

WELCOME TO THE FUTURE

of community banking

BEST 50
OTC QX
2017

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Board of Directors



William A. Benneyan, Chairman

Bill was born and educated in Fresno, CA, and is a graduate of California State University, Fresno. He has lived in the Visalia, Lindsay and Fresno areas his entire life. Bill is a Certified Public Accountant and owned a CPA practice in Lindsay and Visalia. Bill is also a custom home builder and is currently the President of Benart S&L Custom Homes. Bill is the former Vice-Chairman of Mineral King National Bank, a highly successful community bank in Visalia that sold to Vallicorp in 1994 and served on the Vallicorp Board of Directors until its sale to Westamerica Bank. Bill then served on the Central Valley Advisory Board for Westamerica Bank.



Ciaran McMullan, President & CEO

Ciaran is a native of the agricultural north west of Northern Ireland. He held senior roles in banking in Europe and Australia before moving to the U.S., where he served as Chairman of the Great Western Bancorporation, CEO of National Australia Bank Americas based in the Midwest, and as a Managing Director with Capello Capital Corporation in California. His expertise is in agribusiness and small business banking, and in developing and building banking businesses. He is a graduate of Stirling University and Sheffield Hallam University in the UK, and attended Harvard Business School's Executive Education Program in Agribusiness.



David C. Crinklaw

Dave is a resident of Exeter, with business interests throughout the Central Valley. Dave sold his home construction business in 2000 and now specializes in commercial construction. He also farms grapes in Fresno and Tulare counties and manages a farm services company serving the Central Valley.



Gary E. Esajian

Gary has lived in the Lemoore area most of his life. He farms in Kings, Fresno and Tulare counties and manages real estate development interests here and in San Luis Obispo County. Gary serves on the Board of the Westlands Water District and the San Joaquin Valley Cotton Board, and is active in local farm bureaus and chambers of commerce.



Florencio "Frank" Paredes

A native of Tulare County, Frank graduated from College of the Sequoias and farms in the Exeter area. He owns a packinghouse and the Hungry Hollow Borrow Pit in Porterville and is active in local and San Francisco-based farmers' markets. Frank has been active on many boards of directors for organizations throughout Tulare County.



Darrell Tunnell

Darrell was born in Porterville and raised in Terra Bella. He moved to Visalia in 1979, where he began working in the aircraft repair and maintenance field. In 1984 Darrell received his airframe and power plant certificate from the Federal Aviation Administration. Darrell has owned Aircraft Mechanical Services, Inc., which is the Visalia Airport fixed base operator (FBO) since 1988. Darrell is active in many sports and is an active contributor to school and civic organizations. He is also a proud supporter of the American Cancer Society and Wounded Warrior Project.



Marc R. Schuil, Vice Chairman

Marc is a co-founder of Schuil & Associates and has partnered with his two brothers, Mike Schuil and Rick Schuil for over 30 years. Marc earned a Bachelor of Science degree from Fresno State University and an MBA in Finance and Marketing from the University of Southern California. In addition to holding his broker's license in the state of California, he is currently an active licensed broker in the states of California, Texas, Oklahoma, Arizona, Iowa, South Dakota, Oregon, Kansas, Colorado, and New Mexico. Marc's strong investment and analytical skills have assisted him in evaluating profit potentials of various agricultural opportunities. Marc has been involved in a variety of civic organizations.



Daniel C. Jacuzzi

A lifelong resident of the Yuba-Sutter area, Dan is a real estate broker and owner of Century 21 Select Real Estate, Select School of Real Estate, Stanford Mortgage, Select Property Management and Coldwell Banker Select of Nevada. His companies employ nearly 1,000 people throughout Northern California, Lake Tahoe and Northern Nevada. Dan was named Realtor Broker of the Year in 1995 and 1999, and his brokerage firm has been recognized by Realtor Magazine as one of the "Top 100 Largest Real Estate Firms" in the nation. He is an active member of the Association of Realtors in Sacramento, El Dorado, Placer, Butte, Yuba and Sutter counties.



Michael E. Thurlow

Mike is a native of the Reedley/Kingsburg area, and is a graduate of Reedley High, Reedley College and California Polytechnic University, San Luis Obispo. Mike is an owner/manager of a produce company that stores, packs and ships fruit raised in the South Valley. Mike is active in the community personally and through his business.



Eric M. Shannon

Eric's family has been farming in the area for more than 100 years and Eric continues that tradition. A graduate of UC Davis, Eric farms and is active in real estate development projects in the Visalia area. He served as president of his Rotary Club and is active in many other organizations.



Eric Wilkins

Eric was formerly the Vice Chairman of Security First Bank, and was born and raised in Fresno. He received an Associates of Arts degree from Santa Barbara City College and his Bachelor of Political Science degree from University of California, Santa Barbara. Eric, along with his family, owns and operates Wilkins Enterprises. The company specializes in the development, construction and management of office and industrial buildings in the Central Valley. Eric holds a license as a real estate broker from the State of California and an "A" class general engineering contractor's license also issued by the State. He sat as chair of the Oakhurst Citizens Advisory Committee and has been a member of the public relations committee for Madera County Maintenance District 22, and is a member of the Eastern Madera County Chamber of Commerce. He is also a member of the National Association of Realtors and the California Association of Realtors.



Dale B. Margosian

Born in Dinuba, Dale is a longtime resident of Porterville and a graduate of California State University, Fresno. He has managed a thriving CPA practice in Porterville for over 28 years and participates in many civic organizations.



Matthew B. Pomeroy

Born and raised in Yuba City, Matt has been a self-employed contractor with Pomeroy Construction for 20 years, building custom homes in the Yuba County foothills. Matt and his brother, Jarrod, took over their family farming operation in 2011, growing peaches, prunes and walnuts. Matt was a founding board member of Sutter Community Bank. He built his own home in the foothills and enjoys spending time with his wife and two sons.

Dear Shareholders and Customers,

On behalf of the Suncrest Bank Board of Directors, we are pleased to present our annual report for 2016. It has been a truly remarkable year for our bank.

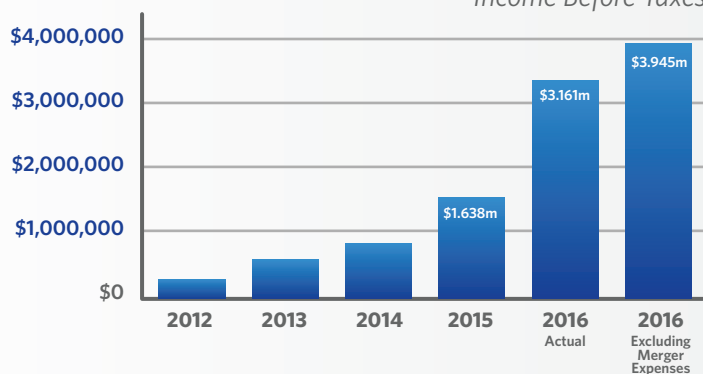
Named to the OTCQX Top 50 Stocks for 2016

This year our strategic plan has really started to pay-off in terms of our stock market performance, with Suncrest Bank being named to the 2017 OTCQX® Best 50 List. This is an annual ranking of the top 50 U.S. and international companies traded on the OTCQX market. The ranking is calculated based on an equal weighting of one-year total shareholder return and average daily dollar volume growth in the calendar year 2016. Suncrest Bank was ranked number 15 on the list, ranking us as the second best performing bank stock on the OTCQX market.

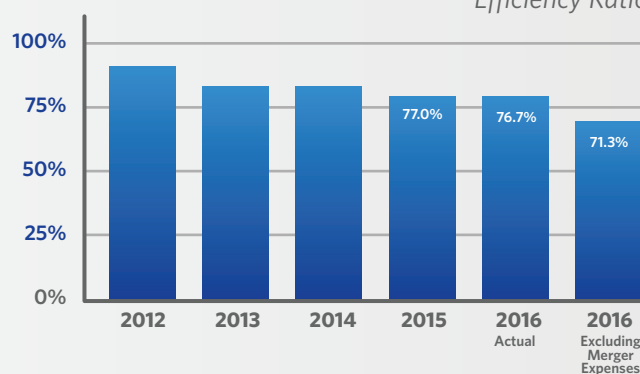
Record Breaking Results

We also had a record breaking year in terms of our financial results. At December 31, 2016, our assets totaled \$447.7 million which is an increase of \$150.8 million, or 51% over the prior years ending balance. Our loan portfolio grew by \$98.9 million to \$307.7 million, a 47 % increase over 2015, and our total deposits grew by \$132.3 million and ended the year at \$389.0 million, a 52% increase over the prior year. Our net income for the year was \$1,733,000 or \$2,263,000 excluding one-time expenses associated with our acquisition of Security First Bank in December 2016. Both our Return on Average Assets (ROAA) and our Efficiency Ratio have continued to improve in line with our strategic growth trajectory and were 0.49% (or 0.69% excluding one-time expenses) and 76.7% (or 71.3% excluding one-time expenses) respectively.

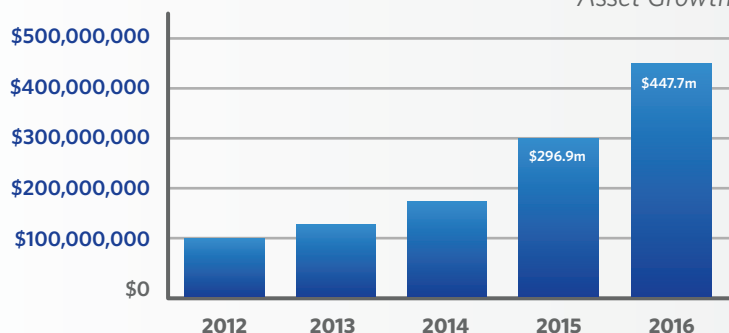
Income Before Taxes



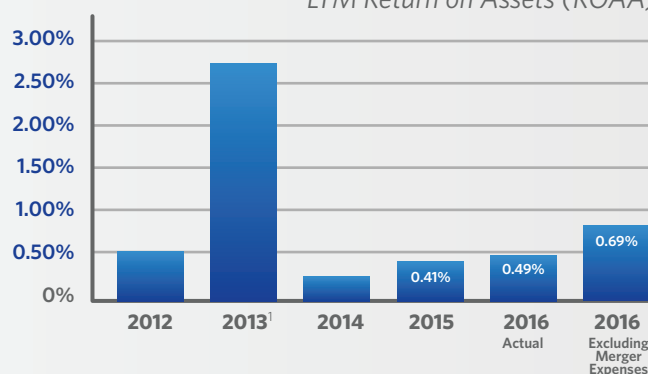
Efficiency Ratio



Asset Growth



LTM Return on Assets (ROAA)



1 2013 includes the impact of the DTA

One of the fastest growing banks in country

In the fall of 2013, we set for ourselves the ambitious target of reaching \$500 million in total assets within five years. We are 90% of the way to reaching that goal with nearly two years to spare, and have grown our total assets by 348% since 2013². This outstanding growth rate places Suncrest Bank as the 23rd fastest growing bank in the US and 3rd fastest growing bank in the State of California, and is a testament to the hard work and dedication of our Board, management and entire employee group.

² % growth in total assets from 3/31/13 to 12/31/16

3rd fastest growing bank
IN CA OUT OF APPROX. 190 SINCE 2013²

Rank	Name	Percent
1	Banc of California	569
2	First Foundation Bank	359
3	Suncrest Bank	348
4	Premier Business Bank	347
5	Pacific Western Bank	314

Source: Bankshape www.bankshape.com

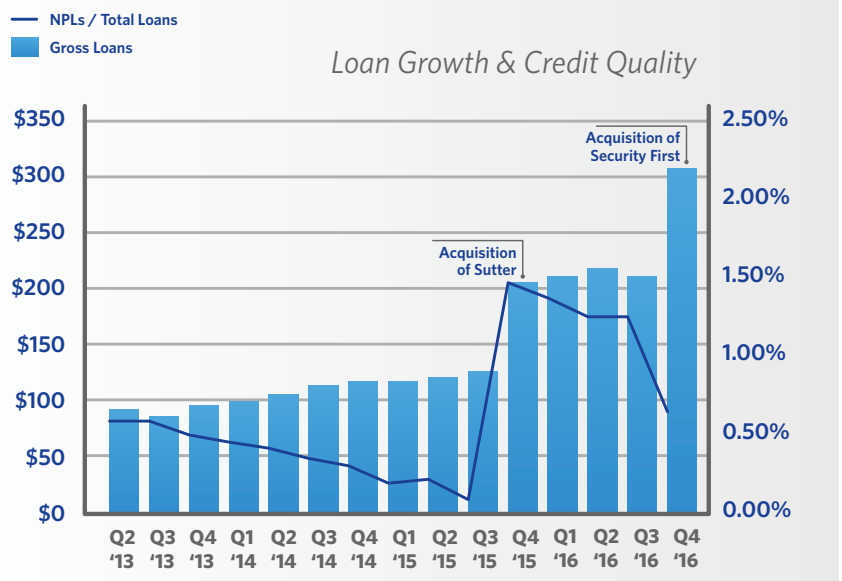
23rd fastest growing bank
IN THE US OUT OF APPROX. 6,800 SINCE 2013²

Rank	Name	State	Percent
21	First Foundation Bank	CA	359
22	Sunshine Bank	FL	355
23	Suncrest Bank	CA	348
24	Premier Business Bank	CA	347
25	ConnectOne Bank	NJ	340

Source: Bankshape www.bankshape.com

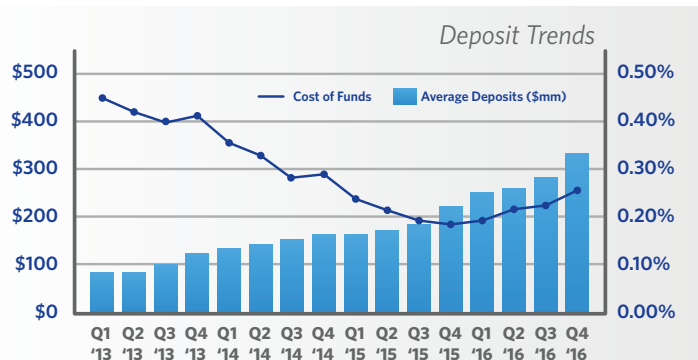
Prudent and Profitable Growth

Through this period of rapid growth we have steadily improved the credit quality of our portfolio. In fact, the legacy Suncrest Bank has had less than \$100,000 in net charge-offs since its inception. We did acquire a small distressed loan pool as a result of our acquisition of Sutter Community Bank in December 2015, consisting of approximately \$3.8 million in non-performing loans and \$0.6 million in OREO, and we have been able to manage that down significantly and non-performing assets improved to 0.47% of total assets at December 31, 2016.



Prudent and Profitable Growth (continued)

In addition, we have been able to maintain an average loan yield of approximately 5.5% throughout this same period of rapid growth, while significantly reducing our average cost of deposits by over 20 basis points.



Acquisition of Security First Bank

In December of 2016, we completed the acquisition of Security First Bank in Fresno, California, welcoming their shareholders, customers and staff to the Suncrest family. Former Vice Chairman, Eric Wilkins joined the Board of Suncrest Bank and former President and CEO, Steve Jones, joined us as our Chief Operating Officer. A number of the former Security First Bank Board Directors have also established a local advisory Board to support our Fresno market team as they continue to build our business in that community. The transaction was attractively priced and structured for both sets of shareholders. We minimized dilution for existing shareholders, with pre-merger tangible book value per share expected to be earned back in just over one year, and Security First Bank shareholders, who opted to take stock in the transaction, have seen a 67% increase in the value of their holdings based on a 12/30/16 closing price for SBKK of \$10.50.

Our Local Market Business Model

At the heart of our success has been our Local Market Business Model. We have four distinct market areas - Visalia-Kingsburg, Porterville, Yuba-Sutter and Fresno - each one led by a Market President, with considerable local decision making authority, focused on growing *only* locally sourced deposits that are in turn

only used to fund small business and ag lending in their respective markets. In each market, we have either Main Board Directors or Local Advisory Board Directors and these Directors actively support their Market Presidents in the building of their businesses. In many ways, each of our main branches feel and operate like standalone community banks run by people from the local area, for people in the local area, supported by a group of local community leaders. This model has been in place since early 2014 for both Visalia and Porterville and in that time we have increased our market share³ from 2.67% to 5.36% in Visalia (growth of 101%) and from 3.85% to 8.18% in Porterville (growth of 112%). The model has been in place in Yuba-Sutter since January of 2016, just after we acquired Sutter Community Bank, and we are currently in the process of implementing it in Fresno, following the acquisition of Security First Bank in December of 2016. Our market share in each of those communities is 3.65% and 0.64%⁴ respectively and we expect to see similar growth rates to those achieved in our Visalia and Porterville markets, over the next three years.

The Future of Community Banking

We designed our Local Market Business Model by leaning heavily on the lessons of the past and the way banking “used to be”, back in the day when your local branch manager could make decisions on the spot and all your banking and lending needs could be served in one place. However, that doesn’t mean we are living in the past. We are equally committed to ensuring we make the best use of modern technology to serve our customer needs quickly and effectively, and that we continue to innovate how our products and services are delivered to the customers and communities we serve. We believe our new state-of-the-art flagship branch in downtown Visalia reflects this commitment and represents the future of community banking, where simple transactions are executed effortlessly using new digital technology but where important conversations about your financial needs are held face-to-face in a welcoming, modern and community focused environment. The new branch, which we will use as a template to make improvements throughout our network, includes a commercial coffee shop and café, an open plan layout utilizing cash recycler stations rather than the traditional teller line, paperless iPad enabled new account opening, and a giant video wall and community presentation space that our clients and local community can utilize for meetings and audio-visual presentations to help support their own businesses or local events. We believe this combination of technology together with face-to-face interaction truly is the future of community banking.

In closing, we want to thank our Board of Directors for their continued guidance and commitment, and all our shareholders and customers for their ongoing investment and support.

William A. Benneyan
Chairman

Ciaran McMullan
President & CEO

3 Source: www.FDIC.gov. Market share data as at 6/30/13 compared to 6/30/16

4 Source: www.FDIC.gov. Market share data as at 6/30/16

This statement has not been reviewed, or confirmed for accuracy or relevance, by the Federal Deposit Insurance Corporation.

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Vavrinek, Trine, Day & Co., LLP
Certified Public Accountants

VALUE THE DIFFERENCE

INDEPENDENT AUDITOR'S REPORT

Board of Directors and Shareholders of
Suncrest Bank

Report on Financial Statements

We have audited the accompanying financial statements of Suncrest Bank, which are comprised of the statements of financial condition as of December 31, 2016 and 2015, and the related statements of income, comprehensive income, changes in shareholders' equity and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Suncrest Bank as of December 31, 2016 and 2015, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Vavrinek, Trine, Day & Co., LLP
Laguna Hills, California
March 29, 2017

FINANCIAL STATEMENTS:

Statements of Financial Condition

*December 31, 2016 & 2015**Assets*

	2016	2015
Cash and Due from Banks	\$15,567,875	\$5,370,556
Federal Funds Sold	36,979,000	8,691,000
Interest-Bearing Deposits in Other Banks	10,000,000	10,000,000
Total Cash and Cash Equivalents	62,546,875	24,061,556
Investment Securities Available for Sale	53,567,064	54,342,949
Loans:		
Real Estate - Other	229,229,127	163,553,994
Construction and Land Development	14,276,680	4,945,745
Commercial and Industrial	63,878,883	39,530,750
Consumer	352,881	807,079
Total Loans	307,737,571	208,837,568
Deferred Loan Fees, Net of Costs	(219,817)	(458,940)
Allowance for Loan Losses	(2,496,163)	(2,245,566)
Net Loans	305,021,591	206,133,062
Federal Home Loan Bank and Other Bank Stock, at Cost	3,152,891	1,465,968
Premises and Equipment	4,218,360	2,778,028
Other Real Estate Owned	788,842	649,092
Bank Owned Life Insurance	5,114,446	2,080,857
Net Deferred Tax Assets	5,661,000	3,507,000
Goodwill	3,325,220	-
Core Deposit Intangible	1,576,611	428,000
Accrued Interest and Other Assets	2,679,728	1,436,599
	\$447,652,628	\$296,883,111

*The accompanying notes are an integral part of these financial statements.

Liability & Shareholders' Equity

	2016	2015
Deposits:		
Noninterest-bearing Demand	\$122,835,165	\$84,064,420
Savings, NOW and Money Market Accounts	181,779,826	114,593,224
Time Deposits Under \$250,000	44,831,946	31,588,069
Time Deposits \$250,000 and Over	39,539,342	26,431,525
Total Deposits	388,986,279	256,677,238
Accrued Interest and Other Liabilities	1,375,691	874,392
Total Liabilities	390,361,970	257,551,630
Commitments and Contingencies - Notes E and K		
Shareholders' Equity:		
Preferred Stock - No par value, 10,000,000 Shares <i>Authorized, None Outstanding</i>	-	-
Common Stock - No par value, 25,000,000 Shares Authorized <i>Shares Issued and Outstanding, 6,979,497 in 2016 and 4,999,895 in 2015</i>	57,046,519	40,653,892
Additional Paid-in Capital	1,851,183	1,703,561
Accumulated Deficit	(1,210,042)	(2,942,986)
Accumulated Other Comprehensive Income Loss - Net <i>Unrealized Loss on Securities Available for Sale, Net of Taxes of \$275,882 in 2016 and \$57,668 in 2015</i>	(397,002)	(82,986)
Total Shareholders' Equity	57,290,658	39,331,481
	\$447,652,628	\$296,883,111

*The accompanying notes are an integral part of these financial statements.

FINANCIAL STATEMENTS:

Statements of Income

For the Years Ended December 31, 2016 & 2015

	2016	2015
Interest Income		
Interest and Fees on Loans	\$12,905,528	\$8,196,445
Interest on Investment Securities	861,307	725,238
Interest on Federal Funds Sold and Other	336,770	118,602
Total Interest Income	14,103,605	9,040,285
Interest Expense		
Interest on Savings Deposits, NOW and Money Market Accounts	203,798	161,343
Interest on Time Deposits	448,644	226,177
Interest on Other Borrowings	3,806	5
Total Interest Expense	656,248	387,525
Net Interest Income	13,447,357	8,652,760
Provision for Loan Losses	235,000	522,275
Net Interest Income After Provision For Loan Losses	13,212,357	8,130,485
Noninterest Income		
Service Charges, Fees, and Other Income	535,563	201,997
Bargain Purchase Gain on Acquisition of Sutter Community Bank	-	314,499
Gain on Sale of Loans	568,612	240,378
	1,104,175	756,874
Noninterest Expense		
Salaries and Employee Benefits	6,092,427	4,182,051
Occupancy Expenses	962,162	704,671
Equipment Expenses	370,703	180,299
Other Expenses	3,730,596	2,182,623
	11,155,888	7,249,644
Income Before Taxes	3,160,644	1,637,715
Income Taxes	1,427,700	729,061
Net Income	\$1,732,944	\$908,654
Net Income Per Share - Basic	\$0.34	\$0.25
Net Income Per Share - Diluted	\$0.34	\$0.25

*The accompanying notes are an integral part of these financial statements.

FINANCIAL STATEMENTS:

Statements of Comprehensive Income

For the Years Ended December 31, 2016 & 2015

	2016	2015
Net Income	\$1,732,944	\$908,654
Other Comprehensive Income (Loss)		
Unrealized Gains and Losses on Securities Available for Sale		
<i>Change in Net Unrealized Loss</i>	(532,230)	(121,698)
	(532,230)	(121,698)
Income Taxes (Benefit):		
<i>Change in Net Unrealized Loss</i>	(218,214)	(49,896)
	(218,214)	(49,896)
Total Other Comprehensive Loss	(314,016)	(71,802)
Total Comprehensive Income	\$1,418,928	\$836,852

*The accompanying notes are an integral part of these financial statements.

FINANCIAL STATEMENTS:

Statements of Changes in Shareholders' Equity

For the Years Ended December 31, 2016 & 2015

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total
	Number of Shares	Amount				
Balance January 1, 2015	2,649,634	\$24,126,478	\$1,614,538	\$(3,851,640)	\$(11,184)	\$21,878,192
Net Income				908,654		908,654
Stock-based Compensation			185,413			185,413
Issuance of Stock to Employees in Exchange for Services Rendered	13,770	96,390	(96,390)			-
Issuance of Common Stock, net of Expenses of \$324,959	1,192,075	8,019,566				8,019,566
Issuance of Common Stock in the Acquisition of Sutter Community Bank	1,144,416	8,411,458				8,411,458
Other Comprehensive Loss, Net of Taxes					(71,802)	(71,802)
Balance at December 31, 2015	4,999,895	40,653,892	1,703,561	(2,942,986)	(82,986)	39,331,481
Net Income				1,732,944		1,732,944
Stock-based Compensation			283,432			283,432
Stock Options Exercised	23,000	145,050				145,050
Issuance of Stock to Employees in Exchange for Services Rendered	19,330	135,810	(135,810)			-
Issuance of Common Stock, net of Expenses of \$338,904	848,486	6,661,105				6,661,105
Issuance of Stock in the Acquisition of Security First Bank	1,088,786	9,450,662				9,450,662
Other Comprehensive Loss, Net of Taxes					(314,016)	(314,016)
Balance at December 31, 2016	6,979,497	\$57,046,519	\$1,851,183	\$(1,210,042)	\$(397,002)	\$57,290,658

*The accompanying notes are an integral part of these financial statements.

FINANCIAL STATEMENTS:

Statements of Cash Flows

For the Years Ended December 31, 2016 & 2015

	2016	2015
Operating Activities		
Net Income	\$1,732,944	\$908,654
Adjustments to Reconcile Net Income to Net Cash From Operating Activities		
Depreciation and Amortization	546,429	242,997
Stock-based Compensation	283,432	185,413
Provision for Loan Losses	235,000	522,275
Deferred Tax (Benefit) Expense	(196,000)	332,000
Earnings on Bank owned Life Insurance	(62,710)	(4,938)
Gain on Sale of Other Real Estate Owned	(13,028)	-
Gain on Sale of Loans	(568,612)	(240,378)
Loans Originated for Sale	(6,255,627)	(2,310,293)
Proceeds from Sale of Loans	6,881,592	2,587,287
Bargain Purchase Gain	-	(314,499)
Other Items	(412,572)	359,052
Net Cash From Operating Activities	2,170,848	2,267,570
Investing Activities		
Purchase of Available-for-Sale Securities	(21,078,836)	(39,770,988)
Maturities of Available-for-Sale Securities	30,660,376	27,548,880
Net Increase in Loans	(20,576,128)	(37,381,921)
Purchase of Federal Home Loan Bank Stock	(299,100)	(427,700)
Proceeds from Sale of Other Real Estate Owned	26,278	-
Cash (Paid) Acquired in Acquisition	(3,441,268)	14,489,998
Purchase of Premises and Equipment	(1,869,458)	(2,353,093)
Net Cash From Investing Activities	(16,578,136)	(37,894,824)
Financing Activities		
Net Increase in Demand Deposits and Savings Accounts	26,196,602	31,374,390
Net Change in Time Deposits	19,889,850	(174,240)
Proceeds from Issuance of Common Stock, Net	6,661,105	8,019,566
Proceeds from Exercise of Stock Options	145,050	-
Net Cash From Financing Activities	52,892,607	39,219,716
Net Increase in Cash and Cash Equivalents	38,485,319	3,592,462
Cash and Cash Equivalents at Beginning of Year	24,061,556	20,469,094
Cash and Cash Equivalents at End of Year	\$62,546,875	\$24,061,556
Supplemental Disclosures of Cash Flow Information		
Interest Paid	\$639,386	\$371,072
Taxes Paid	\$2,005,000	\$455,000

*The accompanying notes are an integral part of these financial statements.

FINANCIAL STATEMENTS:

Notes to Financial Statements

December 31, 2016 & 2015

Note A - Summary of Significant Accounting Policies

Nature of Operations

The Bank has been incorporated in the State of California and organized as a single operating segment that operates five full-service branches in Visalia, Porterville, Kingsburg, Fresno and Yuba City, California. The Bank's primary source of revenue is providing loans to customers, who are predominately small and middle-market businesses and individuals located primarily in the Central Valley of California.

Subsequent Events

The Bank has evaluated subsequent events for recognition and disclosure through March 29, 2017, which is the date the financial statements were available to be issued.

Use of Estimates in the Preparation of Financial Statements

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

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash, due from banks, interest bearing deposits with original maturity of 90 days or less and federal funds sold. Generally, federal funds are sold for periods of 90 days or less.

Cash and Due from Banks

Banking regulations require that banks maintain a percentage of their deposits as reserves in cash or on deposit with the Federal Reserve Bank. The Bank was in compliance with its reserve requirements as of December 31, 2016.

The Bank maintains amounts due from banks, which may exceed federally insured limits. The Bank has not experienced any losses in such accounts.

Investment Securities

Bonds, notes, and debentures for which the Bank has the positive intent and ability to hold to maturity are reported at cost, adjusted for premiums and discounts that are recognized in interest income using the interest method over the period of maturity.

Investments not classified as trading securities nor as held-to-maturity securities are classified as available-for-sale securities and recorded at fair value. Unrealized gains or losses on available-for-sale securities are excluded from net income and reported as an amount net of taxes as a separate component of other comprehensive income included in shareholders' equity. Premiums and discounts on held-to-maturity and available-for-sale securities are amortized or accreted into income using the interest method. Realized gains or losses of held-to-maturity or available-for-sale securities are recorded 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; OTTI related to credit loss, which must be recognized in the income statement and; 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. For equity securities, the entire amount of impairment is recognized through earnings.

Loans Held for Sale

Government Guaranteed loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated market value in the aggregate. Net unrealized losses are recognized through a valuation allowance by

Note A - Summary of Significant Accounting Policies - Continued

charges to income. Gains or losses realized on the sales of loans are recognized at the time of sale and are determined by the difference between the net sales proceeds and the carrying value of the loans sold, adjusted for any servicing asset or liability. Gains and losses on sales of loans are included in noninterest income.

Loans

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at their outstanding unpaid principal balances reduced by any charge-offs or specific valuation accounts and net of deferred fees or costs on originated loans, or unamortized premiums or discounts on purchased loans. Loan origination fees and certain direct origination costs are capitalized and recognized as an adjustment of the yield of the related loan.

Loans on which the accrual of interest has been discontinued are designated as nonaccrual loans. The accrual of interest on loans is discontinued when principal or interest is past due 90 days based on the contractual terms of the loan or when, in the opinion of management, there is reasonable doubt as to collectability. When loans are placed on nonaccrual status, all interest previously accrued but not collected is reversed against current period interest income. Income on nonaccrual loans is subsequently recognized only to the extent that cash is received and the loan's principal balance is deemed collectible. Interest accruals are resumed on such loans only when they are brought current with respect to interest and principal and when, in the judgment of management, the loans are estimated to be fully collectible as to all principal and interest.

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 uncollectability 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. Amounts are charged-off when available information confirms that specific loans or portions thereof, are uncollectible. This methodology for determining charge-offs is consistently applied to each segment.

The Bank determines a separate allowance for each portfolio segment. The allowance consists of specific and general reserves. Specific reserves relate to loans that are individually classified as impaired. A loan is impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Factors considered in determining impairment include payment status, collateral value and the probability of collecting all amounts when due. Measurement of impairment is based on the expected future cash flows of an impaired loan, which are to be discounted at the loan's effective interest rate, or measured by reference to an observable market value, if one exists, or the fair value of the collateral for a collateral-dependent loan. The Bank selects the measurement method on a loan-by-loan basis except that collateral-dependent loans for which foreclosure is probable are measured at the fair value of the collateral.

The Bank recognizes interest income on impaired loans based on its existing methods of recognizing interest income on nonaccrual loans. 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 with measurement of impairment as described above.

If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral.

General reserves cover non-impaired loans and are based on peer bank historical loss rates for each portfolio segment, adjusted for the effects of qualitative or environmental factors that are likely to cause estimated credit losses as of the evaluation date to differ from the portfolio segment's historical loss experience. Qualitative factors include consideration of the following: changes in lending policies and procedures; changes in economic conditions; changes in the nature and volume of the portfolio; changes in the experience, ability and depth of lending management and other relevant staff; changes in the volume and severity of past due, nonaccrual and other adversely graded loans; changes in the loan review system; changes in the value of the underlying collateral for collateral-dependent loans; concentrations of credit and the effect of other external factors such as competition and legal and regulatory requirements.

Portfolio segments identified by the Bank include real estate - other, construction and land development, commercial and industrial, and consumer loans. Relevant risk characteristics for these portfolio segments generally include debt service coverage, loan-to-value ratios and financial performance on non-consumer loans and credit scores, debt-to income, collateral type and loan-to-value ratios for consumer loans.

Note A - Summary of Significant Accounting Policies - Continued

Certain Acquired Loans

As part of business acquisition, the Bank acquired certain loans that have shown evidence of credit deterioration since origination. These acquired loans are recorded at the allocated fair value, such that there is no carryover of the seller's allowance for loan losses. Such acquired loans are accounted for individually. The Bank estimates the amount and timing of expected cash flows for each purchased loan, and the expected cash flows in excess of the allocated fair value is recorded as interest income over the remaining life of the loan (accretable yield). The excess of the loan's contractual principal and interest over expected cash flows is not recorded (non-accretable difference). Over the life of the loan, expected cash flows continue to be estimated. If the present value of expected cash flows is less than the carrying amount, a loss is recorded through the allowance for loan losses. If the present value of expected cash flows is greater than the carrying amount, it is recognized as part of future interest income.

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 the ultimate recovery of par value. Both cash and stock dividends are reported as income.

Other Real Estate Owned

Real estate acquired by foreclosure or deed in lieu of foreclosure is recorded at fair value at the date of foreclosure, establishing a new cost basis by a charge to the allowance for loan losses, if necessary. Other real estate owned is carried at the lower of cost or fair value, less estimated costs to sell. Fair value is based on current appraisals less estimated selling costs. Any subsequent write-downs are charged against operating expenses. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in other operating expenses. As of December 31, 2016 other real estate owned consisted of vacant land and commercial real estate. The Bank did not have any foreclosures in process as of December 31, 2016.

Premises and Equipment

Land is carried at cost. Premises and equipment are carried at cost less accumulated depreciation and amortization. Depreciation is computed using the straight-line method over the estimated useful lives, which ranges from three to ten years for furniture and equipment and forty years for premises. Leasehold improvements are amortized using the straight-line method over the estimated useful lives of the

improvements or the remaining lease term, whichever is shorter. Expenditures for betterments or major repairs are capitalized and those for ordinary repairs and maintenance are charged to operations as incurred.

Goodwill and Other Intangible Assets

Goodwill is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful lives are not amortized, but tested for impairment at least annually. The Bank has selected December 31 as the date to perform the annual impairment test. Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Goodwill is the only intangible asset with an indefinite life on the balance sheet.

Other intangible assets consist of core deposit intangible assets arising from whole bank acquisitions. They are initially measured at fair value and then amortized over their estimated useful lives of approximately seven years. Amortization expense in 2016 was \$65,000 and in 2015 was \$0. Future amortization expense for the next five years is approximately \$208,000 per year.

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 Bank, 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 Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Income Taxes

Deferred income taxes are computed using the asset and liability method, which recognizes a liability or asset representing the tax effects, based on current tax law, of future deductible or taxable amounts attributable to events that have been recognized in the financial statements. A valuation allowance is established to reduce the deferred tax asset to the level at which it is "more likely than not" that the tax asset or benefits will be realized. Realization of tax benefits of deductible temporary differences and operating loss carryforwards depends on having sufficient taxable income of an appropriate character within the carryforward periods.

The Bank has adopted guidance issued by the Financial Accounting Standards Board ("FASB") that clarifies the accounting for uncertainty in tax positions taken or expected

Note A - Summary of Significant Accounting Policies - Continued

to be taken on a tax return and provides that the tax effects from an uncertain tax position can be recognized in the financial statements only if, based on its merits, the position is more likely than not to be sustained on audit by the taxing authorities. Interest and penalties related to uncertain tax positions are recorded as part of income tax expense.

Earnings Per Share ("EPS")

Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity.

Comprehensive Income

Changes in unrealized gains and losses on available-for-sale securities is the only component of accumulated other comprehensive income for the Bank.

Financial Instruments

In the ordinary course of business, the Bank has entered into off-balance sheet financial instruments consisting of commitments to extend credit, commercial letters of credit, and standby letters of credit as described in Note K. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received.

Stock-Based Compensation

The Bank recognizes the cost of employee services received in exchange for awards of stock options, or other equity instruments, based on the grant-date fair value of those awards. This cost is recognized over the period which an employee is required to provide services in exchange for the award, generally the vesting period. See Note L for additional information on the Bank's stock option plan.

Advertising Costs

The Bank expenses the costs of advertising in the period incurred.

Fair Value Measurement

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an 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. Current accounting guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of

unobservable inputs when measuring fair value. The guidance describes three levels of inputs that may be used to measure fair value:

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 Bank's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

See Note N for more information and disclosures relating to the Bank's fair value measurements.

Reclassifications

Certain reclassifications have been made in the 2015 financial statements to conform to the presentation used in 2016. These reclassifications had no impact of the Bank's previously reported financial statements.

Recent Accounting Guidance Not Yet Effective

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This Update requires an entity to recognize revenue as performance obligations are met, in order to reflect the transfer of promised goods or services to customers in an amount that reflects the consideration the entity is entitled to receive for those goods or services. The following steps are applied in the updated guidance: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when, or as, the entity satisfies a performance obligation. These amendments are effective for public business entities for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period and one year later for nonpublic business entities. Early adoption is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that period. The Bank is currently evaluating the effects of ASU 2014-09 on its financial statements and disclosures.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments-Overall: Recognition and Measurement of Financial Assets and Financial Liabilities (Subtopic 825-10)*. Changes made to the current measurement model primarily affect the accounting for equity securities and readily determinable fair values, where changes in fair value will impact earnings instead of other comprehensive income.

Note A - Summary of Significant Accounting Policies - Continued

The accounting for other financial instruments, such as loans, investments in debt securities, and financial liabilities is largely unchanged. The Update also changes the presentation and disclosure requirements for financial instruments including are a requirement that public business entities use exit price when measuring the fair value of financial instruments measured at amortized cost for disclosure purposes. This Update is generally effective for public business entities in fiscal years beginning after December 15, 2017, including interim periods within those fiscal years and one year later for nonpublic business entities. The Bank is currently evaluating the effects of ASU 2016-01 on its financial statements and disclosures.

In February 2016, the FASB issued Accounting Standards Update (ASU) 2016-02, *Leases (Topic 842)*. The most significant change for lessees is the requirement under the new guidance to recognize right-of-use assets and lease liabilities for all leases not considered short-term leases, which is generally defined as a lease term of less than 12 months. This change will result in lessees recognizing right-of-use assets and lease liabilities for most leases currently accounted for as operating leases under current lease accounting guidance. The amendments in this Update are effective for interim and annual periods beginning after December 15, 2018 for public business entities and one year later for all other entities. The Bank is currently evaluating the effects of ASU 2016-02 on its financial statements and disclosures.

In March 2016, the FASB issued ASU 2016-09, *Improvements to Employee Share-Based Payment Accounting (Topic 718)*. ASU 2016-09 includes provisions intended to simplify various aspects related to how share-based payments are accounted for and presented in the financial statements. Under ASU 2016-09, excess tax benefits and certain tax deficiencies will no longer be recorded in additional paid-in capital ("APIC"). Instead, they will record all excess tax benefits and tax deficiencies as income tax expense or benefit in the income statement, and APIC pools will be eliminated. In addition, the guidance requires excess tax benefits be presented as an operating activity on the statement of cash flows rather than as a financing activity. ASU 2016-09 also permits an accounting policy election for the impact of forfeitures on the recognition of expense for share-based payment awards. Forfeitures can be estimated, as required today, or recognized when they occur. This guidance is effective for public business entities for interim and annual reporting periods beginning after December 15, 2016 and for nonpublic business entities annual reporting periods beginning after December 15, 2017 and interim periods within the reporting periods beginning after December 15, 2018. Early adoption is permitted, but all of the guidance must be adopted in the same period.

The Bank is currently evaluating the provisions of ASU 2016-09 to determine the potential impact on its financial statements and disclosures.

In June 2016, the FASB issued ASU No. 2016-13, *Measurement of Credit Losses on Financial Instruments (Topic 326)*. This ASU significantly changes how entities will measure credit losses for most financial assets and certain other instruments that aren't measured at fair value through net income. In issuing the standard, the FASB is responding to criticism that today's guidance delays recognition of credit losses. The standard will replace today's "incurred loss" approach with an "expected loss" model. The new model, referred to as the current expected credit loss ("CECL") model, will apply to: (1) financial assets subject to credit losses and measured at amortized cost, and (2) certain off-balance sheet credit exposures. This includes, but is not limited to, loans, leases, held-to-maturity securities, loan commitments, and financial guarantees. The CECL model does not apply to available-for-sale ("AFS") debt securities. For AFS debt securities with unrealized losses, entities will measure credit losses in a manner similar to what they do today, except that the losses will be recognized as allowances rather than reductions in the amortized cost of the securities. As a result, entities will recognize improvements to estimated credit losses immediately in earnings rather than as interest income over time, as they do today. The ASU also simplifies the accounting model for purchased credit-impaired debt securities and loans. ASU 2016-13 also expands the disclosure requirements regarding an entity's assumptions, models, and methods for estimating the allowance for loan and lease losses. In addition, public business entities will need to disclose the amortized cost balance for each class of financial asset by credit quality indicator, disaggregated by the year of origination. ASU No. 2016-13 is effective for interim and annual reporting periods beginning after December 15, 2019 for SEC filers, one year later for non SEC filing public business entities and annual reporting periods beginning after December 15, 2020 for nonpublic business entities and interim periods within the reporting periods beginning after December 15, 2021. Early adoption is permitted for interim and annual reporting periods beginning after December 15, 2018. Entities will apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (i.e., modified retrospective approach). The Bank is currently evaluating the provisions of ASU No. 2016-13 for potential impact on its financial statements.

Note B - Acquisitions

The Bank accounted for the following acquisitions under the acquisition method of accounting. The acquired assets, assumed liabilities and identifiable intangible assets were recorded at their respective acquisition date fair values.

Note B - Acquisitions -Continued

The Bank determined the fair value of the securities, loans, core deposit intangible and deposits with the assistance of third party valuations. The fair value of other real estate owned (“OREO”) was based on appraisals.

The estimated fair value in these acquisitions is subject to refinement as additional information relative to the closing date fair values become available through the measurement period, which can extend for up to one year after the closing date of the transaction. While additional significant changes to the closing date fair values are not expected, any information relative to the changes in these fair values will be evaluated to determine if such changes are due to events and circumstances that existed as of the acquisition date.

Acquisition of Security First Bank

On December 16, 2016, the Bank acquired all the assets and assumed all the liabilities of Security First Bank (“SFB”) in exchange for Bank stock and cash. The Bank issued 1,088,786 shares of Bank common stock with a fair value of \$8.68 per share and cash in the amount of \$8,982,500, for a total transaction value of approximately \$18.4 million. SFB operated one branch in Fresno, California. The Bank acquired SFB as the location and culture fit within the Bank’s strategic plans for expansion.

Goodwill in the amount of \$3.3 million was recognized in this acquisition. Goodwill represents the future economic benefits arising from net assets acquired that are not individually identified and separately recognized and is attributable to synergies expected to be derived from the combination of the two entities. Goodwill is not deductible for income tax purposes.

For loans acquired from SFB, the contractual amounts due, expected cash flows to be collected and fair value as of December 16, 2016 were as follows (dollar amounts in thousands):

	Purchased Credit- Impaired	All Other Acquired Loans
Contractual Amounts Due	\$ 3,294	\$ 91,638
Cash Flows not Expected to be Collected	538	-
Expected Cash Flows	2,756	91,638
Interest Component of Expected Cash Flows	117	15,544
Fair Value of Acquired Loans	<u>\$ 2,639</u>	<u>\$ 76,094</u>

The following table represents the assets acquired and liabilities assumed of SFB as of December 16, 2016 and the fair value adjustments and the amounts recorded by the Bank in 2016 under the acquisition method of accounting (dollar amounts in thousands):

	SFB Book Value	Fair Value Adjustments	Fair Value
ASSETS ACQUIRED			
Cash and Cash Equivalents	\$ 5,541	\$ -	\$ 5,541
Investment Securities	9,428	-	9,428
Loans, Gross	80,401	(1,668)	78,733
Allowance for Loan Losses	(1,719)	1,719	-
Other Bank Stock	1,385	-	1,385
Premises and Equipment	25	-	25
Bank Owned Life Insurance	2,971	-	2,971
Other Real Estate Owned	188	(35)	153
Deferred Tax Assets	2,372	(577)	1,795
Core Deposit Intangible	-	1,214	1,214
Accrued Interest and Other Assets	501	-	501
Total Assets Acquired	<u>\$ 101,093</u>	<u>\$ 653</u>	<u>\$ 101,746</u>
LIABILITIES ASSUMED			
Deposits	\$ 86,206	\$ 16	\$ 86,222
Other Liabilities	426	(10)	416
Total Liabilities Assumed	<u>86,632</u>	<u>6</u>	<u>86,638</u>
Excess of Assets Acquired Over Liabilities Assumed	<u>14,461</u>	<u>647</u>	<u>15,108</u>
Stock and Cash Consideration Recorded as Goodwill on Acquisition			<u>18,433</u> <u>\$(3,325)</u>

Acquisition of Sutter Community Bank

On December 11, 2015, the Bank acquired all the assets and assumed all the liabilities of Sutter Community Bank (“SCB”) in exchange for Bank stock. The Bank issued 1,144,416 shares of Bank common stock with a fair value of \$7.35 per share total transaction value of approximately \$8,411,000. SCB operated one branch in Yuba City, California. The Bank acquired SCB as the location and culture fit within the Bank’s strategic plans for expansion.

A bargain purchase gain totaling \$314,499 resulted from the acquisition and is included as a component of noninterest income in the statements of income.

For loans acquired from SCB, the contractual amounts due, expected cash flows to be collected and fair value as of December 11, 2015 were as follows (dollar amounts in thousands):

	Purchased Credit- Impaired	All Other Acquired Loans
Contractual Amounts Due	\$ 2,554	\$ 60,193
Cash Flows not Expected to be Collected	364	-
Expected Cash Flows	2,190	60,193
Interest Component of Expected Cash Flows	237	15,945
Fair Value of Acquired Loans	<u>\$ 1,953</u>	<u>\$ 44,248</u>

In accordance with generally accepted accounting principles there was no carryover of the allowance for loan losses that had been previously recorded by SFB or SCB.

Notes to Financial Statements

Note B - Acquisitions - Continued

The following table represents the assets acquired and liabilities assumed of SCB as of December 11, 2015 and the fair value adjustments and the amounts recorded by the Bank in 2015 under the acquisition method of accounting (dollar amounts in thousands):

	SCB Book Value	Fair Value Adjustments	Fair Value
ASSETS ACQUIRED			
Cash and Cash Equivalents	\$ 14,490	\$ -	\$ 14,490
Investment Securities	1,906	(81)	1,825
Loans, Gross	47,538	(1,337)	46,201
Allowance for Loan Losses	(1,493)	1,493	-
Other Bank Stock	398	-	398
Premises and Equipment	86	-	86
Bank Owned Life Insurance	2,076	-	2,076
Other Real Estate Owned	1,171	(522)	649
Deferred Tax Assets	1,495	77	1,572
Core Deposit Intangible	-	428	428
Accrued Interest and Other Assets	558	(219)	339
Total Assets Acquired	\$ 68,225	\$(161)	\$ 68,064
LIABILITIES ASSUMED			
Deposits	\$ 58,977	\$ 84	\$ 59,061
Other Liabilities	287	(10)	277
Total Liabilities Assumed	59,264	74	59,338
Excess of Assets Acquired	8,961	(235)	8,726
Over Liabilities Assumed	\$ 68,225	\$(161)	\$ 68,064
Stock Consideration			8,411
Recorded Gain on Acquisition			\$ 315

Note C - Investment Securities

Debt and equity securities have been classified in the statements of financial condition according to management's intent. The amortized cost of securities and their approximate fair values at December 31 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2016				
Available-for-Sale Securities:				
U.S. Government and Agency Securities	\$19,963,727	\$ 810	\$(376,550)	\$19,587,987
Mortgaged-Backed Securities	34,052,938	70,825	(367,969)	33,755,794
Obligations of State and Political Subdivisions	223,283	-	-	223,283
	<u>\$54,239,948</u>	<u>\$ 71,635</u>	<u>\$(744,519)</u>	<u>\$53,567,064</u>
December 31, 2015				
Available-for-Sale Securities:				
U.S. Government and Agency Securities	\$27,505,350	\$ 15,261	\$(76,102)	\$27,444,509
Mortgaged-Backed Securities	26,978,253	116,815	(196,628)	26,898,440
	<u>\$54,483,603</u>	<u>\$ 132,076</u>	<u>\$(272,730)</u>	<u>\$54,342,949</u>

The amortized cost and estimated fair value of all investment securities as of December 31, 2016 by expected maturities are shown below. 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.

Available-for-Sale Securities

	Amortized Cost	Fair Value
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Due within One Year	\$ 3,501,823	\$ 3,499,622
Due from One Year to Five Years	17,512,654	17,160,646
Due from Five to Ten Years	29,371,547	29,135,294
Due after Ten Years	3,853,924	3,771,502
	<u>\$54,239,948</u>	<u>\$53,567,064</u>

No securities were sold during 2016 and 2015.

The gross unrealized loss and related estimated fair value of investment securities that have been in a continuous loss position for less than twelve months and over twelve months at December 31, 2016 and 2015, are as follows:

	Less than Twelve Months		Over Twelve Months		Total	
	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value
December 31, 2016						
U.S. Government and Agency Securities	\$(374,985)	\$18,088,742	\$(1,565)	\$ 498,435	\$(376,550)	\$18,587,177
Mortgaged-Backed Securities	(367,969)	21,629,266	-	-	(367,969)	21,629,266
	<u>\$(742,954)</u>	<u>\$39,718,008</u>	<u>\$(1,565)</u>	<u>\$ 498,435</u>	<u>\$(744,519)</u>	<u>\$40,216,443</u>
December 31, 2015						
U.S. Government and Agency Securities	\$(64,634)	\$13,176,698	\$(11,468)	\$1,488,330	\$(76,102)	\$14,665,028
Mortgaged-Backed Securities	(196,628)	20,970,132	-	-	(196,628)	20,970,132
	<u>\$(261,262)</u>	<u>\$34,146,830</u>	<u>\$(11,468)</u>	<u>\$1,488,330</u>	<u>\$(272,730)</u>	<u>\$35,635,160</u>

As of December 31, 2016, the Bank has one U.S. government agency security that has been in an unrealized loss position over 12 months. The unrealized loss on this investment security has not been recognized into income as management does not intend to sell, and it is not "more likely than not" that management would be required to sell the security prior to its anticipated recovery, and the decline in fair value is largely due to change in interest rates. The fair value is expected to recover as the bond approaches maturity.

Securities with a fair value of approximately \$3.5 million were pledged to the Federal Home Loan Bank as discussed in Note G.

Note D - Loans

The Bank's loan portfolio consists primarily of loans to borrowers within the Central Valleys of California. Although the Bank seeks to avoid concentrations of loans to a single industry or based upon a single class of collateral, real estate and real estate associated businesses are among the principal industries in the Bank's market area and, as a result, the Bank's loan and collateral portfolios are, to some degree, concentrated in those industries.

Notes to Financial Statements

Note D - Loans -Continued

A summary of the changes in the allowance for loan losses as of December 31 follows:

	2016	2015
Balance at Beginning of Year	\$ 2,245,566	\$ 1,723,391
Additions to the Allowance Charged to Expense	235,000	522,275
Recoveries on Loans Charged-Off	15,597	-
	<u>2,496,163</u>	<u>2,245,666</u>
Less Loans Charged-Off	-	(100)
	<u>\$ 2,496,163</u>	<u>\$ 2,245,566</u>

The following table presents the activity in the allowance for loan losses for the year 2016 and 2015 and the recorded investment in loans and impairment method as of December 31, 2016 and 2015 by portfolio segment:

	Real Estate - Other	Construction and Land Development	Commercial and Industrial	Consumer	Total
December 31, 2016					
Allowance for Loan Losses:					
Beginning of Year	\$ 1,521,184	\$ 47,137	\$ 612,905	\$ 64,340	\$ 2,245,566
Provisions	225,011	15,458	22,230	(27,699)	235,000
Charge-offs	-	-	-	-	-
Recoveries	-	-	15,597	-	15,597
	<u>\$ 1,746,195</u>	<u>\$ 62,595</u>	<u>\$ 650,732</u>	<u>\$ 36,641</u>	<u>\$ 2,496,163</u>
End of Year Reserves:					
Specific	-	-	-	-	-
General	1,746,195	62,595	650,732	36,641	2,496,163
Purchased Credit Impaired Loans	-	-	-	-	-
	<u>\$ 1,746,195</u>	<u>\$ 62,595</u>	<u>\$ 650,732</u>	<u>\$ 36,641</u>	<u>\$ 2,496,163</u>
Loans Evaluated for Impairment:					
Individually	\$ 1,039,740	\$ -	\$ 40,256	\$ 10,318	\$ 1,090,314
Collectively	224,115,715	14,276,680	63,727,194	342,563	302,462,152
Purchased Credit Impaired Loans	4,073,672	-	111,433	-	4,185,105
	<u>\$ 229,229,127</u>	<u>\$ 14,276,680</u>	<u>\$ 63,878,883</u>	<u>\$ 352,881</u>	<u>\$ 307,737,571</u>
December 31, 2015					
Allowance for Loan Losses:					
Beginning of Year	\$ 1,167,486	\$ 48,676	\$ 474,196	\$ 33,033	\$ 1,723,391
Provisions	353,698	(1,539)	138,809	31,307	522,275
Charge-offs	-	-	(100)	-	(100)
Recoveries	-	-	-	-	-
	<u>\$ 1,521,184</u>	<u>\$ 47,137</u>	<u>\$ 612,905</u>	<u>\$ 64,340</u>	<u>\$ 2,245,566</u>
End of Year Reserves:					
Specific	-	-	-	-	-
General	1,521,184	47,137	612,905	64,340	2,245,566
Purchased Credit Impaired Loans	-	-	-	-	-
	<u>\$ 1,521,184</u>	<u>\$ 47,137</u>	<u>\$ 612,905</u>	<u>\$ 64,340</u>	<u>\$ 2,245,566</u>
Loans Evaluated for Impairment:					
Individually	\$ 3,313,570	\$ 241,563	\$ 83,534	\$ 4,541	\$ 3,643,208
Collectively	158,612,919	4,704,182	39,350,625	802,538	203,470,264
Purchased Credit Impaired Loans	1,627,505	-	96,591	-	1,724,096
	<u>\$ 163,553,994</u>	<u>\$ 4,945,745</u>	<u>\$ 39,530,750</u>	<u>\$ 807,079</u>	<u>\$ 208,837,568</u>

The Bank 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, collateral adequacy, credit documentation, and current economic trends, among other factors. The Bank analyzes loans individually by classifying the loans as to credit risk. This analysis typically includes larger, non-homogeneous loans such as commercial real estate and commercial and industrial loans. This analysis is performed on an ongoing basis as new information is obtained. The Bank uses the following definitions for risk ratings:

Pass - Loans classified as pass include loans not meeting the risk ratings defined below.

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 institution'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.

Impaired - A loan is considered impaired, when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Additionally, all loans classified as troubled debt restructurings are considered impaired.

The risk category of loans by class of loans was as follows as of December 31, 2016:

The risk category of loans by class of loans was as follows as of December 31, 2015:

	Special				Total
	Pass	Mention	Substandard	Impaired	
December 31, 2016					
Real Estate Other:					
Commercial	\$ 109,194,259	\$ 1,024,221	\$ 7,036,696	\$ 1,039,740	\$ 118,294,916
Farmland	55,832,554	-	-	-	55,832,554
1-4 Family Residential	38,218,578	-	536,340	-	38,754,918
Multifamily Residential	16,346,739	-	-	-	16,346,739
Construction and Land Development	14,123,109	127,446	26,125	-	14,276,680
Commercial and Industrial	63,227,310	348,271	263,046	40,256	63,878,883
Consumer	342,563	-	-	10,318	352,881
	<u>\$ 297,285,112</u>	<u>\$ 1,499,938</u>	<u>\$ 7,862,207</u>	<u>\$ 1,090,314</u>	<u>\$ 307,737,571</u>

Past due and nonaccrual loans presented by loan class were as follows as of December 31, 2016 and 2015:

	Special				Total
	Pass	Mention	Substandard	Impaired	
December 31, 2015					
Real Estate Other:					
Commercial	\$ 63,087,928	\$ 432,121	\$ 2,002,513	\$ 3,313,570	\$ 68,836,132
Farmland	57,045,546	-	-	-	57,045,546
1-4 Family Residential	26,575,768	-	619,303	-	27,195,071
Multifamily Residential	10,477,245	-	-	-	10,477,245
Construction and Land Development	4,661,388	-	42,794	241,563	4,945,745
Commercial and Industrial	39,324,577	10,456	112,183	83,534	39,530,750
Consumer	802,538	-	-	4,541	807,079
	<u>\$ 201,974,990</u>	<u>\$ 442,577</u>	<u>\$ 2,776,793</u>	<u>\$ 3,643,208</u>	<u>\$ 208,837,568</u>

	Still Accruing			
	30-59 Days Past Due	60-89 Days Past Due	Over 90 Days Past Due	Nonaccrual
	December 31, 2016			
Real Estate Other:				
Commercial	\$ -	\$ 749,934	\$ -	\$ 1,039,740
Farmland	-	-	-	-
1-4 Family Residential	-	-	-	-
Multifamily Residential	-	-	-	-
Construction and Land Development	-	185,958	-	-
Commercial and Industrial	10,000	-	-	40,256
Consumer	-	33,494	-	10,318
	<u>\$ 10,000</u>	<u>\$ 969,386</u>	<u>\$ -</u>	<u>\$ 1,090,314</u>
December 31, 2015				
Real Estate Other:				
Commercial	\$ -	\$ -	\$ -	\$ 2,566,890
Farmland	-	-	-	-
1-4 Family Residential	-	-	-	33,201
Multifamily Residential	-	-	-	-
Construction and Land Development	-	-	-	241,563
Commercial and Industrial	39,125	-	-	185,896
Consumer	-	-	-	4,541
	<u>\$ 39,125</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,032,091</u>

Note D - Loans -Continued

Information relating to individually impaired loans presented by class of loans was as follows as of December 31, 2016 and 2015:

	Impaired Loans					Average Recorded Investment	Interest Income Recognized
	Unpaid Principal Balance	Recorded Investment	Without Specific Allowance	With Specific Allowance	Related Allowance		
December 31, 2016							
Real Estate Other:							
Commercial	\$2,040,093	\$1,039,740	\$1,039,740	\$ -	\$ -	\$1,125,531	\$ -
Farmland	-	-	-	-	-	-	-
1-4 Family Residential	-	-	-	-	-	-	-
Multifamily Residential	-	-	-	-	-	-	-
Construction and Land Development	-	-	-	-	-	-	-
Commercial and Industrial	50,602	40,256	40,256	-	-	22,932	-
Consumer	10,651	10,318	10,318	-	-	2,880	-
	<u>\$2,101,346</u>	<u>\$1,090,314</u>	<u>\$1,090,314</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$1,151,343</u>	<u>\$ -</u>
December 31, 2015							
Real Estate Other:							
Commercial	\$3,910,827	\$3,313,570	\$3,313,570	\$ -	\$ -	\$2,059,000	\$138,708
Farmland	-	-	-	-	-	-	-
1-4 Family Residential	-	-	-	-	-	-	-
Multifamily Residential	-	-	-	-	-	-	-
Construction and Land Development	331,898	241,563	241,563	-	-	20,000	-
Commercial and Industrial	141,960	83,534	83,534	-	-	7,000	-
Consumer	6,470	4,541	4,541	-	-	500	-
	<u>\$4,391,155</u>	<u>\$3,643,208</u>	<u>\$3,643,208</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$2,086,500</u>	<u>\$138,708</u>

The outstanding balance and carrying amount of purchased credit impaired loans as of December 31, 2016 were as follows:

	2016	2015
Outstanding Balance	\$ 5,841,817	\$ 2,511,906
Carrying Amount	\$ 4,185,105	\$ 1,724,096

The change in accretible discount on purchased credit impaired loans during the period was as follows:

	2016	2015
Balance at January 1	\$ 21,637	\$ -
New Loans Purchased	43,556	236,707
Accretion of Income	-	-
Reversals (Sales and Foreclosures)	-	-
Restructuring as TDR	-	-
Transfer to Nonaccretible Discount	-	(215,070)
Balance at December 31	<u>\$ 65,193</u>	<u>\$ 21,637</u>

Income is not recognized on certain purchased loans if the Bank cannot reasonably estimate cash flows expected to be collected. The carrying amount of such loans was \$3.8 million and \$1.3 million at December 31, 2016 and 2015, respectively.

Note E - Premises and Equipment

A summary of premises and equipment as of December 31 follows:

	2016	2015
Land	\$ 600,000	\$ 600,000
Building	1,317,529	1,317,517
Leasehold Improvements	1,398,649	1,362,552
Furniture, Fixtures, and Equipment	1,285,554	1,262,844
Construction in Progress	<u>1,722,704</u>	<u>7,550</u>
	6,324,436	4,550,463
Less Accumulated Depreciation and Amortization	<u>(2,106,076)</u>	<u>(1,772,435)</u>
	<u>\$ 4,218,360</u>	<u>\$ 2,778,028</u>

The Bank has operating leases for branches that will expire at various dates through June 2035. The leases include provisions for periodic rent increases as well as payment by the lessee of certain operating expenses. The leases also include provisions for options to extend the lease. The rental expense relating to the leases and other short term rentals was approximately \$429,000 and \$344,000 for the years ended December 31, 2016 and 2015, respectively.

At December 31, 2016, the future lease rental payable under noncancellable operating lease commitments for the branches was as follows:

2017	\$ 410,906
2018	370,088
2019	338,351
2020	345,624
2021	174,842
Thereafter	<u>1,826,878</u>
	<u>\$ 3,466,689</u>

The minimum rental payments shown above are given for the existing lease obligations and are not a forecast of future rental expense.

Note F - Deposits

At December 31, 2016, the scheduled maturities of time deposits are as follows:

2017	\$ 72,829,859
2018	3,044,313
2019	1,600,234
2020	292,439
2021	<u>6,604,443</u>
	<u>\$ 84,371,288</u>

Note G - Other Borrowings

The Bank may borrow up to \$22.5 million overnight on an unsecured basis from its correspondent banks. As of December 31, 2016, the Bank has no amounts outstanding under these arrangements.

In addition, the Bank is also a member of the Federal Home Loan Bank ("FHLB") and has arranged a secured borrowing line with that institution, secured by the assets of the Bank. Under this line, the Bank may borrow up to approximately \$95.7 million subject to providing adequate collateral and continued compliance with the Advances and Security Agreement and other eligibility requirements established by the FHLB.

Note G - Other Borrowings - Continued

The Bank has pledged \$3.5 million of investment securities and \$215.1 million of loans as collateral for this line. As of December 31, 2016 the Bank had a \$22.0 million outstanding Letter of Credit under this arrangement to secure public monies.

Note H - Other Expenses

Other expenses as of December 31 are comprised of the following:

	2016	2015
Professional Fees	\$ 1,501,888	\$ 817,560
Data Processing	858,393	533,983
Office Expenses	248,945	213,832
Marketing and Business Promotion	397,390	170,806
Insurance	75,249	47,533
Regulatory Assessments	200,689	150,418
Other Expenses	448,042	248,491
	<u>\$ 3,730,596</u>	<u>\$ 2,182,623</u>

Note I - Income Taxes

The provision (benefit) for income taxes for the years ended December 31, consists of the following:

	2016	2015
Current:		
Federal	\$ 1,246,518	\$ 296,019
State	377,182	101,042
	<u>1,623,700</u>	<u>397,061</u>
Deferred	(196,000)	332,000
	<u>\$ 1,427,700</u>	<u>\$ 729,061</u>

The Bank is subject to federal income tax and franchise tax of the state of California. Income tax returns for the years ending after December 31, 2012 are open to audit by the federal authorities and income tax returns for the years ending after December 31, 2011 are open to audit by state authorities. The Bank does not expect the total amount of unrecognized tax benefits to significantly increase or decrease within the next twelve months.

As of December 31, 2016, the Bank has net operating loss carryforwards of approximately \$4,000,000 and \$7,318,000 for Federal and California franchise tax purposes, respectively. The use of the net operating loss carry forwards is limited by Section 382 of the Internal Revenue Service Code and ranges from \$219,000 per year to \$321,000 per year. California net operating loss carryforwards, to the extent not used will begin to expire in 2028.

A comparison of the federal statutory income tax rates to the Bank's effective income tax rates follows:

	2016		2015	
	Amount	Rate	Amount	Rate
Statutory Federal Tax	\$ 1,075,000	34.0%	\$ 557,000	34.0%
State Tax, Net of Federal Benefit	238,000	7.5%	117,000	7.1%
Stock-based Compensation	9,000	0.3%	30,000	1.8%
Merger Expenses	57,000	1.8%	70,000	4.3%
Bargain Purchase Gain	-	-	(107,000)	(6.5%)
Other Items, Net	48,700	1.5%	62,061	3.8%
Actual Tax Expense (Benefit)	<u>\$ 1,427,700</u>	<u>45.1%</u>	<u>\$ 729,061</u>	<u>44.5%</u>

Deferred taxes are a result of differences between income tax accounting and generally accepted accounting principles with respect to income and expense recognition. The following is a summary of the components of the net deferred tax asset accounts recognized in the accompanying statement of financial condition at December 31:

	2016	2015
Deferred Tax Assets:		
Pre-Opening Expenses	\$ 416,000	\$ 432,000
Allowance for Loan Losses Due to Tax Limitations	326,000	756,000
Depreciation Differences	332,000	252,000
Other Real Estate Owned Differences	787,000	713,000
Operating Loss Carryforwards	1,884,000	149,000
Unrealized Loss on Available-for-Sale Securities	276,000	58,000
Stock-Based Compensation	409,000	352,000
Nonaccrual Differences	389,000	240,000
Purchase Accounting Adjustments	651,000	469,000
Other Assets and Liabilities	550,000	270,000
	<u>6,020,000</u>	<u>3,691,000</u>
Deferred Tax Liabilities:		
Other Assets and Liabilities	(359,000)	(184,000)
	<u>(359,000)</u>	<u>(184,000)</u>
	<u>\$ 5,661,000</u>	<u>\$ 3,507,000</u>

Note J - Related Party Transactions

In the ordinary course of business, the Bank has granted loans to certain directors and the companies with which they are associated. The total outstanding principal and commitment of these loans at December 31, 2016 and 2015 was approximately \$5,441,000 and \$5,383,000, respectively.

Also, in the ordinary course of business, certain executive officers, directors and companies with which they are associated have deposits with the Bank. The balances of these deposits at December 31, 2016 and 2015 amounted to approximately \$22.9 million and \$26.5 million, respectively.

Note K - Commitments

In the ordinary course of business, the Bank enters into financial commitments to meet the financing needs of its customers. Those instruments involve to varying degrees, elements of credit and interest rate risk not recognized in the Bank's financial statements.

Note K - Commitments - Continued

The Bank's exposure to loan loss in the event of nonperformance on commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments as it does for loans reflected in the financial statements.

As of December 31, 2016 and 2015, the Bank had the following outstanding financial commitments whose contractual amount represents credit risk:

	<u>2016</u>	<u>2015</u>
Commitments to Extend Credit	<u>\$ 47,009,000</u>	<u>\$ 33,130,000</u>

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. Since many of the commitments are expected to expire without being drawn upon, the total amounts do not necessarily represent future cash requirements. The Bank evaluates each client's credit worthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Bank is based on management's credit evaluation of the customer. The majority of the Bank's commitments to extend credit and standby letters of credit are secured by real estate or cash, respectively.

The Bank is involved in various litigation, which has arisen in the ordinary course of its business. In the opinion of management, the disposition of such pending litigation will not have material effect on the Bank's financial statements.

Note L - Stock-Based Compensation Plans

The Bank's 2007 Stock Option Plan was approved by its shareholders in July 2008. Under the terms of the 2007 Stock Option Plan, officers and key employees may be granted both nonqualified and incentive stock options and directors and organizers, who are not also an officer or employee, may only be granted nonqualified stock options. This plan was replaced by the 2013 Omnibus Stock Incentive Plan.

The Bank's 2013 Omnibus Stock Incentive Plan ("2013 Plan") was approved by its shareholders in May 2013. Under the terms of the 2013 Plan, officers and key employees may be granted both nonqualified and incentive stock options and directors and other consultants, who are not also an officer or employee, may only be granted nonqualified stock options. The 2013 Plan also permits the grant of stock appreciation rights ("SARs"), restricted shares, deferred shares, performance shares and performance unit awards. The 2013 Plan provides for the total number of awards of common stock

that may be issued over the term of the plan not to exceed 573,533 shares, of which a maximum of 400,000 shares may be granted as incentive stock options. The aggregated number of awards that may be granted to an individual participant may not exceed 100,000 shares per year. Stock options and performance share and unit awards are granted at a price not less than 100% of the fair market value of the stock on the date of grant. The 2013 plan provides for accelerated vesting if there is a change of control as defined in the 2013 Plan. Equity awards generally vest over three to five years. Stock options expire no later than ten years from the date of grant.

The Bank recognized stock-based compensation cost of \$283,000 and \$185,000 for the periods ended December 31, 2016 and 2015. The Bank also recognized income tax benefits related to stock-based compensation of \$105,000 in 2016 and \$40,000 in 2015.

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option pricing model with the weighted-average assumptions presented below:

	<u>2016</u>	<u>2015</u>
Expected Volatility	36.00%	43.28%
Expected Term	6.25 Years	6.04 Years
Expected Dividends	None	None
Risk Free Rate	1.25%	1.23%
Grant Date Fair Value	\$ 2.80	\$ 3.00

Since the Bank has a limited amount of historical stock activity the expected volatility is based on the historical volatility of similar banks that have a longer trading history. The expected term represents the estimated average period of time that the options remain outstanding. Since the Bank does not have sufficient historical data on the exercise of stock options, the expected terms is based on the "simplified" method that measures the expected term as the average of the vesting period and the contractual term. The risk free rate of return reflects the grant date interest rate offered for a comparable U.S. Treasury bonds over the expected term of the options.

A summary of the status of the Bank's stock options as of December 31, 2016 and changes during the year ended thereon is presented below:

	<u>Shares</u>	<u>Weighted-Average Exercise Price</u>	<u>Weighted-Average Remaining Contractual Term</u>	<u>Aggregate Intrinsic Value</u>
Outstanding at Beginning of Year	409,730	\$ 8.59		
Cancelled	-	\$ -		
Granted	5,000	\$ 7.50		
Exercised	(23,000)	\$ 6.31		
Forfeited	(32,000)	\$ 9.81		
Outstanding at End of Year	<u>359,730</u>	<u>\$ 8.61</u>	<u>4.66 Years</u>	<u>\$ 680,965</u>
Options Exercisable	<u>256,730</u>	<u>\$ 9.24</u>	<u>3.10 Years</u>	<u>\$ 324,715</u>

Note L - Stock-Based Compensation Plans - Continued

As of December 31, 2016, there was approximately \$204,000 of total unrecognized compensation cost related to the outstanding stock options that will be recognized over a weighted-average period of 1.76 years.

During 2015 the Bank cancelled 90,000 options with a weighted-average exercise price of \$10.00 held by directors and granted 90,000 options that expire in ten years and vest over three years. This is treated as a modification and the incremental increase in the fair value was \$1.83 per option. Additional compensation expense of \$55,000 and \$14,000 was recognized in 2016 and 2015, respectively, as a result of the modification.

A summary of the status of the Bank's deferred share awards as of December 31, 2016 and changes during the year ended thereon is presented below:

	Shares	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2016	18,408	\$ 7.00
New Deferred Share Awards	48,931	\$ 8.04
Shares Vested and Issued	(19,330)	\$ 7.03
Shares Forfeited	(78)	\$ 7.00
Nonvested at December 31, 2016	47,931	\$ 8.05

As of December 31, 2016 there was approximately \$293,000 of unrecognized compensation cost related to the restricted stock grants that will be recognized over a weighted-average period of 3.4 years. The fair value of shares issued in 2016 and 2015 was approximately \$138,000 and \$111,000, respectively.

Note M - Earnings Per Share ("EPS")

The following is a reconciliation of net income and shares outstanding to the income and number of shares used to compute EPS:

	2016		2015	
	Income	Shares	Income	Shares
Net Income as Reported	\$ 1,732,944		\$ 908,654	
Shares Outstanding at Year-End		6,979,497		4,999,895
Impact of Weighting Shares Issued During the Year		(1,873,829)		(1,304,389)
Used in Basic EPS	1,732,944	5,105,669	908,654	3,695,506
Dilutive Effect of Outstanding Deferred Shares		12,118		12,252
Used in Dilutive EPS	\$ 1,732,944	5,117,787	\$ 908,654	3,707,758

As of December 31, 2016 and 2015 there were 359,730 and 385,730, respectively, stock options that could potentially dilute earnings per share in the future that were not included in the computation of diluted earnings per shares because to do so would have been antidilutive.

Note N - Fair Value Measurement

The following is a description of valuation methodologies used for assets and liabilities recorded at fair value:

Securities

The fair values of securities available for sale are determined by matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2).

Other Real Estate Owned

Nonrecurring adjustments to certain commercial and residential real estate properties classified as other real estate owned ("OREO") are measured at the lower of carrying amount or fair value, less costs to sell. Fair values are generally based on third party appraisals or broker opinions, which are frequently adjusted by management to reflect current conditions and estimated selling costs, resulting in a Level 3 classification. In cases where the carrying amount exceeds the fair value, less costs to sell, an impairment loss is recognized.

Appraisals for other real estate owned are performed by certified general appraisers whose qualifications and licenses have been reviewed and verified by the Bank. Once received, a member of the loan department reviews the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value. The Bank also determines what additional adjustments, if any, should be made to the appraisal values on any remaining other real estate owned to arrive at fair value. No significant adjustments to appraised values have been made as a result of this process as of December 31, 2016.

The following table provides the hierarchy and fair value for each major category of assets and liabilities measured at fair value at December 31:

	Fair Value Measurements Using:			Total	Total Losses
	Level 1	Level 2	Level 3		
December 31, 2016					
Assets measured at fair value on a recurring basis					
Securities Available for Sale	\$ -	\$53,567,064	\$ -	\$53,567,064	\$ -
Assets Measured at Fair Value on a Non-recurring Basis					
Other Real Estate Owned, Net	\$ -	\$ -	\$ 788,842	\$ 788,842	\$ -
December 31, 2015					
Assets measured at fair value on a recurring basis					
Securities Available for Sale	\$ -	\$54,342,949	\$ -	\$54,342,949	\$ -
Assets Measured at Fair Value on a Non-recurring Basis					
Other Real Estate Owned, Net	\$ -	\$ -	\$ 649,092	\$ 649,092	\$ -

Quantitative information about the Bank's nonrecurring Level 3 fair value measurements as of December 31 is as follows:

	Fair Value Amount	Valuation Technique	Unobservable Input		Range
December 31, 2016					
Other Real Estate Owned	\$ 788,842	Third Party Appraisals	Liquidation and Selling Costs	8% to 50%	
December 31, 2015					
Other Real Estate Owned	\$ 649,092	Third Party Appraisals	Liquidation and Selling Costs	8% to 50%	

Note O - Fair Value of Financial Instruments

The fair value of a financial instrument is the amount at which the asset or obligation could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Fair value estimates are made at a specific point in time based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the entire holdings of a particular financial instrument. Because no market value exists for a significant portion of the financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature, involve uncertainties and matters of judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on financial instruments both on and off the balance sheet without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Additionally, tax consequences related to the realization of the unrealized gains and losses can have a potential effect on fair value estimates and have not been considered in many of the estimates.

The following methods and assumptions were used to estimate the fair value of significant financial instruments not previously presented:

Cash and Cash Equivalents

The carrying amounts reported in the balance sheet for cash and cash equivalents approximate the fair values of those assets due to the short-term nature of the assets.

Loans

For variable rate loans that re-price frequently and with no significant change in credit risk, fair values are based on carrying amounts. The fair values for all other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers with similar credit quality.

Federal Home Loan Bank Stock and Other Bank Stock

The fair value of Federal Home Loan Bank Stock and other Bank stock is not readily determinable due to the lack of its transferability.

Noninterest-Bearing and Interest Bearing Demand Deposits

The fair values for noninterest-bearing deposits and interest-bearing demand deposits are equal to the amount payable on demand at the reporting date, which is the carrying amount.

Interest-Bearing Time Deposits

The fair values for fixed rate certificates of deposits are estimated using a cash flow analysis, discounted at interest rates being offered at each reporting date by the Bank for certificates with similar remaining maturities.

Off-Balance Sheet Financial Instruments

The fair value of commitments to extend credit and standby letters of credit is estimated using the fees currently charged to enter into similar agreements. The fair value of these financial instruments is not material.

The fair value hierarchy level and estimated fair value of significant financial instruments at December 31, 2016 and 2015 are summarized as follows (dollar amounts in thousands):

Fair Value Hierarchy	2016		2015		
	Carrying Value	Fair Value	Carrying Value	Fair Value	
Financial Assets:					
Cash and Cash Equivalents	Level 1	\$ 62,547	\$ 62,547	\$ 24,062	\$ 24,062
Investment Securities	Level 2	53,567	53,567	54,343	54,343
Loans, net	Level 2	305,022	303,888	206,133	205,266
FHLB and Other Bank Stock		3,153	N/A	1,466	N/A
Financial Liabilities:					
Noninterest-Bearing and Interest-Bearing					
Demand Deposits	Level 1	304,615	304,615	198,658	198,658
Interest-Bearing Time Deposits	Level 2	84,371	84,134	58,019	57,918

The Bank adopted a 401(k) Plan for its employees in 2008. Under the plan, eligible employees may defer a portion of their salaries. The plan also provides for a non-elective discretionary contribution by the Bank. The Bank made \$42,000 in contributions for 2016 and no contributions for 2015.

Note P - Employee Benefit Plan

The Bank adopted a 401(k) Plan for its employees in 2008. Under the plan, eligible employees may defer a portion of their salaries. The plan also provides for a non-elective discretionary contribution by the Bank. The Bank made \$42,000 in contributions for 2016 and no contributions for 2015.

Note Q - Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory - and possibly additional discretionary - actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

In July, 2013, the federal bank regulatory agencies approved the final rules implementing the Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules). The new rules, Basel III, became effective on January 1, 2015, with certain of the requirements phased-in over a multi-year schedule, and fully phased in by January 1, 2019. Under the Basel III rules, the Bank 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% in 2015 to 2.5% by 2019. The capital conservation buffer for 2016 is 0.625%. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total, Tier 1 and CET1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2016 and 2015, that the Bank meets all capital adequacy requirements.

As of December 31, 2016, the most recent notification from the FDIC 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 Bank's category). To be categorized as well capitalized, the Bank must maintain minimum ratios as set forth in the table below.

The following table also sets forth the Bank's actual capital amounts and ratios (dollar amounts in thousands):

	Amount of Capital Required					
	Actual		For Capital Adequacy Purposes		To Be Well-Capitalized Under Prompt Corrective Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2016:						
Total Capital (to Risk-Weighted Assets)	\$54,599	14.5%	\$30,074	8.0%	\$37,592	10.0%
Tier 1 Capital (to Risk-Weighted Assets)	\$52,095	13.9%	\$22,555	6.0%	\$30,074	8.0%
CET1 Capital (to Risk-Weighted Assets)	\$52,095	13.9%	\$16,917	4.5%	\$24,435	6.5%
Tier 1 Capital (to Average Assets)	\$52,095	11.7%	\$17,811	4.0%	\$22,264	5.0%
As of December 31, 2015:						
Total Capital (to Risk-Weighted Assets)	\$41,357	17.0%	\$19,464	8.0%	\$24,330	10.0%
Tier 1 Capital (to Risk-Weighted Assets)	\$39,103	16.1%	\$14,598	6.0%	\$19,464	8.0%
CET1 Capital (to Risk-Weighted Assets)	\$39,103	16.1%	\$10,949	4.5%	\$15,815	6.5%
Tier 1 Capital (to Average Assets)	\$39,103	13.2%	\$11,882	4.0%	\$14,852	5.0%

The California Financial Code provides that a bank may not make a cash distribution to its shareholders in excess of the lesser of the bank's undivided profits or the bank's net income for its last three fiscal years less the amount of any distribution made to the bank's shareholders during the same period.

FRESNO BRANCH

663 West Nees Ave.
(559) 225-1700

KINGSBURG BRANCH

1580 Draper St.
(559) 802-1070

PORTERVILLE BRANCH

65 West Olive Ave.
(559) 306-1300

VISALIA BRANCH

501 West Main St.
(559) 802-1000

YUBA CITY BRANCH

700 Plumas St.
(530) 674-8900

www.suncrestbank.com