired loans; levels of and trends in charge- offs and recoveries; trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures, and practices; experience, ability, and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; and effects of changes in credit concentrations. Related to the current national and local economic conditions, the Company has considered risk factors including the broad deterioration of property values, reduced consumer and business spending as a result of high unemployment and reduced credit availability, and the lack of confidence in a sustainable recovery.

The following portfolio segments have been identified in the Company's loan portfolio, and are also representative of the classes within the portfolio: commercial real estate, SBA loans—real estate, SBA loans—non-real estate, commercial and industrial, trade finance, home mortgage, and consumer. The Company reviews the credit risk exposure of all its portfolio segments by internally assigned grades. The Company categorizes loans into risk grades based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. For the home mortgage and consumer portfolio segments, the Company's primary monitoring tool is reviewing past due listings to determine if the loans are performing.

The determination of the allowance for loan losses is based on estimates that are particularly susceptible to changes in the economic environment and market conditions.

Management believes that as of December 31, 2017 and 2016 the allowance for loan losses is adequate based on information currently available. If a deterioration in the economy of the Company's principal market area occurs, the Company's loan portfolios could be adversely impacted and higher charge-offs and increases in non-performing assets could result. Such an adverse impact could also require a larger allowance for loan losses.

Servicing Assets: When SBA loans are sold with servicing retained, servicing assets are initially recorded at fair value with the income statement effect recorded in gains on sales of loans. Fair value is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, prepayment speeds, and default rates and losses. The Company compares the valuation model inputs and results to published industry data in order to validate the model results and assumptions. Servicing assets are subsequently measured using the amortization method which requires servicing assets to be amortized into non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying loans.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Servicing assets are evaluated for impairment based upon the fair value of the assets as compared to their carrying amount. Impairment is recognized through a valuation allowance to the extent that fair value is less than the carrying amount. If the Company later determines that all or a portion of the impairment no longer exists, a reduction of the valuation allowance may be recorded as an increase to income. Changes in the valuation allowances are reported with other income on the income statement. The fair values of servicing rights are subject to fluctuations as a result of changes in estimated and actual prepayment speeds, default rates, and losses.

Servicing fee income, which is reported on the income statement as other income, is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal and are recorded as income when earned. The amortization of servicing assets is netted against loan servicing fee income. Late fees and ancillary fees related to loan servicing are not material.

Company Owned Life Insurance: The Company has purchased life insurance policies on certain key executives. Company 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.

Transfers of Financial Assets: Transfers of financial assets are accounted for as sales when control over the assets has been relinquished. Control over transferred assets is deemed to be surrendered when the assets have been isolated from the Company, the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Premises and Equipment: Premises and equipment are stated at cost, less accumulated depreciation. Equipment and furnishings are depreciated over 3 to 10 years, and leasehold improvements are amortized over the lesser of the terms of the respective leases or the estimated useful lives. The straight-line method of depreciation is used for financial reporting purposes. Repairs and maintenance are charged to operating expenses as incurred.

Other Real Estate Owned, Net: Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. Physical possession of residential real estate property collateralizing a consumer mortgage loan occurs when the legal title is obtained upon completion of foreclosure or when the borrower conveys all interest in the property to satisfy the loan through the completion of a deed in lieu of foreclosure or through a similar legal agreement. These assets are subsequently accounted for at the lower of their cost or fair value less estimated costs to sell. If their fair value declines subsequent to foreclosure, a valuation allowance is recorded through expense. Operating costs after acquisition are expensed.

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 based on the fair value of the awards at the date of grant. A Black-Scholes model is utilized to estimate the fair value of stock options, while the market price of the Company's common stock at the date of the 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.

Earnings per Common Share: Basic and diluted earnings per share is based on the two-class method prescribed in ASC Topic 260, Earnings Per Share (ASC 260). Stock options and restricted stock awards are considered outstanding for this calculation unless unearned. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable under stock-based compensation plans. Earnings and dividends per share are restated for all stock splits and stock dividends through the date of issuance of the financial statements.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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 tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized.

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 Company does not expect the total amount of unrecognized tax benefits to significantly increase or decrease in the next twelve months.

The Company recognizes interest and/or penalties related to income tax matters in income tax expense. There were no interest or penalties recognized in the years ended December 31, 2017 or 2016.

Comprehensive Income/(Loss): Comprehensive income/(loss) consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on securities available for sale, which are also recognized as separate components of shareholders' equity, net of tax.

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.

Fair Value of Financial Instruments: Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in Note 13–Fair Value of Financial Instruments. 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.

Operating Segments: While the chief decision-makers monitor the revenue streams of the various products and services, operations are managed and financial performance is evaluated on a Company-wide basis. Discrete financial information is not available other than on a Company-wide basis.

Recent Accounting Pronouncements:

In May 2014, the Financial Accounting Standard Board (FASB) issued Accounting Standard Update (ASU) 2014-9 (ASU 2014-09), Revenue from Contracts with Customers. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance also specifies the accounting for some costs to obtain or fulfill a contract with a customer, as well as enhanced disclosure requirements. In August 2015, the FASB issued ASU 2015-14 which deferred the effective date of ASU 2014-09 to fiscal years, and interim reporting periods within those fiscal years, beginning after December 15, 2017. In March 2016, the FASB issued ASU 2016-08 which clarified the revenue recognition implementation guidance on principal versus agent considerations and is effective during the same period as ASU 2014-09. In April 2016, the FASB issued ASU 2016-10 which clarified the revenue recognition guidance regarding the identification of performance obligations and the licensing implementation and is effective during the same period as ASU 2014-09. In May 2016, the FASB issued ASU 2016 -12 which narrowly amended the revenue recognition guidance regarding collectability, noncash consideration, presentation of sales tax and transition. ASU 2016-12 is effective during the same period as ASU 2014-09.

The majority of the Company's revenue consists of net interest income on financial assets and financial liabilities, which is explicitly excluded from the scope of ASU 2014-09. The Company adopted the new standard beginning January 1, 2018. The Company completed its analysis for determining the extent ASU 2014-09 will affect its noninterest income, primarily in the area of fees and service charges on deposit accounts and trade finance activities. Based on the analysis performed, the Company did not have a material change in the timing or measurement of revenues related to noninterest income. The Company will continue to evaluate the effect that this guidance will have on other revenue streams within its scope, as well as changes in disclosures required by the new guidance. However, the Company does not expect this to have a material impact on its consolidated financial statements.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) (ASU 2016-02). ASU 2016-02 is intended to increase transparency and comparability among organizations by recognizing lease assets and liabilities on the balance sheet and disclosing key information about lease arrangements. This ASU is effective for annual periods and interim periods within those annual periods beginning after December 15, 2018. Based on leases outstanding at December 31, 2017, the Company does not expect this ASU to have a material impact on the income statement, but does anticipate a $12 million increase in assets and liabilities once this ASU becomes effective (based on the leases outstanding as of December 31, 2017).

In June 2016, the FASB issued ASU 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments (ASU 2016- 13). The objective of ASU 2016-13 is to provide financial statement users with decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit. ASU 2016-13 includes provisions that require financial assets measured at amortized cost (such as loans and held to maturity (HTM) debt securities) to be presented at the net amount expected to be collected. This will be accomplished through recognition of an estimate of all current expected credit losses. The estimate will include forecasted information for the timeframe that an entity is able to develop reasonable and supportable forecasts. This is a change from the current practice of recognizing incurred losses based on the probable initial recognition threshold under current GAAP. In addition, credit losses on available for sale (AFS) debt securities will be recorded through an allowance for credit losses rather than as a write-down. Under ASU 2016-13, an entity will be able to record reversals of credit losses in current period income when the estimate of credit losses declines, whereas current GAAP prohibits reflecting those improvements in current period earnings.

ASU 2016-13 is effective for annual periods and interim periods within those annual periods beginning after December 15, 2019, and early adoption is permitted for fiscal years, including interim periods, beginning after December 15, 2018. ASU 2016-13 will be applied through a cumulative effect adjustment to retained earnings (modified-retrospective approach), except for debt securities for which an other-than-temporary impairment had been recognized before the effective date. A prospective transition approach is required for these debt securities. The Company is currently evaluating the effects of ASU 2016-13 on its financial statements and disclosures, including software solutions, data requirements and loss estimation methodologies. While the effects cannot yet be quantified, the Company expects ASU 2016-13 to add complexity and costs to its current credit loss evaluation process.

In March 2017, the FASB issued ASU 2017-08, Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20) (ASU 2017-08). ASU 2017-08 amends the amortization period for certain purchased callable debt securities held at a premium. Prior to the issuance of this guidance, premiums were amortized as an adjustment of yield over the contractual life of the instrument. ASU 2017-08 requires premiums on purchased callable debt securities that have explicit, noncontingent call features that are callable at fixed prices to be amortized to the earliest call date. There are no accounting changes for securities held at a discount. This ASU is effective for annual periods and interim periods within those annual periods beginning after December 15, 2018, and early adoption is permitted. ASU 2017-08 will be applied through a cumulative effect adjustment through equity (modified-retrospective approach). The Company is currently evaluating the effects of ASU 2017-08 on its financial statements and disclosures.

In May 2017, the FASB issued ASU 2017-09, Compensation—Stock Compensation (Topic 718), Scope of Modification Accounting (ASU 2017-09). ASU 2017-09 clarifies when changes to the terms and conditions of share-based payment awards must be treated as modifications. Specifically, the new guidance permits companies to make certain changes to awards without accounting for them as modifications. ASU 2017-09 is effective for annual periods beginning after December 31, 2017 and will be applied prospectively to an award modified after the effective date. There have been no changes to the terms and conditions of share-based payment awards, and as a result the adoption of this standard did not have a material effect on the Company’s operating results or financial condition.

NOTE 3—SECURITIES

The following table summarizes the amortized cost, fair value, and the corresponding amounts of gross unrealized gains and losses for available for sale securities at December 31, 2017 and 2016:

As of December 31, 2017	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
U.S. Government sponsored agency securities	$ 6,988,681	$ 2,001	$ (58,674)	$ 6,932,008
Mortgage-backed securities: residential	14,109,433	-	(168,908)	13,940,525
Collateralized mortgage obligations	18,458,814	-	(345,316)	18,113,498
Other securities	2,518,498	-	(32,818)	2,485,680
Total available for sale	$ 42,075,426	$ 2,001	$ (605,716)	$ 41,471,711

As of December 31, 2016	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
U.S. Government sponsored agency securities	$ 6,983,402	$ 27,162	$ (33,402)	$ 6,977,162
Mortgage-backed securities: residential	17,721,150	-	(165,113)	17,556,037
Collateralized mortgage obligations	11,124,174	-	(193,922)	10,930,252
Total available for sale	$ 35,828,726	$ 27,162	$ (392,437)	$ 35,463,451

There were no sales of securities available for sale in 2017, 2016 or 2015. The amortized cost and estimated fair value of securities available for sale at December 31, 2017, by contractual maturity, are shown below. Securities without a contractual maturity are shown separately.

As of December 31, 2017	Amortized Cost	Fair Value
Available for sale		
One to five years	$ 6,988,681	$ 6,932,008
Mortgage-backed securities: residential	14,109,433	13,940,525
Collateralized mortgage obligations	18,458,814	18,113,498
Other securities	2,518,498	2,485,680
Total available for sale	$ 42,075,426	$ 41,471,711

Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. At December 31, 2017 and 2016, 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.

NOTE 3—SECURITIES (Continued)

The following table summarizes securities with unrealized losses at December 31, 2017 and 2016, aggregated by length of time in a continuous unrealized loss position:

As of December 31, 2017	Less Than 12 Months Fair Value	Less Than 12 Months Unrealized Losses	12 Months or Longer Fair Value	12 Months or Longer Unrealized Losses	Total Fair Value	Total Unrealized Losses
Available for sale						
U.S. Government sponsored agency securities	$ 3,957,340	$ (33,620)	$ 1,974,139	$ (25,054)	$ 5,931,479	$ (58,674)
Mortgage-backed securities: residential	7,954,428	(70,965)	5,986,097	(97,943)	13,940,525	(168,908)
Collateralized mortgage obligations	9,642,028	(138,243)	8,471,469	(207,073)	18,113,497	(345,316)
Other securities	2,485,680	(32,818)	-	-	2,485,680	(32,818)
Total available for sale	$ 24,039,476	$ (275,646)	$ 16,431,705	$ (330,070)	$ 40,471,181	$ (605,716)

As of December 31, 2016	Less Than 12 Months Fair Value	Less Than 12 Months Unrealized Losses	12 Months or Longer Fair Value	12 Months or Longer Unrealized Losses	Total Fair Value	Total Unrealized Losses
Available for sale						
U.S. Government sponsored agency securities	$ 3,965,444	$ (33,402)	$ -	$ -	$ 3,965,444	$ (33,402)
Mortgage-backed securities: residential	17,556,036	(165,113)	-	-	17,556,036	(165,113)
Collateralized mortgage obligations	7,791,185	(133,356)	3,139,067	(60,566)	10,930,252	(193,922)
Total available for sale	$ 29,312,665	$ (331,871)	$ 3,139,067	$ (60,566)	$ 32,451,732	$ (392,437)

The Company believes that the unrealized losses are temporary, arising mainly from fluctuations in interest rates and do not reflect a deterioration of credit quality of the issuers. In analyzing an issuer's financial condition, the Company may consider whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. The fair value is expected to recover as the securities approach maturity. Management does not intend to sell and it is likely that management will not be required to sell the securities prior to their anticipated recovery.

There were no securities pledged at December 31, 2017. Securities with fair values of approximately $11,946,357 were pledged to secure public deposits, borrowings, and for other purposes as required or permitted by law at December 31, 2016.

NOTE 4—LOANS

The composition of the loan portfolio was as follows at December 31, 2017 and December 31, 2016:

	December 31, 2017	December 31, 2016
Real estate:		
Commercial real estate	$ 420,759,900	$ 362,585,001
SBA loans—real estate	106,924,278	97,411,302
Total real estate	527,684,178	459,996,303
SBA loans—non-real estate	8,634,879	6,875,189
Commercial and industrial	103,681,574	97,660,178
Home mortgage	104,067,756	104,808,620
Consumer	3,955,514	4,886,484
Gross loans receivable	748,023,901	674,226,774
Allowance for loan losses	(9,139,488)	(7,909,682)
Loans receivable, net	$ 738,884,413	$ 666,317,092

The Company had $10,768 in loans to principal officers, directors, and their affiliates at December 31, 2017. No loans were outstanding to related parties as of December 31, 2016.

The activity in the allowance for loan losses for the years ended December 31 2017, 2016 and 2015 was as follows:

	Commercial Real Estate	SBA Loans Real Estate	SBA Loans Non-Real Estate	Commercial and Industrial	Home Mortgage	Consumer	Total
Balance at January 1, 2015	$ 2,480,934	$ 745,363	$ 128,772	$ 1,599,594	$ 709,581	$ 90,257	$5,754,501
Provision for loan losses	750,676	(42,125)	(7,015)	(335,549)	226,700	(39,844)	552,843
Charge-offs	-	-	(7,880)	-	-	-	(7,880)
Recoveries	-	851	14,900	70,530	-	4,000	90,281
Balance at December 31, 2015	$ 3,231,610	$ 704,089	$ 128,777	$ 1,334,575	$ 936,281	$ 54,413	$6,389,745
Provision for loan losses	985,479	188,516	(49,824)	130,162	427,347	621	1,682,301
Charge-offs	-	-	(32,180)	(142,443)	-	-	(174,623)
Recoveries	-	-	12,259	-	-	-	12,259
Balance at December 31, 2016	$ 4,217,089	$ 892,605	$ 59,032	$ 1,322,294	$1,363,628	$ 55,034	$7,909,682
Provision for loan losses	584,208	189,460	633,345	(56,838)	44,114	(83,357)	1,310,932
Charge-offs	-	-	(168,683)	-	-	-	(168,683)
Recoveries	-	-	14,273	-	-	73,284	87,557
Balance at December 31, 2017	$ 4,801,297	$ 1,082,065	$ 537,967	$ 1,265,456	$1,407,742	$ 44,961	$9,139,488

NOTE 4—LOANS (Continued)

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment as of December 31, 2017 and 2016:

	Loans Individually Evaluated for Impairment	Loans Collectively Evaluated for Impairment	Total
2017			
Allowance for loan losses:			
Commercial real estate	$ -	$ 4,801,297	$ 4,801,297
SBA loans—real estate	-	1,082,065	1,082,065
SBA loans—non-real estate	-	537,967	537,967
Commercial and industrial	353,985	911,471	1,265,456
Home mortgage	-	1,407,742	1,407,742
Consumer	-	44,961	44,961
Total	$ 353,985	$ 8,785,503	$ 9,139,488
Loans:			
Commercial real estate	$ -	$ 421,811,734	$ 421,811,734
SBA loans—real estate	-	107,427,788	107,427,788
SBA loans—non-real estate	-	8,655,808	8,655,808
Commercial and industrial	353,985	103,601,098	103,955,083
Home mortgage	241,164	104,239,551	104,480,715
Consumer	20,763	3,946,491	3,967,254
Total	$ 615,912	$ 749,682,470	$ 750,298,382
2016			
Allowance for loan losses:			
Commercial real estate	$ -	$ 4,217,089	$ 4,217,089
SBA loans—real estate	-	892,605	892,605
SBA loans—non-real estate	3,817	55,215	59,032
Commercial and industrial	367,320	954,974	1,322,294
Home mortgage	-	1,363,628	1,363,628
Consumer	-	55,034	55,034
Total	$ 371,137	$ 7,538,545	$ 7,909,682
Loans:			
Commercial real estate	$ -	$ 363,380,249	$ 363,380,249
SBA loans—real estate	-	97,756,201	97,756,201
SBA loans—non-real estate	3,817	6,892,341	6,896,158
Commercial and industrial	367,320	97,519,413	97,886,733
Home mortgage	-	105,229,707	105,229,707
Consumer	-	4,897,862	4,897,862
Total	$ 371,137	$ 675,675,773	$ 676,046,910

NOTE 4—LOANS (Continued)

The following table presents information related to impaired loans by class of loans as of and for the years ended December 31, 2017, 2016 and 2015. The difference between the unpaid principal balance (net of partial charge-offs) and the recorded investment in the loans is not considered to be material.

	Recorded Investment	Allowance Allocated	Average Recorded Investment	Interest Income Recognized
2017				
With no related allowance recorded:				
Home mortgage	$ 241,164	$ -	$ 242,210	$ -
Consumer	20,763	-	30,521	-
With an allowance recorded:				
Commercial and industrial	353,985	353,985	360,653	16,801
	$ 615,912	$ 353,985	$ 633,384	$ 16,801
2016				
With an allowance recorded:				
SBA loans – non-real estate	$ 3,817	$ 3,817	$ 9,325	$ 1,959
Commercial and industrial	367,320	367,320	545,616	15,292
	$ 371,137	$ 371,137	$ 554,941	$ 17,251
2015				
With an allowance recorded:				
SBA loans – non-real estate	$ 47,183	$ 47,183	$ 47,147	$ 5,618
Commercial and industrial	723,911	723,911	883,012	14,860
	$ 771,094	$ 771,094	$ 930,159	$ 20,478

The difference between interest income recognized and cash basis interest recognized was immaterial.

The following table presents the recorded investment in nonaccrual loans and loans past due greater than 90 days still accruing interest by class of loans as of December 31, 2017 and 2016:

	Nonaccrual	Loans >90 Days Past Due & Still Accruing	Total
2017			
Home mortgage	$ 662,365	$ -	$ 662,365
Consumer	20,763		20,763
Total	$ 683,128	$ -	$ 683,128
2016			
SBA loans—non-real estate	$ 208,802	$ -	$ 208,802
Total	$ 208,802	$ -	$ 208,802

Nonaccrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

NOTE 4—LOANS (Continued)

The following table represents the aging of the recorded investment in past due loans as of December 31, 2017 and 2016:

	30-59 Days Past Due	60-89 Days Past Due	> 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
2017						
Commercial real estate	$ -	$ -	$ -	$ -	$421,811,734	$421,811,734
SBA—real estate	139,806	-	-	139,806	107,287,982	107,427,788
SBA—non-real estate	61,611	-	-	61,611	8,594,197	8,655,808
Commercial and industrial	-	-	-	-	103,955,083	103,955,083
Home mortgage	-	-	662,365	662,365	103,818,350	104,480,715
Consumer	-	-	-	-	3,967,254	3,967,254
	$201,417	$ -	$ 662,365	$ 863,782	$749,434,600	$750,298,382
2016						
Commercial real estate	$ -	$ -	$ -	$ -	$363,380,249	$363,380,249
SBA—real estate	241,576	825,694	-	1,067,270	96,688,931	97,756,201
SBA—non-real estate	-	-	208,802	208,802	6,687,356	6,896,158
Commercial and industrial	-	-	-	-	97,886,733	97,886,733
Home mortgage	-	814,551	-	814,551	104,415,156	105,229,707
Consumer	-	-	-	-	4,897,862	4,897,862
	$241,576	$1,640,245	$ 208,802	$2,090,623	$673,956,287	$676,046,910

Troubled Debt Restructurings: As of December 31, 2017 and 2016, the Company had a recorded investment in troubled debt restructurings of $353,985 and $367,320, respectively. The Company has allocated $353,985 and $367,320 of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as of December 31, 2017 and 2016, respectively. The Company has not committed to lend any additional amounts to customers with outstanding loans that are classified as troubled debt restructurings.

Modifications made were primarily extensions of existing payment modifications on loans previously identified as troubled debt restructurings. There were no new loans identified as trouble debt restructurings during the years ended December 31, 2017, 2016 or 2015. There were no payment defaults during the years ended December 31, 2017, 2016 or 2015 of loans that had been modified as troubled debt restructurings within the previous twelve months.

Credit Quality Indicators: The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. For consumer loans, a credit grade is established at inception, and generally only adjusted based on performance. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis is performed on a quarterly basis. The Company uses the following definitions for risk ratings:

Special Mention—Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the Company's credit position at some future date.

Substandard—Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

NOTE 4—LOANS (Continued)

Doubtful—Loans classified as 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 existing facts, conditions, and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass-rated loans.

As of December 31, 2017 and 2016, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

	Pass	Special Mention	Substandard	Doubtful	Total
2017					
Commercial real estate	$421,811,734	$ -	$ -	$ -	$421,811,734
SBA loans—real estate	106,405,966	-	1,021,822	-	107,427,788
SBA loans—non-real estate	8,594,375	32,702	28,731	-	8,655,808
Commercial and industrial	103,601,098	-	353,985	-	103,955,083
Home mortgage	103,818,350	-	662,365	-	104,480,715
Consumer	3,946,491	-	20,763	-	3,967,254
	$748,178,014	$ 32,702	$ 2,087,666	$ -	$750,298,382
2016					
Commercial real estate	$363,380,249	$ -	$ -	$ -	$363,380,249
SBA loans—real estate	96,847,750	-	908,451	-	97,756,201
SBA loans—non-real estate	6,852,884	39,457	3,817	-	6,896,158
Commercial and industrial	97,212,559	306,854	367,320	-	97,886,733
Home mortgage	104,415,156	-	814,551	-	105,229,707
Consumer	4,897,862	-	-	-	4,897,862
	$673,606,460	$ 346,311	$ 2,094,139	$ -	$676,046,910

NOTE 5—PREMISES AND EQUIPMENT

The Company's premises and equipment consisted of the following at December 31, 2017 and 2016:

	December 31, 2017	December 31, 2016
Leasehold improvements	$ 5,061,520	$ 4,834,045
Furniture and fixtures	2,492,623	2,441,082
Equipment and others	1,677,175	1,564,168
Total cost	9,231,318	8,839,295
Accumulated depreciation	(4,750,526)	(3,772,200)
Net book value	$ 4,480,792	$ 5,067,095

Total depreciation expense included in occupancy and equipment expenses was $1,007,736, $1,084,071, and $940,404 for the years ended December 31, 2017, 2016 and 2015, respectively.

NOTE 6—SERVICING ASSETS

Activity for loan servicing assets during the years ended December 31, 2017, 2016 and 2015 is as follows:

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Beginning balance	6,782,555	5,550,975	4,670,462
Additions	1,923,459	2,645,278	2,148,116
Amortized to expense	(1,934,917)	(1,413,698)	(1,267,603)
Ending balance	6,771,097	6,782,555	5,550,975

There was no valuation allowance recorded against the carrying value of the servicing assets as of December 31, 2017 or 2016.

The fair value of the servicing assets was $8,739,146 at December 31, 2017. Fair value of the servicing assets at December 31, 2017 was determined using discount rates ranging from 4.15% to 10.40% and prepayment speeds ranging from 10.2% to 10.9%, depending on the stratification of the specific assets.

The fair value of the servicing assets was $8,703,142 at December 31, 2016. Fair value of the servicing assets at year-end 2016 was determined using discount rates ranging from 4.50% to 10.86% and prepayment speeds ranging from 9.8% to 10.1%, depending on the stratification of the specific assets.

NOTE 7—DEPOSITS

Time deposits that exceed the FDIC insurance limit of $250,000 at December 31, 2017 and 2016 were $108,952,059 and $96,641,799, respectively.

The scheduled maturities of time deposits were as follows at December 31, 2017:

2018	$ 217,783,392
2019	14,325,669
2020	441,883
2022	182,549
Total	$ 232,733,493

Deposits from principal officers, directors, and their affiliates at December 31, 2017 and 2016 were $1,068,580 and $597,226, respectively.

NOTE 8—BORROWING ARRANGEMENTS

As of December 31, 2017, the Company had a $25 million advance outstanding from the Federal Home Loan Bank of San Francisco. The maturity date of this advance was January 2, 2018 and the interest rate on the advances was 1.41%. The advance was paid off on January 2, 2018 as scheduled. In addition, the Company has a letter of credit with the FHLB in the amount of $49,000,000 to secure a public deposit.

The Company had available borrowings from the following institutions as of December 31, 2017:

Federal Home Loan Bank—San Francisco	$ 145,761,000
Federal Reserve Bank	92,830,000
Pacific Coast Bankers Bank	4,000,000
Zions Bank	5,500,000
Total	$ 248,091,000

The Company has pledged approximately $643,724,000 of loans as collateral for these lines of credit as of December 31, 2017.

NOTE 9—INCOME TAXES

Income tax expense/(benefit) was as follows:

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Current federal expense	$ 5,893,432	$ 5,116,854	$ 2,534,570
Current state expense	2,002,308	1,430,189	267,629
	7,895,740	6,547,043	2,802,199
Deferred federal expense	(1,061,464)	(1,375,939)	538,824
Deferred state expense	(278,586)	(276,649)	828,850
Deferred tax asset revaluation	1,336,299	-	-
	(3,751)	(1,652,588)	1,367,674
Total tax expense	$ 7,891,989	$ 4,894,455	$ 4,169,873

Effective tax rates differ from the federal statutory rates of 35% for 2017 and 34% for 2016 and 2015 applied to income before taxes due to the following:

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Federal statutory rate times financial statement income	$ 5,994,965	$ 4,188,741	$ 3,445,294
Effect of:			
Meals and entertainment	45,246	36,981	29,622
State income taxes, net of federal tax benefit	1,096,258	831,920	656,476
Stock option expense and related excess tax benefits	(300,879)	34,956	43,664
Company owned life insurance	(112,032)	(113,786)	(120,048)
Other, net	(167,868)	(84,357)	114,865
Deferred tax asset revaluation	1,336,299	-	-
	1,897,024	705,714	724,579
Total tax expense	$ 7,891,989	$ 4,894,455	$ 4,169,873

On December 22, 2017, H.R.1, commonly known as the Tax Cuts and Jobs Act (the "Tax Act"), was signed into law, which among other items reduces the federal corporate tax rate to 21% from 35%, effective January 1, 2018. U.S. generally accepted accounting principles requires companies to revalue certain tax-related assets as of the date of enactment of the new legislation with resulting tax effects accounted for in the reporting period of enactment. As a result, the Company performed an analysis to determine the impact of the revaluation of the net deferred tax asset. The value of the Company's deferred tax asset was reduced by $1.3 million, and such $1.3 million was recorded as tax expense for the year ended December 31, 2017.

ASU 2016-09, "Compensation-Stock Compensation (Topic 718) Improvements to Employee Share-Based Payment Accounting" requires the Company to recognize all excess tax benefits or tax deficiencies through the income statement as income tax expense/benefit. Under previous GAAP, any excess tax benefits were recognized in additional paid-in capital to offset current-period and subsequent-period tax deficiencies. Due to the adoption of ASU 2016-09 in 2017, the Company recorded the related excess tax benefits of $318,771 through the income statement as income tax benefit.

NOTE 9—INCOME TAXES (Continued)

The net deferred tax asset included in the statement of financial position includes the following components at the dates indicated below:

	December 31, 2017	December 31, 2016	December 31, 2015
Deferred tax assets:			
Pre-opening expense	$ 42,265	$ 83,183	$ 107,529
Organizational costs	32,040	47,650	-
Allowance for loan losses	2,228,954	2,102,881	1,148,132
Loans held for sale	432,739	60,501	217,202
Stock-based compensation	273,444	367,748	376,057
Accrued compensation	74,632	110,506	88,794
Accrued contributions	-	301,291	216,286
Accrued rent	590,118	862,240	782,016
State taxes	410,057	510,277	24,514
Net unrealized loss on securities available for sale	178,480	150,311	162,243
Nonaccrual loan interest income	48,023	121,605	111,161
Other	18,801	29,596	25,628
Total deferred tax assets	4,329,553	4,747,789	3,259,562
Deferred tax liabilities:			
Loan origination costs	(476,756)	(490,010)	(401,818)
Depreciation	(434,294)	(939,524)	(1,137,845)
Other	(35,138)	(42,192)	(84,492)
Total deferred tax liabilities	(946,188)	(1,471,726)	(1,624,155)
Net deferred tax asset	$ 3,383,365	$ 3,276,063	$ 1,635,407

A valuation allowance for deferred tax assets is recorded when it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income and tax planning strategies which will create taxable income during the periods in which those temporary differences become deductible. At December 31, 2017, management reevaluated all positive and negative evidence that existed and concluded all deferred tax assets are realizable. Therefore, no valuation allowance is necessary.

The Company is subject to U.S. Federal income tax as well as various state taxing jurisdictions. The Company is no longer subject to examination by Federal taxing authorities for tax years prior to 2014 and for state taxing authorities for tax years prior to 2013.

There were no significant unrealized tax benefits recorded as of December 31, 2017, 2016 and 2015, and the Company does not expect any significant increase in unrealized tax benefits in the next twelve months.

NOTE 10—COMMITMENTS AND CONTINGENCIES

Lease Commitments: The Company leases its headquarters and office facilities from nonaffiliated parties under operating leases. Rent expense for the years ended December 31, 2017, 2016 and 2015 was $2,007,705, $1,717,807 and $1,489,736, respectively. Rent commitments related to the lease of the Company's main office and branch facilities, before considering renewal options and additional lessor charges, were as follows:

2018	$ 1,629,972
2019	1,606,245
2020	1,645,328
2021	1,693,146
2022	1,684,852
Thereafter	3,762,002
Total	$ 12,021,545

Off-Balance-Sheet Credit Risk: The commitments and contingent liabilities include various commitments to extend credit and standby letters of credit, which arise in the normal course of business. Commitments to extend credit are legally binding loan commitments with set expiration dates. Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. They are intended to be disbursed, subject to certain conditions, upon request of the borrower.

The Company evaluates the creditworthiness of each customer. Collateral, if deemed necessary by the Company upon the extension of credit, is obtained based on management's evaluation of the borrower. Collateral for commercial and industrial loans may vary, but may include securities, accounts receivable, inventory, property, plant and equipment, and income producing commercial or other properties.

The Company had loan commitments granted and undisbursed of approximately $60,748,000 and $54,774,000; commitments under outstanding commercial letters of credit of approximately $1,608,000 and $915,000; and standby letters of credit and guarantee of approximately $1,627,000 and $1,499,000 at December 31, 2017 and 2016, respectively. The majority of these off-balance sheet commitments have a variable interest rate. Management does not anticipate any material losses as a result of these transactions.

NOTE 11—STOCK-BASED COMPENSATION

The Company has two stock-based compensation plans currently in effect as of December 31, 2017, as described further below. Total compensation cost that has been charged against earnings for these plans in 2017, 2016 and 2015 was $668,018, $1,205,117, and $868.444, respectively.

2005 Plan: In 2005, the Board of Directors and shareholders of the Bank approved a stock option plan for the benefit of directors and employees of the Bank (the "2005 Plan"). The 2005 Plan was assumed by the Company in 2016 at the time of the bank holding company reorganization. Under the 2005 Plan, the Bank was authorized to grant options to purchase up to 770,000 shares of the Company's common stock. The exercise prices of the options may not be less than 100 percent of the fair value of the Company's common stock at the date of grant.

The options, when granted, vest either immediately or ratably over five years from the date of the grant and expire after ten years if not exercised.

There were no stock options granted under the 2005 Plan during 2017 or 2016.

NOTE 11—STOCK-BASED COMPENSATION (Continued)

A summary of the transactions under the 2005 Plan for the year ended December 31, 2017 is as follows:

	Number of Options Outstanding	Weighted Average Exercise Price	Aggregate Intrinsic Value
Outstanding, beginning of year	375,000	$ 3.95	
Options granted	-	-	
Options exercised	(40,000)	3.54	
Options forfeited	-	-	
Options expired	-	-	
Outstanding, as of December 31, 2017	335,000	3.99	$ 1,944,950
Fully vested and expected to vest	328,500	3.95	$ 1,921,435
Vested	309,000	$ 3.81	$ 1,850,890

Information related to the 2005 Plan during each year follows:

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Intrinsic value of options exercised	$ 174,700	$ 71,250	$ 175,000
Cash received from option exercises	141,550	76,250	152,500
Tax benefit realized from option exercised	-	-	-

There were no shares available for grant under the 2005 Plan as of December 31, 2017. The weighted average remaining contractual term of stock options outstanding under the 2005 Plan at December 31, 2017 was 3.55 years. The weighted average remaining contractual term of stock options that were exercisable at December 31, 2017 was 3.37 years.

As of December 31, 2017, the Company had approximately $24,173 of unrecognized compensation costs related to unvested stock options under the 2005 Plan. The Company expects to recognize these costs over a weighted average period of 0.75 year.

2010 Plan: In 2010, the Board of Directors of the Bank approved a new equity incentive plan for granting stock options and restricted stock awards to key employees, officers, and non-employee directors of the Bank (the "2010 Plan"). In 2013, the 2010 Plan was amended and approved by the shareholders to increase the number of shares authorized to be issued under from 1,350,000 shares to 2,500,000 shares of common stock. The 2010 Plan was assumed by the Company in 2016 at the time of the bank holding company reorganization.

The exercise prices of stock options granted under the plan may not be less than 100 percent of the fair value of the Company's stock at the date of grant. The options, when granted, vest ratably over five years from the date of the grant and expire after ten years if not exercised. Option prices under the 2010 Plan are to be equal to the fair value of the Company's common stock on the date of grant. There were no stock options granted under the 2010 Plan during 2017 or 2016.

Restricted stock awards issued under the 2010 Plan may or may not be subject to vesting provisions. Awards which were granted in 2017 and 2016 are not subject to vesting provisions. Owners of the restricted stock awards shall have all of the rights of a shareholder including the right to vote the shares and to all dividends (cash or stock). Compensation expense related to restricted stock awards will be recognized over the vesting period of the awards based on the fair value of the Company's common stock at the issue date.

NOTE 11—STOCK-BASED COMPENSATION (Continued)

A summary of stock options issued under the 2010 Plan for the year ended December 31, 2017 is as follows:

	Number of Options Outstanding	Weighted Average Exercise Price	Aggregate Intrinsic Value
Outstanding, beginning of year	895,000	$ 4.07	
Options granted	-	-	
Options exercised	(100,000)	2.85	
Options forfeited	-	-	
Options expired	-	-	
Outstanding, as of December 31, 2017	795,000	4.22	$ 4,437,350
Fully vested and expected to vest	765,000	4.07	$ 4,383,350
Vested	675,000	$ 3.55	$ 4,221,350

Information related to stock options issued under the 2010 Plan during each year follows:

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Intrinsic value of options exercised	$ 497,000	$ 124,900	$ 268,460
Cash received from option exercises	285,000	80,700	196,590
Tax benefit realized from option exercised	208,988	37,858	81,374

The weighted average remaining contractual term of stock options outstanding under the 2010 Plan at December 31, 2017 was 3.69 years. The weighted average remaining contractual term of stock options that were exercisable at December 31, 2017 was 3.24 years.

A summary of the changes in the Company's non-vested restricted stock awards under the 2010 Plan for the year ended December 31, 2017 is as follows:

	Shares Issued	Weighted Average Grant Date Fair Value	Aggregate Intrinsic Value
Non-vested, beginning of year	644,000	$ 5.68	
Awards granted	153	9.85	
Awards vested	(188,653)	5.02	
Awards forfeited	(2,000)	5.75	
Non-vested, end of year	453,500	$ 5.95	$ 4,444,300

Information related to non-vested restricted stock awards under the 2010 Plan during each year follows:

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Tax benefit realized from awards vested	$ 614,711	$ 483,286	$ 488,459

NOTE 11—STOCK-BASED COMPENSATION (Continued)

There were 218,605 shares available for grant under the 2010 Plan as of December 31, 2017 (in either stock options or restricted stock awards). As of December 31, 2017, the Company had approximately $2,505,538 of unrecognized compensation cost related to unvested stock options and restricted stock awards under the 2010 Plan. The Company expects to recognize these costs over a weighted average period of 2.35 years. The total fair value of shares vested during 2017was $1,039,362.

NOTE 12—EMPLOYEE BENEFIT PLAN

The Company established a 401(k) profit sharing plan (the "401(k) Plan") which is open to all eligible employees who are at least 21 years old and have completed 90 days of service. Each employee is allowed to contribute to the 401(k) Plan up to the maximum percentage allowable, not to exceed the limits of applicable IRS Code Sections. Each year, the Company may, in its discretion, make matching contributions to the 401(k) Plan. Total employer contributions to the 401(k) Plan amounted to $419,733, $374,692, and $298,154 for the years ended December 31, 2017, 2016 and 2015, respectively.

NOTE 13—FAIR VALUE OF FINANCIAL INSTRUMENTS

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. There are three levels of inputs that may be used to measure fair values:

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

Securities Available for Sale: The fair values of investment securities are determined by matrix pricing, which is a mathematical technique used to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2). Management obtains the fair values of investment securities on a monthly basis from a third-party pricing service.

Impaired Loans: The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's judgment, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

Appraisals for collateral-dependent impaired loans are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Company. Once received, a member of the credit department reviews the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison with independent data sources such as recent market data or industry-wide statistics.

NOTE 13—FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Assets and liabilities measured at fair value on a recurring basis at December 31, 2017 and 2016 are summarized below:

		Fair Value Measuring Using		
	Total Fair Value	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
As of December 31, 2017:				
U.S. Government sponsored agency securities	$ 6,932,008	$ -	$ 6,932,008	$ -
Mortgage-backed securities - residential	13,940,525	-	13,940,525	-
Collateralized mortgage obligations	18,113,498	-	18,113,498	-
Other securities	2,485,680	-	2,485,680	-
As of December 31, 2016:				
U.S. Government sponsored agency securities	$ 6,977,162	$ -	$ 6,977,162	$ -
Mortgage-backed securities - residential	17,556,037	-	17,556,037	-
Collateralized mortgage obligations	10,930,252	-	10,930,252	-

There were no transfers between level 1 and level 2 during 2017 or 2016. There were no assets or liabilities measured at fair value on a non-recurring basis at December 31, 2017 or 2016.

Financial Instruments: The carrying amounts and estimated fair values of financial instruments not carried at fair value, at December 31, 2017 are as follows:

	Carrying Amount	Level 1	Level 2	Level 3	Value
Financial Assets:					
Cash and cash equivalents	$ 63,249,952	$63,249,952	$ -	$ -	$ 63,249,952
Loans held for sale	15,739,305	-	17,203,060	-	17,203,060
Loans receivable, net	738,884,413	-	-	731,436,572	731,436,572
Accrued interest receivable	2,463,486	-	189,005	2,274,481	2,463,486
FHLB and PCBB stock	4,286,500	N/A	N/A	N/A	N/A
Financial Liabilities:					
Deposit	$773,306,014	$ -	$773,071,521	$ -	$773,071,521
FHLB Advances	25,000,000	-	25,000,000	-	25,000,000
Accrued interest payable	423,239	-	423,239	-	423,239

NOTE 13—FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

The carrying amounts and estimated fair values of financial instruments not carried at fair value at December 31, 2016 are as follows:

	Carrying Amount	Level 1	Level 2	Level 3	Value
Financial Assets:					
Cash and cash equivalents	$ 20,126,028	$20,126,028	$ -	$ -	$ 20,126,028
Loans held for sale	1,646,250	-	1,793,260	-	1,793,260
Loans receivable, net	666,317,092	-	-	661,997,633	661,997,633
Accrued interest receivable	2,001,488	-	181,352	1,820,136	2,001,488
FHLB and PCBB stock	3,437,600	N/A	N/A	N/A	N/A
Financial Liabilities:					
Deposit	$661,783,900	$ -	$662,160,942	$ -	$662,160,942
FHLB Advances	10,000,000	-	10,000,000	-	10,000,000
Accrued interest payable	321,753	-	321,753	-	321,753

The methods and assumptions, not previously presented, used to estimate fair value are described as follows:

(a) Cash and Cash equivalents

The carrying amounts of cash and short-term instruments approximate fair values and are classified as Level 1.

(b) Loans Held for Sale

The fair value of loans held for sale is estimated based upon binding contracts and quotes from third party investors resulting in a Level 2 classification.

(c) Loans Receivable, Net

Fair values of loans, excluding loans held for sale, are estimated as follows: For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values resulting in a Level 3 classification. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality resulting in a Level 3 classification. Impaired loans are valued at the lower of cost or fair value as described previously. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

(d) FHLB and PCBB Stock

It is not practical to determine the fair value of FHLB and PCBB stock due to restrictions placed on their transferability.

(e) Deposits

The fair values disclosed for demand deposits (e.g., interest and non-interest checking, passbook savings, and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amount) resulting in a Level 2 classification. The carrying amounts of variable rate, fixed-term money market accounts and certificates of deposit approximate their fair values at the reporting date resulting in a Level 2 classification. Fair values for fixed rate certificates of deposit are estimated using a discounted cash flows calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits resulting in a Level 2 classification.

NOTE 13—FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

(f) Federal Home Loan Bank Advances

The fair values of Federal Home Loan Bank Advances are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements, resulting in a Level 2 classification.

(g) Accrued Interest Receivable/Payable

The carrying amounts of accrued interest approximate fair value and are classified within the same fair value hierarchy level as the related asset or liability.

(h) Off-balance Sheet Instruments

Fair values for off-balance sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value of commitments is not material.

NOTE 14—REGULATORY CAPITAL MATTERS

Banks and bank holding companies are subject to regulatory capital requirements administered by federal banking 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 capital requirements can initiate regulatory action. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Company on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Under the Basel III rules, the Company must hold a capital conservation buffer above the adequately capitalized risk-based capital ratios. The capital conservation buffer is being phased in from 0.0% for 2015 to 2.50% by 2019. The capital conservation buffers for 2016 and 2017 are 0.625% and 1.25%, respectively. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital. Management believes as of December 31, 2017 and 2016, the Company and Bank meet all capital adequacy requirements to which they are subject.

Prompt corrective action regulations provide 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 December 31, 2017 and 2016, 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.

NOTE 14—REGULATORY CAPITAL MATTERS (Continued)

Actual and required capital amounts (in thousands) and ratios, exclusive of the capital conservation buffer, are presented below at December 31, 2017 and 2016:

(Dollars in thousands)	Actual		Required for Capital Adequacy Purposes		Minimum To be Considered "Well Capitalized"	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2017:						
Total capital (to risk-weighted assets)						
Consolidated	$ 100,713	13.49%	$ 59,729	8.00%	N/A	N/A
Bank	100,648	13.48%	59,726	8.00%	74,658	10.00%
Tier 1 capital (to risk-weighted assets)						
Consolidated	91,510	12.26%	44,797	6.00%	N/A	N/A
Bank	91,445	12.25%	44,795	6.00%	59,726	8.00%
Common equity Tier 1 capital (to risk-weighted assets)						
Consolidated	91,510	12.26%	33,597	4.50%	N/A	N/A
Bank	91,445	12.25%	33,596	4.50%	48,528	6.50%
Tier 1 capital (to average assets)						
Consolidated	91,510	10.46%	35,009	4.00%	N/A	N/A
Bank	91,445	10.45%	35,007	4.00%	43,759	5.00%

(Dollars in thousands)	Actual		Required for Capital Adequacy Purposes		Minimum To be Considered "Well Capitalized"	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2016:						
Total capital (to risk-weighted assets)						
Consolidated	$ 89,286	13.40%	$ 53,311	8.00%	N/A	N/A
Bank	89,225	13.39%	53,306	8.00%	66,632	10.00%
Tier 1 capital (to risk-weighted assets)						
Consolidated	81,304	12.20%	39,983	6.00%	N/A	N/A
Bank	81,244	12.19%	39,979	6.00%	53,306	8.00%
Common equity Tier 1 capital (to risk-weighted assets)						
Consolidated	81,304	12.20%	29,987	4.50%	N/A	N/A
Bank	81,244	12.19%	29,985	4.50%	43,311	6.50%
Tier 1 capital (to average assets)						
Consolidated	81,304	10.89%	29,859	4.00%	N/A	N/A
Bank	81,244	10.88%	29,857	4.00%	37,321	5.00%

NOTE 15—EARNINGS PER SHARE

The two-class method is used in the calculation of basic and diluted earnings per share. Under the two-class method, earnings available to common shares are allocated between common shares and participating securities. The Company's restricted stock awards are considered participating securities as the unvested awards have non-forfeitable rights to dividends, paid or unpaid, on unvested awards. The factors used in the earnings per share computation follow:

	Year Ended December 31,		
	2017	2016	2015
Basic			
Net income	$ 9,236,482	$ 7,425,371	$ 5,963,345
Undistributed earnings allocated to participating securities	(366,031)	(402,328)	(412,190)
Net income allocated to common shares	8,870,451	7,023,043	5,551,155
Weighted average common shares outstanding	13,063,344	12,788,378	12,549,915
Basic earnings per common share	$ 0.68	$ 0.55	$ 0.44
Diluted			
Net income allocated to common shares	$ 8,870,451	$ 7,023,043	$ 5,551,155
Weighted average common shares outstanding for basic earnings per common share	13,063,344	12,788,378	12,549,915
Add: Dilutive effects of assumed exercises of stock options	422,447	369,777	394,952
Average shares and dilutive potential common shares	13,485,791	13,158,155	12,944,867
Diluted earnings per common share	$ 0.66	$ 0.53	$ 0.43

Stock options and restricted stock awards for 220,000, 305,000 and 305,000 shares of common stock were not considered in computing diluted earnings per common share for the year ended December 31, 2017, 2016 and 2015 because they were antidilutive.

NOTE 16—PARENT COMPANY ONLY CONDENSED FINANCIAL INFORMATION

OP Bancorp (the "Company") is a California corporation whose common stock is quoted on the OTCQB under the ticker symbol, "OPBK." The Company was formed to acquire 100% of the voting equity of Open Bank (the "Bank") and commenced operation as a bank holding company on June 1, 2016. This transaction was treated as an internal reorganization as all shareholders of the Bank became shareholders of the Company. The Company has no operations other than ownership of the Bank. For the parent company only condensed statements of income and comprehensive income, and cash flows, we have assumed that the Company existed as of January 1, 2016.

Condensed financial information of OP Bancorp follows:

CONDENSED BALANCE SHEETS
December 31, 2017 and 2016

	December 31, 2017	December 31, 2016
ASSETS		
Investment in banking subsidiaries	$ 91,414,795	$ 81,223,077
Other assets	65,155	60,710
Total assets	$ 91,479,950	$ 81,283,787
LIABILITIES AND SHAREHOLDERS' EQUITY		
Shareholders' equity	91,479,950	81,283,787
Total liabilities and shareholders' equity	$ 91,479,950	$ 81,283,787

NOTE 16—PARENT COMPANY ONLY CONDENSED FINANCIAL INFORMATION (Continued)

CONDENSED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
Years ended December 31, 2017 and 2016

	2017	2016
Other expense	$ 37,824	$ 144,464
Income before income tax and undistributed subsidiary income	(37,824)	(144,464)
Income tax benefit	(15,903)	(59,500)
Equity in undistributed subsidiary income	9,258,403	7,510,335
Net income	$ 9,236,482	$ 7,425,371

CONDENSED STATEMENT OF CASH FLOWS
Years ended December 31, 2017 and 2016

	2017	2016
Cash flows from operating activities		
Net income	$ 9,236,482	$ 7,425,371
Adjustments:		
Equity in undistributed subsidiary income	(9,258,403)	(7,510,335)
Change in other assets	21,921	84,964
Net cash from operating activities	-	-
Cash flows from investing activities		
Investment in subsidiaries	-	-
Net cash from investing activities	-	-
Cash flows from financing activities		
Proceeds from subsidiaries	-	-
Net cash from financing activities	-	-
Net change in cash and cash equivalents	-	-
Cash and cash equivalents at beginning of year	-	-
Cash and cash equivalents at end of year	$ -	$ -