2019 FINANCIAL STATEMENTS

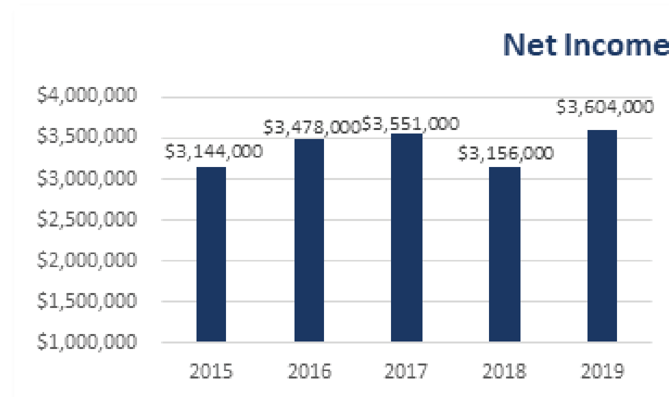
MISSION
VALLEY
BANCORP

To our Shareholders, Clients & Friends,

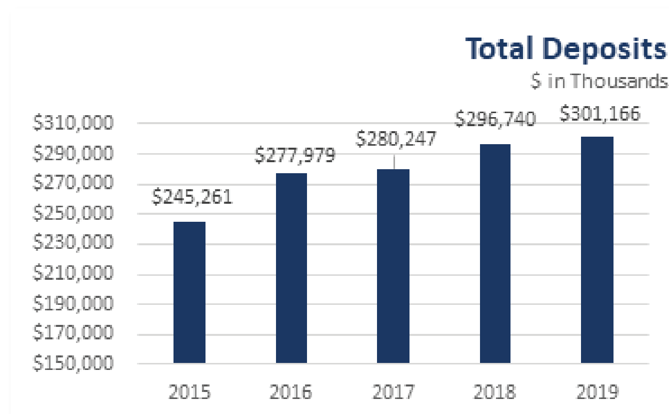
On behalf of Mission Valley's Management Team and the Board of Directors, we are pleased to report that 2019 proved to be the most profitable year in the history of our organization. Net earnings for the year ended December 31, 2019 surpassed $3.6 million, or $1.12 per diluted share, compared to $3.2 million, or $0.98 per diluted share for the year ended December 31, 2018.

2019 Performance Highlights:

- Net Income surpassed $3.6 million for the year ended December 31, 2019 compared to $3.2 million for the year ended December 31, 2018.
- Total assets rose to $357.8 million at December 31, 2019 from $351.2 million at December 31, 2018.
- Total deposits closed 2019 at $301.2 million up from $296.7 million reported at December 31, 2018.
- Total interest income surpassed $15.9 million for the year ended December 31, 2019 as compared to $15.4 million for the year ended December 31, 2018.
- Gross Loans increased to $266.3 million at December 31, 2019 as compared to $248.2 million at December 31, 2018.
- Mission Valley Bancorp issued its fourth cash dividend in February of 2019 – $0.10 per common share.
- $3.6 million of debt at the holding company level was repaid during 2019, resulting in lower interest costs in excess of $190,000 annually.



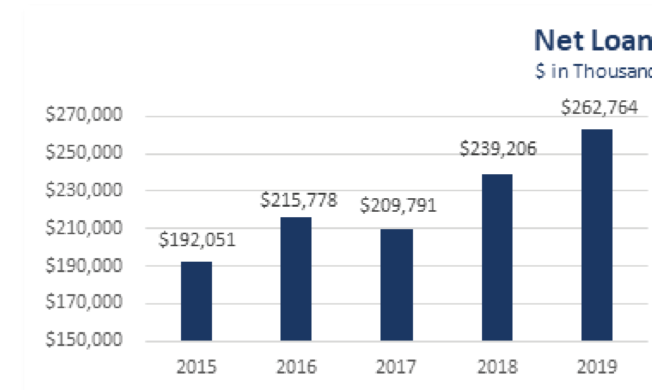
2019 opened with Federal Reserve interest rates ranging from 2.25 to 2.50 percent and the financial industry anticipating (and planning for) as many as three additional rate hikes through 2019. However, early in the year it became evident that the central bank had changed course. Responding to slower global growth and trade uncertainties, the Federal Reserve left rates unchanged until late July when the first of three rate decreases took place, ending the year with the Federal Reserve interest rate range between 1.50 and 1.75 percent. Despite these unexpected turns, loan demand remained steady. Net loans grew to $262.8 million, up $23.6 million at December 31, 2019, a 9.85% increase from the $239.2 million reported at December 31, 2018. Loan quality remained strong with non-accrual loans totaling $530 thousand or 0.20% of total loans, with no Other Real Estate Owned as of December 31, 2019.



Total deposits held steady over the course of the year, up 1.49% to $301.2 million at December 31, 2019, as compared to $296.7 at December 31, 2018. Total interest income rose 3.41% to $15.94 million for the year ended December 31, 2019 from $15.42 million in 2018. Total interest expense increased 5.00%, to $1.22 million for the year ended December 31, 2019 as compared to $1.16 million for the year ended December 31, 2018, resulting in net interest income rising 3.28% to $14.72 million in 2019, from $14.26 million in 2018.

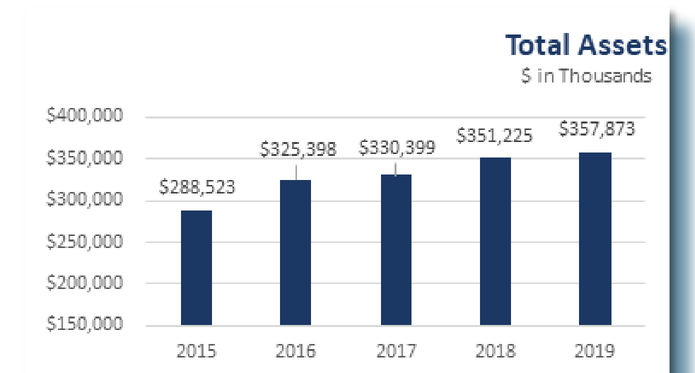
Evidence of the impact of the Bank's continued focus on the growth and diversification of our core, top line revenue sources is non-interest income showing an increase of more than 56.0%, reaching $4.19 million for the year ended December 31, 2019, as compared to $2.68 million for the year ended December 31, 2018.

As we continue through 2020 – both our balance sheet and capital position are strong. For the year ended December 31, 2019, both Mission Valley Bancorp and Mission Valley Bank's capital ratios continue to exceed regulatory requirements with Mission Valley Bancorp reporting a Total Leverage ratio of 12.1%, Common Equity Tier 1 Capital ratio of 12.8%, Tier 1 Capital ratio of 14.8% and a Total Capital ratio of 16.0%. Mission Valley Bank reported a Total Leverage ratio of 11.74%, Common Equity Tier 1 Capital ratio of 14.27%, Tier 1 Capital ratio of 14.27% and a Total Capital ratio of 15.52%. Regulatory requirements for a "Well Capitalized" bank are 5%, 6.5%, 8% and 10%, respectively.



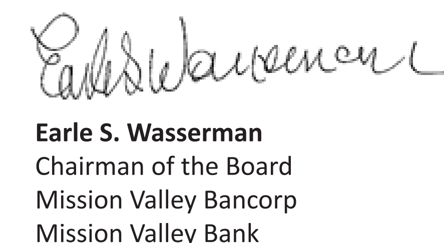
At Mission Valley, we are proud of the work we do for our clients and our shareholders. We are equally proud of the contributions we make to the communities we serve. Throughout 2019, our contributions and performance continued to be recognized by a number of organizations. In August, Rachel Carrillo (Credit Administration Assistant at our Santa Clarita office) was the ninth consecutive Mission Valley Banker to be honored by the San Fernando Valley Business Journal among the 2019 Valley's Most Trusted Advisors – Business Banking. Additionally, The American Banker Newspaper ranked Mission Valley among the Top 200 Banks & Thrifts in the Nation, while Bauer Financial, Veribanc and BankRate.com, all continue to recognize Mission Valley's soundness and financial strength with their highest ratings.

While we started off 2020 strong, unforeseen challenges have made it difficult to project how this year will unfold. From the disruption caused by the pandemic and "safer at home" orders to the rioting and protests concerning racial injustice it seems everything has changed. We must now adjust to manage through these unprecedented times. We have taken all necessary precautions to ensure the safety of our staff and our clients while continuing to provide much needed services. This situation caused us to have to delay our Annual Shareholders' meeting which is now scheduled for August 25,, 2020, though we continue to closely monitor the situation. It is important to point out that the Bank entered 2020 and the pandemic with a strong balance sheet reflecting a Tier 1 Leverage Ratio well in excess of the regulatory definition of "Well Capitalized" which will help us to manage potential stress to the credit portfolio that may lie ahead.



While the pandemic has resulted in very trying times for all of us, we are confident that the steps we have taken combined with us all working together to do our part to control the spread of this virus we will come through it and be stronger for it. Until then, our wish is that you all stay safe and healthy.

Tamara Gurney
President & CEO
Mission Valley Bancorp
Mission Valley Bank



Earle S. Wasserman
Chairman of the Board
Mission Valley Bancorp
Mission Valley Bank

2019 Awards, Recognitions & Industry Accolades

The Findley Reports
named Mission Valley Bank among the
2019 Premier Performing Banks
www.Findley-Reports.com

BankRate.com
rated Mission Valley Bank as a
5 Star Financial Institution
Exhibiting Superior Condition and Earning a
Full 5 Star Rating for Safety & Soundness
www.BankRate.com

Bauer Financial, Inc.
named Mission Valley Bank
5-Star Superior
www.BauerFinancial.com

Veribanc
ranked Mission Valley Bank as a
Green Three Star "Blue Ribbon Bank"
www.Veribanc.com

Mission Valley Bank's Rachel Carrillo (Credit Administrative Assistant)
named one of the ***Valley's Most Trusted Advisors – Business Banking Award*** by the
San Fernando Valley Business Journal marking Mission Valley Bank's
9th Consecutive Year receiving this honor
www.SFVBJ.com

The American Banker
named Mission Valley Bank among the
Top 200 Bank's & Thrifts
www.AmericanBanker.com

During 2019, the ***San Fernando Valley Business Journal*** and the ***Los Angeles Business Journal***
recognized Mission Valley Bank among the following:
Top Ranked Banks
Largest Ranked Banks
Top Public Companies
www.LABJ.com | www.SFVBJ.com

2019 FINANCIAL STATEMENTS

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MOSSADAMS

Report of Independent Auditors

The Board of Directors and Shareholders
Mission Valley Bancorp

Report on Financial Statements

We have audited the accompanying consolidated financial statements of Mission Valley Bancorp and its subsidiary, which comprise the consolidated statements of financial condition as of December 31, 2019 and 2018, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated 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 audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mission Valley Bancorp and its subsidiary as of December 31, 2019 and 2018, and the results of their operations and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Moss Adams LLP

Los Angeles, California
March 31, 2020

Mission Valley Bancorp
Consolidated Statements of Financial Condition
(In Thousands, Except Share Data)

ASSETS

	December 31, 2019	December 31, 2018
CASH AND DUE FROM BANKS	$ 23,977	$ 20,575
FEDERAL FUNDS SOLD	28,225	53,760
Total cash and cash equivalents	52,202	74,335
INTEREST BEARING DEPOSITS IN OTHER BANKS	5,469	4,294
INVESTMENT SECURITIES		
Available-for-sale, at fair value	18,031	12,080
Held-to-maturity, at amortized cost	1	17
LOANS HELD FOR SALE	-	4,697
LOANS, net	262,764	239,206
PREMISES AND EQUIPMENT, net	297	286
DEFERRED TAX ASSET, net	1,425	876
BANK OWNED LIFE INSURANCE	10,302	10,024
RESTRICTED EQUITY SECURITIES	1,921	1,889
ACCRUED INTEREST RECEIVABLE	972	836
OTHER ASSETS	4,489	2,685
Total assets	$ 357,873	$ 351,225

LIABILITIES AND SHAREHOLDERS' EQUITY

	2019	2018
LIABILITIES		
Deposits:		
Non-interest-bearing demand	$ 206,756	$ 188,552
Interest-bearing demand	64,880	64,201
Savings	9,340	18,495
Time deposits under $250,000	5,798	8,812
Time deposits $250,000 and over	14,392	16,680
Total deposits	301,166	296,740
Junior subordinated deferrable interest debentures	6,186	6,186
Notes payable	6,692	10,336
Accrued interest payable and other liabilities	7,095	4,695
Total liabilities	321,139	317,957
COMMITMENTS AND CONTINGENCIES – Note 14		
SHAREHOLDERS' EQUITY		
Common stock – 10,000,000 shares authorized; no par value; 3,233,365 and 3,208,365 shares issued and outstanding	12,747	12,747
Additional paid in capital	1,689	1,400
Retained earnings	23,037	19,754
Accumulated other comprehensive loss	(739)	(633)
Total shareholders' equity	36,734	33,268
Total liabilities and shareholders' equity	$ 357,873	$ 351,225

Consolidated Statements of Income

(In Thousands, Except Per Share Data)

	Years Ended December 31, 2019	2018
INTEREST INCOME		
Interest and fees on loans	$ 14,270	$ 13,994
Interest on investment securities	317	262
Other interest income	1,356	1,162
Total interest income	15,943	15,418
INTEREST EXPENSE		
Interest on deposits	506	359
Interest on borrowings	713	802
Total interest expense	1,219	1,161
NET INTEREST INCOME	14,724	14,257
PROVISION FOR LOAN LOSSES	563	609
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	14,161	13,648
NON-INTEREST INCOME		
Service charges and other income	1,858	1,740
Gain (loss) on sale of loans	978	(386)
Net merchant income	569	548
Increase in cash surrender value of bank owned life insurance	278	271
Gain on sale of OREO	6	-
Other income	499	511
Total non-interest income	4,188	2,684
NON-INTEREST EXPENSES		
Salaries, wages, and employee benefits	8,548	7,539
Legal, professional, and consulting	907	950
Furniture and equipment	918	876
Data processing	709	623
Occupancy and equipment expenses	646	531
Advertising	159	208
Insurance	86	159
Other operating expenses	1,359	1,395
Total non-interest expenses	13,332	12,281
NET INCOME BEFORE PROVISION FOR INCOME TAXES	5,017	4,051
Provision for income taxes	1,413	895
NET INCOME	3,604	3,156
PREFERRED STOCK DIVIDENDS	-	-
NET INCOME AVAILABLE TO COMMON SHAREHOLDERS	$ 3,604	$ 3,156
EARNINGS PER SHARE AVAILABLE TO COMMON SHAREHOLDERS – basic and diluted	$ 1.12	$ 0.98

Mission Valley Bancorp

Consolidated Statements of Comprehensive Income

(In Thousands)

	Years Ended December 31, 2019	2018
NET INCOME	$ 3,604	$ 3,156
Other comprehensive loss:		
Net change in unrealized losses on cash flow hedge	(362)	(395)
Change in unrealized losses on available for sale securities, net of taxes of $108 and $10 in 2019 and 2018, respectively	256	(110)
Other comprehensive loss	(106)	(505)
Total comprehensive income	$ 3,498	$ 2,651

Mission Valley Bancorp
Consolidated Statements of Changes in Shareholders' Equity
(In Thousands, Except Share Data)

	Common Stock Number of Shares	Common Stock Amount	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
BALANCE, December 31, 2017	3,208,365	$ 12,747	$ 1,199	$ 16,598	$ (128)	$ 30,416
Share-based compensation expense	-	-	64	-	-	64
Issuance of stock awards	-	-	137	-	-	137
Total comprehensive income	-	-	-	3,156	(505)	2,651
BALANCE, December 31, 2018	3,208,365	12,747	1,400	19,754	(633)	33,268
Share-based compensation expense	-	-	109	-	-	109
Issuance of stock awards	25,000	-	180	-	-	180
Dividends on common stock	-	-	-	(321)	-	(321)
Total comprehensive income	-	-	-	3,604	(106)	3,498
BALANCE, December 31, 2019	3,233,365	$ 12,747	$ 1,689	$ 23,037	$ (739)	$ 36,734

Mission Valley Bancorp
Consolidated Statements of Cash Flows
(In Thousands)

	Years Ended December 31, 2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 3,604	$ 3,156
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of premises and equipment	142	112
Provision for loan losses	563	609
Amortization of deferred loan fees, costs, and premium, net	2,439	1,715
Origination of loans held for sale	-	(1,300)
Proceeds from sale of loans held for sale	1,824	21,430
(Gain) loss on sale of loans held for sale	(978)	386
Accretion and amortization on investments	(115)	61
Shared-based compensation expense	289	201
Deferred taxes	549	487
Increase in cash surrender value of bank owned life insurance	(278)	(271)
Net change in:		
Accrued interest receivable and other assets	(2,292)	(994)
Accrued interest payable and other liabilities	1,196	1,085
Net cash provided by operating activities	6,943	26,677
CASH FLOWS FROM INVESTING ACTIVITIES		
Changes in interest bearing deposits in other banks, net	(1,175)	(1,569)
Purchases of available-for-sale investments	(9,467)	-
Proceeds from repayments, sales, and maturities of available-for-sale investments	3,983	2,544
Proceeds from prepayments and maturities of held-to-maturity investments	16	62
Net purchases of restricted equity securities	(32)	(15)
Net increase in loans	(22,709)	(24,368)
Purchases of premises and equipment	(153)	(129)
Net cash used in investing activities	(29,537)	(23,475)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net (decrease) increase in time deposits	(5,302)	6,827
Decrease in notes payable	(3,644)	-
Net increase in other deposits	9,728	9,666
Dividends on common stock	(321)	-
Net cash provided by financing activities	461	16,493
CHANGE IN CASH AND CASH EQUIVALENTS	(22,133)	19,695
Cash and cash equivalents, beginning of year	74,335	54,640
Cash and cash equivalents, end of year	$ 52,202	$ 74,335
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Interest paid	$ 1,238	$ 1,170
Taxes paid	$ 1,993	$ 1,109
SUPPLEMENTAL DISCLOSURES OF NONCASH INVESTING AND FINANCING ACTIVITIES		
Change in unrealized gain and losses on investments available-for-sale	$ (352)	$ 120
Transfers of loans receivable held for sale to loans receivable held for investment	$ 3,302	$ 6,601
Transfers from loans receivables held for investments to other real estate owned	$ 550	$ -
Lease liabilities arising from obtaining right-of-use-assets	$ 1,450	$ -

Note 1 – Summary of Significant Accounting Policies

Nature of operations – Mission Valley Bank (the “Bank”) was formed during 2001 and on May 24, 2005, the shareholders of the Bank approved the exchange of common stock in Mission Valley Bank for common stock of a newly formed holding company, Mission Valley Bancorp (the “Company”). The transaction was consummated on August 20, 2005. The Bank is the Company’s only subsidiary and it is wholly owned by the Company. The Company provides a full range of banking services to individual and corporate customers through the Bank. The Bank has two branches located in Sun Valley and Santa Clarita, California. The Company has been authorized by the Federal Reserve Bank of San Francisco to engage in lending activities separate from the Bank but to date has not done so.

Mission Valley Bank is a state chartered depository institution subject to regulation and examination by the California Department of Business Oversight (DBO) and Federal Deposit Insurance Corporation (FDIC).

Basis of presentation and consolidation – The accompanying consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) and general practices within the banking industry. The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Mission Valley Bank. All significant intercompany balances and transactions have been eliminated in consolidation.

In 2005, the Company issued $6,186,000 of junior subordinated deferrable interest debentures through Mission Valley Statutory Trust I. The Company follows U.S. GAAP that determines when variable interest entities should be consolidated and determined that the Mission Valley Statutory Trust I should not be consolidated. As a result, the consolidated statements of financial condition include $6,186,000 as junior subordinated deferrable interest debentures. Also included in other assets in the consolidated statements of financial condition is $186,000 of investments in Mission Valley Statutory Trust I, which is reported using the cost method.

Use of estimates – The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated statements of financial condition, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, valuation of investment securities, valuation of deferred tax assets, and share-based compensation.

Concentrations of credit risk – Assets and liabilities that subject the Company to concentrations of credit risk consist of interest-bearing deposits at other banks, investments available-for-sale, loans, and deposits. Most of the Company’s customers are located within Los Angeles County and surrounding areas. For the years ended December 31, 2019 and 2018, the Company did not have any significant concentrations in its business with any one customer.

Note 1 – Summary of Significant Accounting Policies (continued)

As of December 31, 2019 and 2018, the Company has cash deposits at other financial institutions in excess of the FDIC insured limits. The Company places these deposits with major financial institutions and monitors the financial condition of these institutions. Management believes the risk of loss associated with such deposits to be minimal.

The Company’s loan portfolio consists primarily of loans to borrowers within Southern California. Although the Company has a diversified loan portfolio, a substantial part of the debtors’ ability to honor their contracts is dependent upon the economic conditions in this region. Real estate secured loans represented approximately 56% and 62% of total gross loans held for investment at December 31, 2019 and 2018, respectively. Management has taken this factor into account in the determination of the allowance for loan losses.

Cash and cash equivalents – For purposes of reporting cash and cash equivalents in the consolidated statements of financial condition and the consolidated statements of cash flows, cash and cash equivalents include cash, due from banks, and federal funds sold, all of which have original maturities of ninety days or less.

Banking regulations require that banks maintain a percentage of their deposits as reserves in cash or on deposit with the Federal Reserve Bank. The Company was in compliance with its reserve requirements as of December 31, 2019 and 2018.

Interest-bearing deposits in other banks – Interest-bearing deposits in other banks are purchased with an original maturity date greater than ninety days and are carried at amortized cost. Interest-bearing deposits in other banks include certificates of deposits in major financial institutions located throughout the United States of America.

Investment securities – In accordance with generally accepted accounting principles, the Company is required to designate its readily marketable investments securities as “held-to-maturity,” “available-for-sale,” or “trading.” The Company did not designate any of its investments as trading securities. Debt securities are classified as held-to-maturity if the Company has both the intent and ability to hold those securities to maturity regardless of changes in market conditions, liquidity needs, or changes in general economic conditions. These securities are carried at cost adjusted for amortization of premium and accretion of discount, computed by the effective interest method over their contractual lives. Debt securities classified as available-for-sale are reported at fair value, with unrealized gains and losses excluded from earnings and reported as a separate component of shareholders’ equity as an item of other comprehensive income. Investment transactions are recorded on the trade date. Gains and losses realized on disposition of investment securities are recognized at the time of sale based upon the specific identification method. Premiums and discounts are recognized in interest income using the interest method over the period to maturity.

Note 1 – Summary of Significant Accounting Policies (continued)

Interest income from the investment securities portfolio is accrued as earned including the accretion of discounts and the amortization of premiums based on the original cost of each security owned. Discounts and premiums are accreted and amortized on a method that approximates the effective interest method to the maturity date of the security with the exception of the mortgage-backed securities. Discounts and premiums on mortgage-backed securities are accreted and amortized to the expected maturity date of the investment security. Realized gains or losses on the sale of investment and mortgage-backed securities are reported in the consolidated statement of operations as of the trade date and determined using the amortized cost of the specific security sold. Declines in the fair value of individual securities below their cost that are deemed other than temporary result in write-downs of the individual securities to their fair value.

Management performs regular impairment analyses on the securities portfolio in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) guidance related to the consideration of impairment related to certain debt and equity securities. If it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the debt security not impaired at acquisition, an other-than-temporary impairment is considered to have occurred. When an other-than-temporary impairment (OTTI) occurs, the cost basis of the security is written down to its fair value (as the new cost basis) and the write-down is accounted for as a realized loss if it is credit related. In assessing whether impairment represents OTTI, the Company must consider whether it intends to sell a security or if it is likely that they would be required to sell the security before recovery of the amortized cost basis of the investment, which may be maturity. For debt securities, if the Company intends to sell the security or it is likely that a sale of the security may be required before recovering the cost basis, the entire impairment loss would be charged to results of operations as an OTTI. If the Company does not intend to sell the security and it is not likely the sale of the security is required by the Company, and the Company does not expect to recover the entire amortized cost basis of the security, only the portion of the impairment loss representing credit losses would be charged to results of operations. The credit loss on a security is measured as the difference between the amortized cost basis and the present value of the cash flows to be expected to be collected. Projected cash flows are discounted by the original or current effective interest rate depending on the nature of the security being measured for potential OTTI. The remaining impairment related to other factors, the difference between the present value of the cash flows to be expected to be collected and fair value, is recognized as a charge to other comprehensive income (OCI).

Note 1 – Summary of Significant Accounting Policies (continued)

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 amounts and net of any deferred fees or costs on originated loans or unamortized premiums or discounts on purchased loans. Interest income on loans is calculated by the simple-interest method on daily balances of the principal amount outstanding. Loan origination fees and origination costs are capitalized and recognized as an adjustment to yield over the life of the related loan using the effective interest method. The accrual of interest on loans is discontinued at the time the loan becomes ninety-days delinquent unless the credit is well secured and in process of collection. In some cases, loans can be placed on nonaccrual status or charged off at an earlier date if collection of principal or interest is considered doubtful. Subsequent collections of interest are applied to unpaid balances or included in interest income based upon management's assessment of the likelihood that principal will be collected.

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.

A loan is considered impaired when it is probable that the Company will not be able to collect all principal and interest amounts due according to the loan's contractual terms based upon available information and events. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. The amount of the valuation allowance for impaired loans is determined by comparing the recorded investment in each loan with its value measured by one of three methods: (i) the estimated present value of total expected future cash flows, discounted at the loan's effective interest rate; (ii) the loan's observable market price, if available from a secondary market; or (iii) by the fair value of the underlying collateral if the loan is collateral dependent.

If the measure of impairment for an impaired loan is less than the related recorded investment, the shortfall is charged-off or a specific valuation allowance (impairment allowance) is established as a component of the allowance for loan losses through a charge to the provision for loan losses. Subsequent permitted adjustments to the impairment allowance are made through a corresponding charge or credit to the provision for loan losses.

Note 1 – Summary of Significant Accounting Policies (continued)

Loans are reported as Troubled Debt Restructuring (TDR) when the Company grants concession(s) to a borrower experiencing financial difficulties that it would not otherwise consider. Examples of such concession include forgiveness of principal or accrued interest, extending the maturity date(s), or providing a lower interest rate than would be normally available for a transaction of similar risk. As a result of these concessions, TDR loans are impaired as the Company will not collect all amounts due, both principal and interest, in accordance with the terms of the original loan agreement. Impairment allowances on non-collateral dependent TDR loans are measured by comparing the present value of expected future cash flows on the TDR loans discounted at the interest rate of the original loan agreement to the loan's carrying value. These impairment allowances are recognized as a specific component to be provided for in the allowance for loan losses.

Allowance for loan losses – The provision for loan losses charged to results of operations is an amount sufficient to bring the allowance for loan losses to an estimated balance considered adequate to absorb probable losses inherent in the portfolio at the date of the consolidated financial statements. 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.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans that considers historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. The evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. The allowance consists of specific, general, and unallocated components. The specific component relates to loans that are classified as impaired. The general component covers non-impaired loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

In addition, bank regulatory authorities, as part of their periodic examination of the Company, may require additional charges to the provision for loan and lease losses in future periods if warranted as a result of their review. A significant decline in real estate market values may require an increase in the allowance for loan and lease losses. The prolonged U.S. recession, the housing market downturn, and declining real estate values in our markets have negatively impacted aspects of the Company's residential development, commercial real estate, commercial construction, and commercial loan portfolios. A continued deterioration in the Company's markets may adversely affect its loan portfolio and may lead to additional charges to the provision for loan losses.

Note 1 – Summary of Significant Accounting Policies (continued)

Loans held for sale and non-guaranteed portion of SBA loans – The portions of U.S. Small Business Administration (SBA) loans that are guaranteed by the SBA are classified by management as loans held for sale since the Company intends to sell these loans. Loans held for sale are recorded at the lower of aggregate cost or estimated fair value. The fair value of SBA loans held for sale is based primarily on prices that secondary markets are currently offering for loans with similar characteristics. Net unrealized losses, if any, are recognized through a valuation allowance through a charge to income. The carrying value of SBA loans held for sale is net of premiums as well as deferred origination fees and costs. Premiums and net origination fees and costs are deferred and included in the basis of the loans in calculating gains and losses upon sale. SBA loans are generally secured by the borrowing entities' assets such as accounts receivable, property and equipment, and other business assets. The Company generally recognizes gains or losses on these loan sales based on the difference between the sales proceeds received and the allocated carrying value of the loans sold (which can include deferred premiums and net origination fees and costs). The non-guaranteed portion of SBA loans is not typically sold by the Company and is classified as held for investment.

Servicing assets – In connection with the Company's SBA lending activities, the Company recognizes servicing assets when servicing rights are retained. The Company initially recognizes and measures at fair value servicing rights obtained from SBA loan sales. The Company subsequently measures these servicing assets by using the amortization method, which amortizes servicing assets in proportion to, and over the period of, estimated net servicing income. The amortization of the servicing assets is analyzed periodically and is adjusted to reflect changes in prepayment rates and other estimates. The servicing asset is included in other assets on the consolidated statements of financial condition and the related amortization is net against other non-operating income in the consolidated statements of income.

Premises and equipment – Premises and equipment are reported at cost less accumulated depreciation and amortization. Depreciation is computed using the straight-line method over the estimated useful lives, which typically range from three to seven years for furniture and equipment. Leasehold improvements are amortized over the shorter of the remaining lease term and the subsequent option period that is likely to be exercised or the estimated useful lives of the leasehold improvements.

Expenditures for betterments or major repairs are capitalized and those for ordinary repairs and maintenance are charged to results of operations as incurred. Gains and losses on dispositions are included in current results of operations.

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amounts of such assets may not be recoverable. If the sum of the expected future cash flows is less than the stated amount of the asset, an impairment loss is recognized for the difference between the fair value of the asset and its carrying amount.

Note 1 – Summary of Significant Accounting Policies (continued)

Other real estate owned – Assets acquired in settlement of loans are recorded at fair value less estimated disposal costs. Any excess of the carrying amount of the loan over the fair value of the asset is charged against the allowance for loan losses at the time of transfer. Subsequent to the transfer, any losses on disposition or write-downs as a result of declines in market value of specific assets are charged against current results of operations. Real estate acquired through foreclosure sale, deed-in-lieu of foreclosure, and bank property for which banking use is no longer contemplated are classified as other real estate owned on the consolidated statements of financial condition. Operating income and expenses incurred on these properties are reflected in current earnings within non-interest expense. There was one other real estate owned property that was acquired and sold during the year ended 2019. There was no other real estate owned activity during 2018.

Derivative financial instruments and hedging activities – The Company enters into derivative transactions principally to protect against the risk of adverse price or interest rate movements on the future cash flows of certain assets. ASC Topic 815, *Derivatives and Hedging (ASC 815)*, establishes accounting and reporting standards requiring that every derivative instrument be recorded in the consolidated statements of financial condition as either an asset or liability measured at its fair value. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and on the type of hedging relationship. On the date the derivative contract is entered into, the Company designates the derivative as a fair value hedge, a cash flow hedge, or a non-designated derivative. The Company's derivative contract is designated as a cash flow hedge.

Cash flow hedges are accounted for by recording the changes in the fair value of the effective portion of the derivative instrument in other comprehensive income (loss) and are recognized in the consolidated statements of operations when the hedged item affects earnings.

The Company formally documents the relationship between a derivative instrument and a hedged asset or liability, as well as its risk management objective and strategy for undertaking various hedge transactions.

The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in the hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

Income taxes – The Company uses the asset and liability method to account for income taxes. The objective of the asset and liability method is to establish deferred tax assets and liabilities for the temporary differences between the financial reporting basis and the income tax basis of the Company's assets and liabilities at enacted tax rates expected to be in effect when such amounts are realized or settled. Changes in enacted tax rates result in a revaluation of deferred tax assets and liabilities through the income tax provision in the period that the tax rate changes are enacted.

Note 1 – Summary of Significant Accounting Policies (continued)

The Company's annual tax rate is based on its income, statutory tax rates, and tax planning opportunities available in which it operates. Tax laws are complex and subject to different interpretations by the taxpayer and respective governmental taxing authorities. Significant judgment is required in determining tax expense and in evaluating tax positions, including evaluating uncertainties. Accounting for income taxes prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return.

Benefits from tax positions are recognized in the financial statements only when it is more-likely-than-not that the tax position will be sustained upon examination by the appropriate taxing authority that would have full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. The Company reviews its tax positions periodically and adjusts the balances as new information becomes available. It is the Company's policy to recognize interest and penalties associated with uncertain tax positions as components of other operating expenses in the income statement.

Deferred income tax assets represent amounts available to reduce income taxes payable on taxable income in future years. Such assets arise because of temporary differences between the financial reporting and tax bases of assets and liabilities, as well as from net operating loss and tax credit carry forwards. The Company evaluates the recoverability of these future tax deductions by assessing the adequacy of future expected taxable income from all sources, including reversal of taxable temporary differences, forecasted operating earnings, and available tax planning strategies. These sources of income inherently rely heavily on estimates. The Company uses historical experience and short- and long-range business forecasts to provide insight. Deferred tax assets could be reduced in the near term if estimates of taxable income are significantly reduced or available tax planning strategies are no longer viable.

Bank Owned Life Insurance – The Company invests in Bank Owned Life Insurance (BOLI). BOLI involves the purchasing of life insurance by the Company on a chosen group of employees. The Company is the owner and beneficiary of these policies. BOLI is recorded as an asset at cash surrender value. Increases in the cash value of these policies, as well as insurance proceeds received, are recorded in other non-interest income and are not subject to income tax.

Restricted equity securities – At December 31, 2019 and 2018, the Company held $1,391,000 and $1,359,000, respectively, of shares of Federal Home Loan Bank ("FHLB"). The Company evaluates its investment in FHLB stock for impairment on a periodic basis. The FHLB has been in compliance with all of its regulatory capital requirements at the end of 2019 and 2018. The Company has not recorded an impairment on its investment of FHLB stock during 2019 and 2018.

The Company also invests in the stock of Pacific Coast Bankers Bank ("PCBB") in connection with its correspondent banking arrangement with PCBB. At December 31, 2019 and 2018, the Company held approximately $531,000, par value, of PCBB stock. PCBB stock is restricted as to purchase, sale, and redemption.

Note 1 – Summary of Significant Accounting Policies (continued)

The investments in FHLB stock and PCBB stock are carried as cost method investments as of December 31, 2019 and 2018.

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

Share-based compensation – The Company accounts for stock option awards whereby the compensation cost relating to share-based payment transactions be recognized in the statements of operations based upon the grant-date fair value of the stock options granted by the Company. The effect of stock-based accounting rules is to require entities to measure the cost of employee services received in exchange for stock options and to recognize the cost over the period the employee is required to provide services for the award. The fair value of stock options is measured using a Black-Scholes pricing model.

The Company's 2017 Stock Option and Restricted Stock Grant Plan provides for granting of restricted stock units for the benefit of certain members of the board of directors, executives, and key employees of the Company and its affiliates. Restricted stock grants are subject to performance-based vesting as well as other approved vesting conditions. Compensation expense is recognized over the service period to the extent restricted stock units are expected to vest.

Advertising costs – Advertising costs of $160,000 and $208,000 for the years ended December 31, 2019 and 2018, respectively, were expensed as incurred.

Comprehensive income – Comprehensive income consists of net income and other comprehensive income (loss). Other comprehensive income (loss) consists of unrealized gains and losses on the Company's cash flow hedge and securities available-for-sale, which are also recognized as separate components of consolidated shareholders' equity.

Common stock – The Company has authorized 10 million shares of common stock. Each share entitles the holder to one vote. There are no dividend or liquidation preferences, participation rights, call prices or dates, conversion prices or rates, sinking fund requirements, or unusual voting rights associated with these shares.

Preferred stock – The Company has authorized 10 million shares of preferred stock.

Note 1 – Summary of Significant Accounting Policies (continued)

Earnings per share (EPS) – Earnings per share amounts have been computed using the weighted average number of shares outstanding of common stock for the purposes of computing basic EPS. There were no common stock equivalents outstanding that would have a dilutive impact on EPS at December 31, 2019 or 2018. Basic EPS is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding for the period. Basic EPS excludes the dilutive effect that could occur if any securities or other contracts to issue common stock were exercised or converted into or resulted in the issuance of common stock. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock, such as stock options, result in the issuance of common stock which shares in the earnings available to common shareholders of the Company. The Company's restricted stock awards outstanding are not eligible to be issued or to receive dividends until fully vested. There were 25,000 stock awards that vested and issued during the year ended December 31, 2019. The treasury stock method is applied to determine the dilutive effect of stock options in computing dilutive earnings per share. Basic EPS is calculated as follows:

(In thousands, except per share data)	2019	2018
BASIC EARNINGS PER SHARE		
Net income available to common shareholders	$ 3,604	$ 3,156
Weighted average common shares outstanding	3,231	3,208
Earnings per share available to common shareholders – basic and diluted	$ 1.12	$ 0.98

Note 1 – Summary of Significant Accounting Policies (continued)

Fair value measurements – FASB ASC 820, *Fair Value Measurements and Disclosures,* defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. FASB ASC 820 establishes a three-level hierarchy for disclosure of assets and liabilities recorded at fair value. The classification of assets and liabilities within the hierarchy is based on whether the inputs to the valuation methodology used for measurement are observable or unobservable. Observable inputs reflect market-derived or market-based information obtained from independent sources, while unobservable inputs reflect our estimates about market data. In general, fair values determined by Level 1 inputs utilize quoted prices for identical assets or liabilities traded in active markets that the Company has the ability to access. Fair values determined by Level 2 inputs utilize inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability and include situations where there is little, if any, market activity for the asset or liability. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

Recent accounting pronouncements – In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326)*: *Measurement of Credit Losses on Financial Instruments*. The ASU is intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The ASU requires the measurement of all expected credit losses for certain financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates but will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. The ASU requires enhanced disclosures to help investors and other financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio. These disclosures include qualitative and quantitative requirements that provide additional information about the amounts recorded in the financial statements. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The FASB has deferred the effective date of this ASU to fiscal years beginning on or after December 15, 2022, including interim periods within those fiscal years for public business entities. The Company is currently evaluating the impact of ASU No. 2016-13 on its consolidated financial statements.

Note 1 – Summary of Significant Accounting Policies (continued)

Adoption of new accounting standards – On January 1, 2018, the Company adopted ASU 2014-09, *Revenue from Contracts with Customers*, and all subsequent amendments to the ASU (collectively, "ASC 606"), which (i) creates a single framework for recognizing revenue from contracts with customers that fall within its scope and (ii) revises when it is appropriate to recognize a gain (loss) from the transfer of nonfinancial assets, such as other real estate owned (OREO). To determine revenue recognition for arrangements that an entity determines are within the scope of Topic 606, the Company performs the following five steps: (i) identify the contract(s) with a customer; (ii) identify the performance obligations in the contract; (iii) determine the transaction price; (iv) allocate the transaction price to the performance obligations in the contract; and (v) recognize revenue when (or as) the Company satisfies a performance obligation. The majority of the Company's revenues come from interest income and other sources, including loans, leases, securities, and derivatives, that are outside the scope of ASC 606. The Company's services that fall within the scope of ASC 606 are presented within non-interest income and are recognized as revenue as the Company satisfies its obligation to the customer. Services within the scope of ASC 606 include deposit service charges, debit and ATM interchange income, brokerage revenue, merchant fee income, credit card and interchange income, and gain (loss) on other real estate owned, net. Refer to Note 18 – Revenue from Contracts with Customers for further discussion on the Company's accounting policies for revenue sources within the scope of ASC 606.

The Company adopted ASC 606 using the modified retrospective method applied to all contracts not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018, are presented under ASC 606 while prior period amounts continue to be reported in accordance with legacy U.S. GAAP. The adoption of ASC 606 did not result in a material change to the accounting for any of the in-scope revenue streams; as such, no cumulative effect adjustment was recorded.

On January 1, 2019, the Company adopted ASU No. 2016-02, *Leases (Topic 842)*, and subsequent amendments thereto, which requires the Company to recognize most leases on the balance sheet. The Company adopted the standard under a modified retrospective approach as of the date of adoption and elected to apply several of the available practical expedients, including:

1) Carry over of historical lease determination and lease classification conclusions
2) Carry over of historical initial direct cost balances for existing leases
3) Accounting for lease and non-lease components in contracts in which the Company is a lessee as a single lease component

The Company has several lease agreements, such as branch locations, which are considered operating leases and, therefore, were not previously recognized on the Company's consolidated balance sheet. The new guidance requires these lease agreements to be recognized on the consolidated balance sheet as a right-of-use asset (ROU) and a corresponding lease liability.

Note 1 – Summary of Significant Accounting Policies (continued)

Adoption of the leasing standard resulted in the recognition of operating right-of-use assets of $1.4 million and operating lease liabilities of $1.4 million as of January 1, 2019. These amounts were determined based on the present value of remaining minimum lease payments, discounted using the Company's incremental borrowing rate as of the date of adoption. There was no material impact to the timing of expense or income recognition in the Company's consolidated statement of operations. Prior periods were not restated and continue to be presented under legacy U.S. GAAP. Disclosures under the Company's leasing activities are presented in Note 14 – Commitments and Contingencies.

In January 2016, the FASB issued ASU No. 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. The new guidance is intended to improve the recognition and measurement of financial instruments. This ASU requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. In addition, the amendment requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes and requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (i.e., securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements. This ASU also eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet. The amendment also requires a reporting organization to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument specific credit risk (also referred to as "own credit") when the organization has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. ASU No. 2016-01 is effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted for certain provisions. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, *Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. 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. The areas for simplification include income tax consequences, forfeitures, and classification of awards as either equity or liabilities and classification on the statement of cash flows. ASU 2016-09 is effective for fiscal years in annual periods beginning after December 15, 2016, and interim periods within those fiscal years' annual periods. The adoption of ASU 2016-09 did not have a material impact on the consolidated financial statements.

Reclassification – Certain amounts from the prior year footnotes have been reclassified, in order to conform to the current year presentation. There was no impact on net income or retained earnings.

Note 2 – Investment Securities

The carrying amounts of securities and their estimated fair values at December 31, 2019 and 2018, were as follows:

(In thousands)	December 31, 2019 Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-Sale				
Mortgage- and asset-backed securities	$ 14,142	$ 48	$ (26)	$ 14,164
Corporate bonds	3,074	7	(2)	3,079
Other	800	-	(12)	788
	$ 18,016	$ 55	$ (40)	$ 18,031

(In thousands)	December 31, 2019 Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Held-to-Maturity				
Mortgage- and asset-backed securities	$ 1	$ -	$ -	$ 1
	$ 1	$ -	$ -	$ 1

(In thousands)	December 31, 2018 Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-Sale				
Mortgage- and asset-backed securities	$ 11,231	$ 1	$ (304)	$ 10,928
Corporate bonds	-	-	-	-
Municipal investments	388	-	(1)	387
Other	800	-	(35)	765
	$ 12,419	$ 1	$ (340)	$ 12,080

(In thousands)	December 31, 2018 Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Held-to-Maturity				
Mortgage- and asset-backed securities	$ 17	$ -	$ -	$ 17
	$ 17	$ -	$ -	$ 17

Note 2 – Investment Securities (continued)

Information pertaining to investment securities with gross unrealized losses at December 31, 2019 and 2018, aggregated by investment category and length of time that individual securities have been in continuous loss position is as follows:

	2019					
	Less Than 12 Months		12 Months or Longer		Total	
(In thousands)	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
Available-for-Sale						
Corporate bonds	$ 2,057	$ (2)	$ -	$ -	$ 2,057	$ (2)
Mortgage- and asset-backed securities	4,053	(19)	1,499	(7)	5,552	(26)
Other	-	-	788	(12)	788	(12)
	$ 6,110	$ (21)	$ 2,287	$ (19)	$ 8,397	$ (40)

	2018					
	Less Than 12 Months		12 Months or Longer		Total	
(In thousands)	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
Available-for-Sale						
Mortgage- and asset-backed securities	$ 617	$ (4)	$ 10,652	$ (301)	$ 11,269	$ (305)
Other	-	-	765	(35)	765	(35)
	$ 617	$ (4)	$ 11,417	$ (336)	$ 12,034	$ (340)

There were eight and twenty-three available-for-sale and one and one held-to-maturity securities in an unrealized loss position for the years ended December 31, 2019 and 2018, respectively. There was one available-for-sale security in an unrealized loss position for twelve months or more for the year ended December 31, 2019.There were twenty-one available-for-sale securities in an unrealized loss position for twelve months or more for the year ended December 31, 2018.

Management evaluates securities for OTTI at least on a quarterly basis and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value, which may be maturity. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. The Company does not have any securities that were considered to be other than temporarily impaired in 2019 or 2018.

Note 2 – Investment Securities (continued)

The amortized cost and estimated fair values of investment securities at December 31, 2019 and 2018, by contractual maturity, are shown below. Expected and actual maturities may differ from contractual maturities because issuers or borrowers may have the right to call or prepay obligations with or without prepayment penalties.

	December 31, 2019		December 31, 2018	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
(In thousands)				
Available-for-Sale				
Due in one year or less	$ 354	$ 354	$ -	$ -
Due from one to five years	5,825	5,837	938	934
Due in more than five years	11,837	11,840	11,481	11,146
	$ 18,016	$ 18,031	$ 12,419	$ 12,080

	December 31, 2019		December 31, 2018	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
(In thousands)				
Held-to-Maturity				
Due in one year or less	$ 1	$ 1	$ -	$ -
Due from one to five years	-	-	17	17
	$ 1	$ 1	$ 17	$ 17

There were no sales of available-for-sale securities for the year ended December 31, 2019 or 2018.

Note 3 – Loans and Allowance for Loan Losses

The composition of the Company's loan portfolio at December 31, 2019 and 2018, was as follows:

(In thousands)	2019	2018
Real estate loans	$ 149,016	$ 151,567
Commercial loans	51,116	38,067
Consumer loans	2,455	2,486
SBA loans	40,820	35,485
Accounts receivable loans	20,221	15,809
Leasing	-	65
Advanced restaurant financing	1,310	-
Overdrafts	1,404	29
Gross loans	266,342	243,508
Less:		
Allowance for loan losses	3,731	3,791
Discount on retained loans	1,254	1,678
Deferred loan costs, net	(1,407)	(1,167)
Net loans	$ 262,764	$ 239,206

The adequacy of the allowance for loan losses is determined by the Company's management based upon evaluation and review of credit quality of the loan portfolio, consideration of historical loss experience, relevant internal and external factors that affect the collection of a loan, and other pertinent factors. The allowance for loan loss analysis is a formula methodology based upon assigning a risk rating to each loan upon loan origination and is periodically reassessed and validated during the term of the loan through the Company's credit review processes. The Company's risk rating methodology assigns risk ratings ranging from 1 to 9 where a higher rating represents a higher risk.

Additionally, the Company's management utilizes qualitative adjustments to the allowance for loan loss analysis in order to systematically quantify the credit risk impact of other trends and changes within the loan portfolio. The qualitative factors consider the following nine factors, which are patterned after the guidelines provided under the Federal Financial Institutions Examination Council Interagency Policy Statement on the Allowance for Loan and Lease Losses issued in 2006:

- Changes in lending policies and procedures, including changes in underwriting standards and collection, charge-off, and recovery practices not considered elsewhere in estimating credit losses;

- Changes in international, national, regional, and local economic and business conditions and developments that affect the collectability of the portfolio, including the condition of various market segments;

Note 3 – Loans and Allowance for Loan Losses (continued)

- Changes in the nature and volume of the portfolio and in the terms of loans;

- Changes in the experience and ability of lending management and other relevant staff;

- Changes in the volume and severity of past due loans, the volume of nonaccrual loans, and the volume and severity of adversely classified or graded loans;

- Changes in the quality of the institution's loan review system;

- Changes in the value of underlying collateral for collateral-dependent loans;

- The existence and effect of any concentrations of credit and changes in the level of such concentrations; and

- The effect of other external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the institutions' existing portfolio.

The Company also establishes specific loss allowances for loans where management has identified potential credit risk conditions or circumstances related to a specific individual credit. The specific allowance amounts are determined by a method prescribed by FASB ASC 310-10-35-22, *Measurement of Impairment*. The loans identified as impaired will be accounted for in accordance with one of the three acceptable valuations as follows: (1) the present value of future cash flows discounted at the loan's effective interest rate; (2) the loan's observable market price; or (3) the fair value of the collateral, if the loan is collateral dependent. For the collateral dependent impaired loans, the Company obtains an appraisal to determine the amount of impairment at the date that the loan becomes impaired. If third-party market data indicates that the value of collateral property values has declined since the most recent valuation date, the value of the property is adjusted downward to reflect current market conditions. If the fair value of the collateral, less cost to sell, is less than the recorded amount of the loan, the Company either recognizes impairment by creating or adjusting an existing valuation allowance with a corresponding charge to the provision for loan losses or charge-off to the impaired balance on collateral dependent loans if it is determined that such loss amount represents a confirmed loss.

Management believes that the allowance for loan losses was adequate as of December 31, 2019 and 2018. There is, however, no assurance that future loan losses will not exceed the levels provided for in the allowance for loan losses and could possibly result in additional charges to the provision for loan losses.

Note 3 – Loans and Allowance for Loan Losses (continued)

The following tables present by portfolio segment the activity in the allowance for loan losses for the years ended December 31, 2019 and 2018. The following also presents by loan type the balance and activity for the allowance for loan losses disaggregated on the basis of the Company's impairment measurement method and the related recorded investment in loans and leases as of and for the years December 31, 2019 and 2018. Recorded investment is defined as the unpaid principal balance, adjusted for deferred fees/costs, premiums, discounts, accrued interest, and may also reflect a previous write-down of the investment. However, for reporting purposes, recorded investments for the Company approximate unpaid principal balance as the other components are not deemed material.

Allowance for Loan Losses
As of and For the Year Ended December 31, 2019

(In thousands)	Beginning Balance	Provision (Recapture) for Loan Losses Charged to Expense	Charge-offs	Recoveries on Loans Previously Charged-off	Ending Balance	Ending Balance Individually Evaluated for Impairment
Real estate loans	$ 2,234	$ (273)	$ -	$ -	$ 1,961	$ 1
Commercial loans	528	549	(582)	128	623	83
Consumer loans	35	(9)	(1)	-	25	-
SBA loans	517	148	(399)	231	497	-
Accounts receivable loans	472	(164)	-	-	308	-
Leasing	1	(1)	-	-	-	-
Advance restaurant financing loans	-	12	-	-	12	-
Overdrafts	4	207	-	-	211	-
Unallocated	-	94	-	-	94	-
Total	$ 3,791	$ 563	$ (982)	$ 359	$ 3,731	$ 84

Allowance for Loan Losses
As of and For the Year Ended December 31, 2018

(In thousands)	Beginning Balance	Provision (Recapture) of Loan Losses Charged to Expense	Charge-offs	Recoveries on Loans Previously Charged-off	Ending Balance	Ending Balance Individually Evaluated for Impairment
Real estate loans	$ 1,403	$ 831	$ -	$ -	$ 2,234	$ 2
Commercial loans	358	172	(96)	94	528	47
Consumer loans	25	10	-	-	35	-
SBA loans	536	319	(338)	-	517	-
Accounts receivable loans	1,123	(651)	-	-	472	-
Leasing	1	-	-	-	1	-
Advance restaurant financing loans	8	(8)	-	-	-	-
Overdrafts	43	(29)	(10)	-	4	-
Unallocated	35	(35)	-	-	-	-
Total	$ 3,532	$ 609	$ (444)	$ 94	$ 3,791	$ 49

Note 3 – Loans and Allowance for Loan Losses (continued)

Recorded Investment in Loans
As of December 31, 2019

(In thousands)	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment	Ending Balance
Real estate	$ 437	$ 148,579	$ 149,016
Commercial	1,233	49,883	51,116
Consumer	-	2,455	2,455
SBA	1,126	39,694	40,820
Accounts receivable	-	20,221	20,221
Leasing	-	-	-
Advance restaurant financing	-	1,310	1,310
Overdrafts	-	1,404	1,404
Total	$ 2,796	$ 263,546	$ 266,342

Recorded Investment in Loans
As of December 31, 2018

(In thousands)	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment	Ending Balance
Real estate	$ 434	$ 151,133	$ 151,567
Commercial	1,359	36,708	38,067
Consumer	-	2,486	2,486
SBA	821	34,664	35,485
Accounts receivable	-	15,809	15,809
Leasing	-	65	65
Advance restaurant financing	-	-	-
Overdrafts	-	29	29
Total	$ 2,614	$ 240,894	$ 243,508

Note 3 – Loans and Allowance for Loan Losses (continued)

As previously noted, the Company uses several credit quality indicators to manage credit risk in an ongoing manner. The Company's primary credit quality indicators are to use an internal credit risk rating system that categorizes loans and leases into pass, special mention, or classified categories. Credit risk ratings are applied individually to all loans that have significant or unique credit characteristics that benefit from a case-by-case evaluation. The following are the definitions of the Company's credit quality indicators:

- Pass/watch: Loans in all classes that comprise the commercial and consumer portfolio segments that are not adversely rated, are contractually current as to principal and interest, and are otherwise in compliance with the contractual terms of the loan or lease agreement. Management believes that there is a low likelihood of loss related to those loans that are considered pass.

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

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

- Doubtful/loss: Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or repayment in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors, which may work towards strengthening of the asset, classification as a loss (and immediate charge-off) is deferred until more exact status may be determined. In certain circumstances, a doubtful rating will be temporary, while the Company is awaiting an updated collateral valuation. In these cases, once the collateral is valued and appropriate margin applied, the remaining un-collateralized portion will be charged off. The remaining balance, properly margined, may then be upgraded to substandard; however, it must remain on nonaccrual. A loss rating is assigned to loans considered un-collectible and of such little value that the continuance as an active Company asset is not warranted. This rating does not mean that the loan has no recovery or salvage value, but rather that the loan should be charged off now, even though partial or full recovery may be possible in the future.

Note 3 – Loans and Allowance for Loan Losses (continued)

The following tables present, by portfolio segment and by credit quality indicator, the recorded investment in the Company's loans as of December 31, 2019 and 2018:

	Internal Risk Rating by Loan Class For the Year Ended December 31, 2019				
(In thousands)	Pass/Watch	Special Mention	Substandard	Doubtful/Loss	Total
Real estate loans	$ 145,584	$ -	$ 3,432	$ -	$ 149,016
Commercial loans	49,860	-	1,256	-	51,116
Consumer loans	2,455	-	-	-	2,455
SBA loans	38,963	-	1,765	92	40,820
Accounts receivable loans	20,221	-		-	20,221
Leasing	-	-	-	-	-
Advanced restaurant financing	1,310	-	-	-	1,310
Overdrafts	1,404	-	-	-	1,404
Total	$ 259,797	$ -	$ 6,453	$ 92	$ 266,342

	Internal Risk Rating by Loan Class For the Year Ended December 31, 2018				
(In thousands)	Pass/Watch	Special Mention	Substandard	Doubtful/Loss	Total
Real estate loans	$ 150,410	$ 394	$ 763	$ -	$ 151,567
Commercial loans	36,433	-	1,634	-	38,067
Consumer loans	2,486	-	-	-	2,486
SBA loans	31,587	2,423	903	572	35,485
Accounts receivable loans	13,437	-	2,372	-	15,809
Leasing	65	-	-	-	65
Advanced restaurant financing	-	-	-	-	-
Overdrafts	29	-	-	-	29
Total	$ 234,447	$ 2,817	$ 5,672	$ 572	$ 243,508

Note 3 – Loans and Allowance for Loan Losses (continued)

The following tables present, by portfolio segment, an aging analysis and the recorded investment in loans and leases past due as of December 31, 2019 and 2018:

Aging Analysis of Past Due Loans
As of December 31, 2019

(In thousands)	30–59 Days Past Due	60–89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans Receivable
Real estate	$ -	$ -	$ -	$ -	$ 149,016	$ 149,016
Commercial	100	-	-	100	51,016	51,116
Consumer	-	-	-	-	2,455	2,455
SBA	595	-	353	948	39,872	40,820
Accounts receivable	-	-	-	-	20,221	20,221
Leasing	-	-	-	-	-	-
Advanced restaurant financing	-	-	-	-	1,310	1,310
Overdrafts	-	-	-	-	1,404	1,404
Total	$ 695	$ -	$ 353	$ 1,048	$ 265,294	$ 266,342

Aging Analysis of Past Due Loans
As of December 31, 2018

(In thousands)	30–59 Days Past Due	60–89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans Receivable
Real estate	$ -	$ -	$ -	$ -	$ 151,567	$ 151,567
Commercial	-	-	-	-	38,067	38,067
Consumer	-	-	-	-	2,486	2,486
SBA	50	-	-	50	35,435	35,485
Accounts receivable	-	-	-	-	15,809	15,809
Leasing	-	-	-	-	65	65
Advanced restaurant financing	-	-	-	-	-	-
Overdrafts	-	-	-	-	29	29
Total	$ 50	$ -	$ -	$ 50	$ 243,458	$ 243,508

There were no loans that were greater than ninety days past due and still accruing interest at December 31, 2019 and 2018. The recorded investment in loans and leases on nonaccrual status as of December 31, 2019, consisted of $530,000 in SBA loans. The recorded investment in loans and leases on nonaccrual status as of December 31, 2018, consisted of $376,000 in real estate loans and $1,494,000 in SBA loans.

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Note 3 – Loans and Allowance for Loan Losses (continued)

The following tables present information related to impaired loans as of and for the years ended December 31, 2019 and 2018. There were no impaired loans that were fully reserved with an allowance for loan loss for the years ended December 31, 2019 and December 31, 2018:

Impaired Loans
For the Year Ended December 31, 2019

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Real estate	$ 437	$ 437	$ -	$ 390	$ 21
Commercial	181	181	-	91	12
SBA	1,126	1,126	-	974	310
Consumer	-	-	-	-	-
Accounts receivable	-	-	-	-	-
With an allowance recorded:					
Real estate	$ -	$ -	$ 1	$ 29	$ -
Commercial	1,052	1,052	83	1,205	62
SBA	-	-	-	-	-
Consumer	-	-	-	-	-
Accounts receivable	-	-	-	-	-
Total:					
Real estate	$ 437	$ 437	$ 1	$ 419	$ 21
Commercial	1,233	1,233	83	1,296	74
SBA	1,126	1,126	-	974	310
Consumer	-	-	-	-	-
Accounts receivable	-	-	-	-	-

Note 3 – Loans and Allowance for Loan Losses (continued)

	Impaired Loans For the Year Ended December 31, 2018				
(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Real estate	$ 376	$ 376	$ -	$ 567	$ 22
Commercial	-	-	-	48	-
SBA	821	821	-	932	128
Consumer	-	-	-	-	-
Accounts receivable	-	-	-	151	-
With an allowance recorded:					
Real estate	$ 58	$ 58	$ 2	$ 281	$ 8
Commercial	1,359	1,359	47	679	35
SBA	-	-	-	-	-
Consumer	-	-	-	-	-
Accounts receivable	-	-	-	-	-
Total:					
Real estate	$ 434	$ 434	$ 2	$ 848	$ 30
Commercial	1,359	1,359	47	727	35
SBA	821	821	-	932	128
Consumer	-	-	-	-	-
Accounts receivable	-	-	-	151	-

Troubled debt restructurings – The Company offers a variety of modifications to borrowers. The modification categories offered can generally be described in the following categories:

Rate modification – A modification in which the interest rate is changed.

Term modification – A modification in which the maturity date, timing of payments, or frequency of payments is changed.

Interest only modification – A modification in which the loan is converted to interest only payments for a period of time.

Payment modification – A modification in which the dollar amount of the payment is changed, other than an interest only modification described above.

Combination modification – Any other type of modification, including the use of multiple categories above.

Note 3 – Loans and Allowance for Loan Losses (continued)

As of December 31, 2019, there were two restructured loans in the amount of $586,000 with no allocated allowance included within the impaired loan balance as of December 31, 2019.

As of December 31, 2018, there was one restructured loan in the amount of $376,000 with no allocated allowance included within the impaired loan balance as of December 31, 2018.

There was one newly restructured loan that met the definition of a troubled debt restructuring during the years ended December 31, 2019 and 2018, respectively.

Loans held for sale – There were no loans held for sale and $4,697,000 at December 31, 2019 and 2018, respectively. Loans held for sale for the secondary market are carried at lower of aggregate cost or fair market value. Net unrealized losses, if any, are recorded as a valuation allowance and are charged against earnings through gain/loss on sale of loans. Loans designated as held for sale consist primarily of SBA loans.

The valuation allowance on loans held for sale was $0 and $1,344,000 at December 31, 2019 and 2018, respectively. During the year ended December 31, 2018, a valuation allowance was placed on one commercial real estate 2nd trust deed loan in the amount of $1,022,000. A valuation allowance was established as the loan migrated to nonaccrual status and was subsequently placed into liquidation. The full amount of the loan was subsequently charged off. During the year ended December 31, 2019, the Company received a net recovery on this loan in the amount of $810,000 which was recorded in gain on sale of loans in the consolidated statements of income.

SBA loans are generally sold with servicing rights retained. The carrying value of SBA loans sold is reduced by the proportional amount of deferred costs, if any, when applicable. Gains and losses on sale of SBA loans are based on the difference between the selling price and the carrying value of the related loans sold.

Note 4 – Premises and Equipment

Premises and equipment as of December 31, 2019 and 2018, are summarized as follows:

(In thousands)	2019	2018
Building improvements	$ 1,521	$ 1,508
Furniture, fixtures, and equipment	2,547	2,498
	4,068	4,006
Less accumulated depreciation and amortization	(3,771)	(3,720)
	$ 297	$ 286

Depreciation and amortization expense for the years ended December 31, 2019 and 2018, amounted to $142,000 and $112,000, respectively.

Note 5 – Servicing Assets

Activity for servicing assets and the related changes in fair value for the years ended December 31, 2019 and 2018, is as follows:

(In thousands)	2019	2018
Beginning balance	$ 1,442	$ 1,455
Additions, net	(404)	178
Changes in fair value	(30)	(191)
Ending balance	$ 1,008	$ 1,442

Loans serviced for others, consisting solely of SBA loans, are not included in the consolidated statements of financial condition. The unpaid principal balances of these loans serviced for others were $100,113,000 and $110,468,000 as of December 31, 2019 and 2018, respectively. Net servicing fees totaled $216,000 and $226,000 for the years ended December 31, 2019 and 2018, respectively.

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Notes to Consolidated Financial Statements

Note 6 – Deposits

At December 31, 2019, the scheduled maturities of time deposits are as follows:

(In thousands) Matures During Year Ending December 31,	Time Deposits Under $250,000	Time Deposits $250,000 and Over
2020	$ 4,912	$ 14,010
2021	527	382
2022	303	-
2023	33	-
2024	23	-
	$ 5,798	$ 14,392

Note 7 – Borrowings

On May 1, 2017, the Company entered into three unsecured term notes for $1,750,000 with a maturity date of May 1, 2022, bearing interest at a rate of 5.00% with interest only paid semi-annually and principal due at maturity. At December 31, 2019 and 2018, the outstanding balance of these notes was $1,750,000 and interest paid on these notes was $88,000 for both the years ended December 31, 2019 and 2018.

On August 1, 2017, the Company entered into an unsecured note agreement for $8,586,000 with a maturity date of August 14, 2022, and bears interest at a rate of 5.23%. At December 31, 2019 and 2018, the outstanding balance on this note was $4,942,000 and $8,586,000, respectively, and interest paid was $324,000 and $455,000 for the years ended December 31, 2019 and 2018, respectively.

The following is a summary of principal maturities for the next five years and thereafter:

Fiscal Years	
2020	$ 858,600
2021	858,600
2022	4,974,850
2023	-
Total	$ 6,692,050

Note 7 – Borrowings (continued)

The Company has a line of credit available from the FHLB, which is secured by pledged loans. Borrowings may include overnight advances as well as loans with terms of up to 30 years. There were no outstanding borrowings at December 31, 2019 and 2018. The Company had $114,209,000 and $82,693,000 of borrowing capacity from the FHLB at December 31, 2019 and 2018, respectively, based upon loans available to be pledged. The carrying value of loans pledged to the FHLB as collateral was $231,527,000 at December 31, 2019. The Company had $2,336,000 and $3,115,000 of borrowing capacity from the Federal Reserve Bank of San Francisco (“FRB”) as of December 31, 2019 and 2018, respectively, based upon loans available to be pledged. The carrying balance of loans pledged to the FRB as collateral was $2,957,000 at December 31, 2019.

The Company has an unsecured revolving line of credit with PCBB providing for federal fund purchases up to $8,200,000 and $8,000,000 with Zions Bank at December 31, 2019 and 2018, respectively. Borrowings are payable on demand and interest on outstanding borrowings accrues at rates negotiated at the time of the borrowing. As of December 31, 2019 and 2018, the Company did not have an outstanding balance against these lines of credits.

Note 8 – Junior Subordinated Deferrable Interest Debentures

The Mission Valley Statutory Trust I (the “Trust”) was formed by the Company for the sole purpose of issuing trust preferred securities fully and unconditionally guaranteed by the Company. For financial reporting purposes, the Trust is not consolidated and the fixed rate junior subordinated deferrable interest debentures held by the Trust, issued and guaranteed by the Company, are reflected in borrowings within the Company’s consolidated statements of financial condition.

On September 16, 2005, the Trust issued $6,000,000 fixed rate Capital Trust Pass-Through Securities (“TRUPS”) with a liquidation value of $1,000 per security for gross proceeds of $6,000,000. The entire proceeds of the issuance were invested by the Trust in $6,186,000 of junior subordinated deferrable interest debentures issued by the Company with identical maturity, repricing, and payment terms as the TRUPS. These debentures represent the sole assets of the Trust and mature on December 15, 2035, and bore interest at 5.97% through September 15, 2010, and variable rate equal to 3-month LIBOR plus 1.50% from September 15, 2010 through maturity. Interest payments are due on a quarterly basis. The interest is deferrable at the Company’s option for a period of up to twenty consecutive quarterly periods but in any event not beyond September 16, 2035.

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Note 9 – Derivative Instrument and Hedge Activity

During the year ended December 31, 2018, the Company entered into an interest rate swap agreement with a counterparty to manage interest rate risk associated with its variable rate borrowings on the TRUPS. The interest rate swap is designated as a cash flow hedge with the aggregate fair value of the swap recorded in other assets or other liabilities with changes in fair value of the hedge accounted for within the statement of comprehensive income, net of taxes, to the extent effective. The amount included in accumulated other comprehensive income would be reclassified to current interest incurred from the hedged variable rate borrowings on the TRUPS when it affects earnings. The Company assesses the effectiveness of the hedging relationship by comparing the changes in fair value of the derivative hedging instrument with the changes in fair value of the designated hedged transaction. The Company expects the hedge to remain highly effective during the remaining terms of the swap and did not recognize any hedge ineffectiveness in current earnings during the year ended December 31, 2019. The notional amount of the swap agreement is $6,000,000 with a variable interest rate of 3-month LIBOR plus 1.50% maturing on December 15, 2035. The fixed rate paid on the instrument was 3.27% at December 31, 2019. The fair value of the swap is approximately $1,076,000 and $395,000 and is recorded in accrued interest payable and other liabilities at December 31, 2019 and 2018, respectively. The Company did not record any ineffectiveness on the cash flow hedge within the consolidated statements of income for the year ended December 31, 2019 or 2018.

Note 10 – Income Taxes

The provision for income taxes for years ended December 31, 2019 and 2018, consisted of the following:

(In thousands)	2019	2018
Current		
Federal	$ 1,165	$ 787
State	587	560
	1,752	1,347
Deferred		
Federal	(276)	(206)
State	(63)	(246)
	(339)	(452)
	$ 1,413	$ 895

Note 10 – Income Taxes (continued)

A reconciliation of the Company's effective tax rate with the statutory federal income tax rate for years ended December 31, 2019 and 2018, is as follows:

(In thousands)	2019		2018	
Statutory federal income tax rate	$ 1,053	21.0 %	$ 851	21.0 %
State franchise tax, net of federal benefit	430	8.6	295	7.3
Stock compensation	(8)	(0.2)	19	0.5
Tax exempt interest	(6)	(0.1)	(16)	(2.0)
BOLI	(82)	(1.6)	(80)	(0.4)
Other	26	0.5	(174)	(4.3)
	$ 1,413	28.2 %	$ 895	22.1 %

The following is a summary of the components of the net deferred tax asset at December 31, 2019 and 2018:

(In thousands)	2019	2018
Deferred tax assets:		
Allowance for loan losses	$ 778	$ 612
Lease liability	320	-
State tax	123	118
Unrealized loss on investment securities	310	100
Non-accrual interest	50	30
Deferred compensation	910	808
Other, net	-	-
Total deferred tax assets	2,491	1,668
Deferred tax liabilities:		
Loan origination costs	(573)	(601)
Right of use asset	(320)	-
Depreciation and amortization	(60)	(68)
Certain prepaid assets	(113)	(123)
Total deferred tax liabilities	(1,066)	(792)
Net deferred tax asset	$ 1,425	$ 876

Management believes, based upon the Company's historical performance and future projections, it is more-likely-than-not the deferred tax asset will be realized in the normal course of operations and has determined that no valuation allowance is necessary as of December 31, 2019 and 2018, respectively.

Note 10 – Income Taxes (continued)

The Company recognizes the tax benefit from uncertain tax positions only if it is more-likely-than-not that the tax positions will be sustained on examination by the tax authorities, based on the technical merits of the position. The tax benefit is measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement.

The Company recognizes interest and penalties related to income tax matters in other operating expenses in the statements of operations. The Company does not anticipate that the amount of unrecognized tax benefits will significantly increase or decrease in the next twelve months. There were no interest and penalties accrued for the years ended December 31, 2019 and 2018. The Company files income tax returns in the U.S. federal jurisdiction and in California.

Note 11 – Employee Benefit Plans

The Company has established a 401(k) Plan for the benefit of eligible employees, whereby each employee being at least twenty-one years of age may become a participant at specified intervals. Employees may contribute up to 50% of their annual compensation to the 401(k) Plan each year subject to certain limits based on federal tax laws. The Company may elect to make some level of matching contributions to the plan at the discretion of the Board of Directors. Matching contributions of $147,000 and $135,000 were made for the years ended December 31, 2019 and 2018, respectively.

The Company sponsors a supplemental executive retirement plan (SERP), which is a nonqualified unfunded pension plan covering a select group of executives. The plan provides a retirement benefit payable in the form of a life annuity to the participants, which is based on a specified dollar amount as stated in the agreements. The accrued postretirement benefit balance was $2,511,000 and $2,230,000 at December 31, 2019 and 2018, respectively, and is reported in accrued interest payable and other liabilities within the consolidated statements of financial condition. The postretirement benefit expense reported within salaries, wages, and employee benefits in the consolidated statements of income was $421,000 and $594,000 for the years ended December 31, 2019 and 2018, respectively.

Note 12 – Share-Based Compensation

The Company approved the 2017 Omnibus Stock Equity Plan (the "Plan"), voted into effect by the majority of shares represented at its May 23, 2017 Annual Shareholders' Meeting and set to expire March 28, 2027. Under the Plan, directors and key employees receive long-term incentives ("Awards") in the form of incentive and nonqualified stock options and restricted stock. The Plan is administered by the Board of Directors, or a committee to be appointed by the Board, who will select the directors and key executives to receive options or Awards, the form of those Awards, the number of shares or dollar targets, and all terms and conditions. The Plan provides for terms with respect to accelerated vesting should a change in control occur.

Note 12 – Share-Based Compensation (continued)

Stock options expire no later than ten years from the date of grant. Stock options granted to an optionee who owns stock representing more than ten percent of the voting power of all classes of stock of the Company shall expire not more than five years from the date of grant.

	2019		2018	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
(In thousands)				
Outstanding at beginning of year	49,250	$ 15.90	-	$ -
Exercised	-	-	-	-
Granted	59,578	14.05	49,250	15.90
Expired or forfeited	(24,509)	15.57	-	-
Outstanding at end of year	84,319	$ 14.69	49,250	$ 15.90
Options exercisable	9,653	$ 15.90	-	$ -
Weighted average remaining contractual life of options outstanding	9.0 years		9.5 years	

No stock options were exercised during 2019 and 2018. As of December 31, 2019, there was $284,000 of total unrecognized compensation cost related to nonvested stock options granted under the Plan. The cost is expected to be recognized over a weighted-average remaining period of 2.3 years. Composition cost associated with the fair value of stock options that vested in 2019 and 2018 was $109,000 and $64,000, respectively. The aggregate intrinsic value of the options exercisable plus options expected to vest in the future years is $0 based on a stock price of $14.35 and $14.00 per share for the years ended December 31, 2019 and 2018, respectively.

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model using the assumptions shown in the following table. The expected volatility was based on the volatility of the Company's stock price over a period commensurate with the expected term of the option. The Company uses historical data on option exercises to determine the expected term within the valuation model.

	2019	2018
Risk free interest rate	1.85%–2.58%	2.96%
Weighted-average expected life	6 years	6 years
Volatility	31.1%–31.6%	32.2%
Dividends	None	None

The weighted-average fair value of options granted during the year ended December 31, 2019 and 2018, was $4.82 and $5.88, respectively.

Note 12 – Share-Based Compensation (continued)

The maximum number of shares available for all Awards under the 2017 Plan is up to 600,000 shares of the Bank's common stock. No more than 250,000 shares may be issued pursuant to Awards of restricted stock, and no more than 500,000 shares, may be issued pursuant to Awards of incentive stock options; provided, however, that in no event may the total of all the restricted stock awards, incentive stock options, and nonqualified stock options granted under the 2018 Plan exceed 600,000. Restricted stock awards are ineligible to received stock dividends during the period in which they are unvested.

During the year ended December 31, 2018, 16,750 restricted stock awards were issued at a price of $15.95 per share. During the year ended December 31, 2019, 4,000 shares were forfeited resulting in 12,750 remaining in restricted stock awards. As of December 31, 2019, there was $96,000 of total unrecognized compensation cost related to nonvested restricted stock awards granted related to this issuance. The cost is expected to be recognized over a weighted-average remaining period of 1.4 years.

During the year ended December 31, 2019, 37,500 restricted stock awards were issued at a price of $14.12 per share. As of December 31, 2019, there was $441,000 of total unrecognized compensation cost related to nonvested restricted stock awards granted related to this issuance. The cost is expected to be recognized over a weighted-average remaining period of 2.5 years.

At December 31, 2019, 25,000 stock awards were fully vested, and there were 50,250 unvested restricted stock awards under the 2017 equity plan. Compensation expense related to the grant of restricted stock for the years ended December 31, 2019 and 2018, totaled $180,000 and $137,000, respectively. Restricted stock awards are ineligible to received stock dividends during the period in which they are unvested. As of December 31, 2019, there was $284,000 of total unrecognized compensation cost related to nonvested restricted stock awards granted under the plan. The cost is expected to be recognized over a weighted-average remaining period of 2.5 years.

At December 31, 2019, there were 199,750 shares of restricted stock awards available for future grant. At December 31, 2019, there were 265,281 shares of incentive stock options and of qualified stock options available for future grant.

Note 13 – Leases

The Company currently has operating leases for its administrative offices and branches. The right-of-use asset and operating lease liability are recorded in fixed assets and other liabilities, respectively, in the consolidated statements of financial condition.

Note 13 – Leases (continued)

The ROU asset represents our right to use an underlying asset during the lease term. Operating lease liabilities represent our obligation to make lease payments arising from the lease. ROU assets and operating lease liabilities are recognized based on the present value of the remaining lease payments using a discount rate that represents our incremental borrowing rate at the date of implementation of the new accounting standard. These operating leases call for various monthly payments and expire in the years ranging from 2020 to 2023. All of the operating leases are currently in their final option periods. As such, the Company's measurement of the operating lease liability and right-of-use asset does not extend beyond the option term renewal since it is not reasonably certain that the Company knows what the renewal terms, if offered, will be or if alternative locations from a strategic standpoint will be undertaken. Short-term leases (initial term of less than 12 months) are not recorded on the balance sheet and lease expense is recognized on a straight-line basis over the lease term. The Company has no material finance leases.

The Company recorded an initial $1.4 million ROU asset and operating lease liability at January 1, 2019.

The Company recorded lease expense of $447,000 and $339,000 for the years ended December 31, 2019 and 2018, respectively.

Additional information regarding our operating leases is summarized below for the year ended December 31, 2019:

Cash paid for amounts included in the measurement of lease liabilites for operating leases	$	447,000
ROU assets obtained in exchange for lease liabilities	$	1,082
Weighted average remaining lease term in months		40
Weighted average discount rate		4.23 %

The following table shows future minimum payments under operating leases with terms in excess of year as of December 31, 2019:

Year Ending December 31 *(in thousands),*		
2020	$	408
2021		294
2022		297
2023		180
Thereafter		-
Total undiscounted lease payments		1,179
Less: interest		(93)
Present value of lease liabilities	$	1,086

Note 14 – Commitments and Contingencies

The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit. These instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized on the statements of financial condition. To mitigate this risk posed by these off-balance-sheet exposures, the Company has established an off-balance-sheet reserve totaling $9,000 and $25,000 as of December 31, 2019 and 2018, respectively, included in accrued interest payable and other liabilities on the statements of financial condition.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those guarantees are preliminarily issued to support public and private borrowing arrangements, including commercial paper, bond financing, and similar transactions. All standby letters of credit issued by the Company expire within one year of issuance.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation.

Collateral held varies but may include receivables, inventory, property, plant, and equipment, residential properties, and income-producing commercial properties.

A summary of the contractual or notional amounts of the Company's significant off-balance-sheet financial instruments as of December 31, 2019 and 2018, is as follows:

(In thousands)	2019		2018	
Commitments to extend credit	$	28,628	$	28,329
Standby letters of credit		1,085		1,224
	$	29,713	$	29,553

Litigation – In the ordinary course of business, the Company becomes involved in litigation. Management believes, based upon opinions of legal counsel, that the disposition of all suits pending against the Company will not have a material adverse effect on its financial position or results of operations.

Note 15 – Transactions with Related Parties

In the ordinary course of business, the Company enters into transactions with certain directors, officers, and shareholders, and certain affiliates of the Company.

As part of its normal banking activities, the Company has extended credit to and received deposits from certain members of its Board of Directors, major shareholders, and officers, as well as entities with which these individuals are associated. These related parties had deposits at the Company totaling approximately $35,048,000 and $31,986,000 at December 31, 2019 and 2018, respectively. There was one related party loan in the amount of $657,000 at December 31, 2019, and none at December 31, 2018. Management believes these transactions were made in the ordinary course of business on substantially the same terms and conditions, including interest rates and collateral requirements, as comparable loans and deposits with other customers, and the loans did not involve more than normal credit risk or present other unfavorable features.

Note 16 – Fair Value of Financial Instruments

Fair value measurements within the ASC defines fair value, establishes a framework for measuring fair value under U.S. GAAP, and expands disclosures about fair value measurement. Fair value measurements apply to all financial assets and liabilities that are being measured and reported at fair value on a recurring and non-recurring basis.

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.

A three-level hierarchy is used for disclosure of assets and liabilities recorded at fair value. The classification of assets and liabilities within the hierarchy is based on whether the inputs to the valuation methodology used for measurement are observable or unobservable. Observable inputs reflect market-derived or market-based information obtained from independent sources, while unobservable inputs reflect our estimates about market data.

Note 16 – Fair Value of Financial Instruments (continued)

In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) for identical instruments that are highly liquid, observable, and actively traded in over-the-counter markets. Fair values determined by Level 2 inputs utilize inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-derived valuations whose inputs are observable and can be corroborated by market data. Level 3 inputs are unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

The following tables present information about the Company's assets and liabilities measured at fair value on a recurring and non-recurring basis as of December 31, 2019 and 2018, and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value. In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) for identical instruments that are highly liquid, observable, and actively traded in over-the-counter markets.

	December 31, 2019			
(In thousands)	Total	Level 1	Level 2	Level 3
Recurring Items				
Financial assets				
Securities available-for-sale				
Mortgage backed securities	$ 14,163	$ 14,163	$ -	$ -
Corporate bonds	3,079	3,079	-	-
Municipal investments	-	-	-	-
Other	788	788	-	-
Servicing assets	1,008	-	-	1,008
Financial liabilities				
Derivative liability	1,076	-	-	1,076
Nonrecurring Items				
Impaired loans	2,764	-	-	2,764

	December 31, 2018			
(In thousands)	Total	Level 1	Level 2	Level 3
Recurring Items				
Financial assets				
Securities available-for-sale				
Mortgage backed securities	$ 10,928	$ 10,928	$ -	$ -
Corporate bonds	-	-	-	-
Municipal investments	387	387	-	-
Other	765	765	-	-
Servicing assets	1,442	-	-	1,442
Financial liabilities				
Derivative liability	395	-	-	395
Nonrecurring Items				
Impaired loans	2,614	-	-	2,614

Note 16 – Fair Value of Financial Instruments (continued)

The following table presents additional information about the unobservable inputs used in the fair value measurements on a recurring basis that were categorized within Level 3 of the fair value hierarchy as of December 31, 2019:

Financial Instrument	Valuation Technique	Unobservable Inputs	Range of Inputs	Weighted Average Input	Impact to Valuation from an Increased or Higher Input Value
Servicing assets	Discounted cash flow	Prepayment speeds	11.13% – 23.61%	19.81%	Decrease
		Discount rate	9.07% – 25.42%	11.64%	Decrease
		Expected weighted average on loan	4.25% – 8.25%	3.76 years	Increase

Securities available-for-sale – The table above presents the balance of securities available-for-sale, which is measured at fair value on a recurring basis. An independent third party performs market valuations of the Company's securities available-for-sale. The fair values are determined by using several sources for valuing securities. The techniques include pricing models that vary based on the type of asset being valued and incorporate available trade, bid, and other market information. Market valuation sources include observable market inputs and are therefore considered Level 2 inputs for purposes of determining the fair values.

Servicing assets – Fair value is based on a loan-by-loan basis, taking into consideration the original term to maturity, the current age of the loan, and the remaining term to maturity. The valuation methodology utilized for the servicing assets begins with generating future cash flows for each servicing asset, based on their unique characteristics and market-based assumptions for prepayment speeds. The present value of the future cash flows is then calculated utilizing market-based discount rate assumptions.

Derivative instruments – Interest rate swaps are valued by a third party, using models that primarily use market observable inputs, such as yield curves, and are validated by comparison with valuations provided by the respective counterparties. Derivative financial instruments are included in other assets and other liabilities in the consolidated statements of financial condition.

Impaired loans and other real estate owned – The loan balance shown in the table above represents all of the Company's impaired loans for which impairment was recognized during the period. These loans are measured at fair value on a non-recurring basis. Impaired loans that are collateral-dependent are measured based on the fair value of their collateral while non-collateral-dependent loans are measured on a discounted cash flow basis. The fair value of each loan's collateral is generally based on estimated market prices from an independently prepared appraisal, which is then adjusted for the cost related to liquidating such collateral. The estimated fair value of other real estate owned is based on the appraised values or other information for the estimated fair values of such assets. We generally use an 8–10% discount for selling costs which is applied to all properties, regardless of size. Appraised values may be adjusted to reflect changes in market conditions that have occurred subsequent to the appraisal date or for revised estimates regarding the timing or cost of the property sale. These adjustments are based on qualitative judgments made by management on a case-by-case basis. There have been no significant changes in the valuation techniques during the period ended December 31, 2019.

Note 16 – Fair Value of Financial Instruments (continued)

The following tables present information about the level in the fair value hierarchy for the Company's assets and liabilities that are not measured at fair value as of December 31, 2019 and 2018. The valuation of loans receivable held for investment was impacted by the adoption of ASU 2016-01. In accordance with ASU 2016-01, the fair value of loans held for investment is estimated using discounted cash flow analyses. The discount rates used to determine fair value use interest rate spreads that reflect factors such as liquidity, credit, and nonperformance risk of the loans. Loans are considered a Level 3 classification.

Transfers between levels of the fair value hierarchy are recognized on the actual date of the events or circumstances that caused the transfer, which generally corresponds to the Company's quarterly valuation process. During the years ended December 31, 2019 and 2018, there were no transfers between levels of the fair value hierarchy.

	2019				
			Fair Value Measurements Using		
(In thousands)	Carrying Value	Estimated Fair Value	Level 1	Level 2	Level 3
Financial assets					
Cash and cash equivalents	$ 52,202	$ 52,202	$ 52,202	$ -	$ -
Interest bearing deposit in other banks	5,469	5,450	-	5,450	-
Investment securities, held-to-maturity	1	1	-	1	-
Loans, net	262,764	265,718	-	-	265,718
Loans, held for sale	-	-	-	-	-
Bank owned life insurance	10,302	10,302	10,302	-	-
Restricted equity securities	1,921	1,921	1,921	-	-
Accrued interest receivable	972	972	972	-	-
Financial liabilities					
Deposits	$ 301,166	$ 278,805	$ -	$ -	$ 278,805
Subordinated debentures	6,186	4,983	-	-	6,186
Notes payable	6,692	6,692	-	-	-
Accrued interest payable	2	2	2	-	-

	2018				
			Fair Value Measurements Using		
(In thousands)	Carrying Value	Estimated Fair Value	Level 1	Level 2	Level 3
Financial assets					
Cash and cash equivalents	$ 74,335	$ 74,335	$ 74,335	$ -	$ -
Interest bearing deposit in other banks	4,294	4,294	-	4,294	-
Investment securities, held-to-maturity	17	17	-	17	-
Loans, net	239,206	239,206	-	-	235,191
Loans, held for sale	4,697	4,697	-	4,697	-
Bank owned life insurance	10,024	10,024	10,024	-	-
Restricted equity securities	1,889	1,889	1,889	-	-
Accrued interest receivable	836	836	836	-	-
Financial liabilities					
Deposits	$ 296,740	$ 274,762	$ -	$ -	$ 274,762
Subordinated debentures	6,186	6,186	-	-	4,933
Notes payable	10,336	10,336	-	-	10,065
Accrued interest payable	4	4	4	-	-

Note 17 – Regulatory Matters

The Company and the Bank are 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 Company's and the Bank's financial statements. Under capital adequacy guidelines, the Company and the Bank must meet specific capital adequacy guidelines that involve quantitative measures of the Company's and the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Company's and the Bank's capital classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the following table) of Tier 1 capital (as defined in the regulations) to total average assets (as defined) and minimum ratios of Tier 1, common equity Tier 1 and total capital (as defined) to risk-weighted assets (as defined). Management believes, as of December 31, 2019 and 2018, that the Company and the Bank meets all capital requirements to which it is subject.

The Bank has been notified by its regulator that, as of its most recent regulatory examination, the Bank is regarded as "well capitalized" under the regulatory framework for prompt corrective action. Such determination has been made based on the Bank's Tier 1, common equity Tier 1, total capital, and leverage ratios. There have been no conditions or events since this notification that management believes would change the Bank's categorization as well capitalized under the ratios listed below.

The Company's and the Bank's actual and required capital amounts and ratios are (dollars in thousands):

Mission Valley Bancorp	Actual		Amount of Capital Required: Minimum Capital Requirement		Amount of Capital Required: Minimum to Be Well-Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						
As of December 31, 2019						
Total capital ratio	$ 47,147	16.00%	$ 23,503	8.00%	$ 29,379	10.00%
Tier 1 capital ratio	43,473	14.80%	17,628	6.00%	23,503	8.00%
Tier 1 leverage ratio	47,147	12.10%	14,339	4.00%	17,924	5.00%
Common equity Tier 1 capital ratio	37,473	12.80%	13,221	4.50%	19,097	6.50%
As of December 31, 2018						
Total capital ratio	$ 43,444	15.20%	$ 22,872	8.00%	$ 28,591	10.00%
Tier 1 capital ratio	39,867	13.90%	17,154	6.00%	22,872	8.00%
Tier 1 leverage ratio	39,867	12.10%	13,223	4.00%	16,528	5.00%
Common equity Tier 1 capital ratio	33,268	11.80%	12,866	4.50%	18,584	6.50%

Note 17 – Regulatory Matters (continued)

Mission Valley Bank	Actual		Amount of Capital Required: Minimum Capital Requirement		Amount of Capital Required: Minimum to Be Well-Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						
As of December 31, 2019						
Total capital ratio	$ 45,437	15.52%	$ 23,414	8.00%	$ 29,268	10.00%
Tier 1 capital ratio	41,778	14.27%	17,561	6.00%	23,414	8.00%
Tier 1 leverage ratio	45,437	11.74%	14,231	4.00%	17,789	5.00%
Common equity Tier 1 capital ratio	41,778	14.27%	13,170	4.50%	19,024	6.50%
As of December 31, 2018						
Total capital ratio	$ 51,116	17.89%	$ 22,863	8.00%	$ 25,579	10.00%
Tier 1 capital ratio	47,541	16.64%	17,147	6.00%	22,863	8.00%
Tier 1 leverage ratio	47,541	14.43%	13,180	4.00%	16,475	5.00%
Common equity Tier 1 capital ratio	47,541	16.64%	12,860	4.50%	18,576	6.50%

The Bank is required to establish and phase-in a "conservation buffer," consisting of a common equity Tier 1 capital amount equal to 2.5% of risk-weighted assets by 2019. As of December 31, 2019, the "conservation buffer" amount was 2.5% and fully phased-in. An institution that does not meet the conservation buffer requirement will be subject to restrictions on certain activities including payment of dividends, stock repurchases, and discretionary bonuses to executive officers. The phase-in began in 2016 and increases until fully phased-in by 2019.

The difference in common equity Tier 1 capital ratio between Mission Valley Bancorp and Mission Valley Bank is due to the TRUPS securities disclosed in Note 8.

Note 18 – Revenue from Contracts with Customers

As noted in Note 1, the Company adopted the provisions of ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, on January 1, 2018, and all subsequent ASUs that modified Topic 606. Results for reporting periods beginning after December 31, 2017, are presented under Topic 606, while prior period amounts have not been adjusted and continue to be reported in accordance with Topic 605.

All of the Company's revenue from contracts with customers in the scope of ASC 606 is recognized in non-interest income. Gains/losses on the sale of other real estate owned are included in non-interest expense and are generally recognized when the performance obligation is completed. This is typically at delivery of control over the property to the buyer at time of each real estate closing. There was no gain/loss activity related to other real estate owned during 2018.

Note 18 – Revenue from Contracts with Customers (continued)

The following table presents the Company's sources of non-interest income for the twelve months ended December 31:

(In thousands)	2019	2018
Non-interest income		
Service charges and other income	$ 1,858	$ 1,740
Gain (loss) on sale of loans	978	(386)
Net merchant income	569	548
Increase in cash surrender value of bank owned life insurance	278	271
Other income	505	511
Total non-interest income	$ 4,188	$ 2,684

Deposit service charges – The Company earns fees from its deposit customers for account maintenance, transaction-based activity, and overdraft services. Account maintenance fees consist primarily of account fees and analyzed account fees charged on deposit accounts on a monthly basis. The performance obligation is satisfied and the fees are recognized on a monthly basis as the service period is completed. Transaction-based fees on deposit accounts are charged to deposit customers for specific services provided to the customer, such as non-sufficient funds fees, overdraft fees, and wire fees. The performance obligation is completed as the transaction occurs and the fees are recognized at the time each specific service is provided to the customer.

Debit and ATM interchange fee income and expenses – Debit and ATM interchange income represent fees earned when a debit card issued by the Company is used. The Company earns interchange fees from debit cardholder transactions through the Visa payment network. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, concurrently with the transaction processing services provided to the cardholder. The performance obligation is satisfied and the fees are earned when the cost of the transaction is charged to the cardholders' debit card. Certain expenses directly associated with the credit and debit card are recorded on a net basis with the interchange income.

Merchant fee income – Merchant fee income represents fees earned by the Company for card payment services provided to its merchant customers. The Company has a contract with a third party to provide card payment services to merchants that contract for those services. The third-party provider passes the payments made by the merchants through to the Company. The Company, in turn, pays the third-party provider for the services it provides to the merchants. These payments to the third party-provider are recorded as expenses as a net reduction against fee income. In addition, a portion of the payment received represents interchange fees which are passed through to the card issuing bank. Income is primarily earned based on the dollar volume and number of transactions processed. The performance obligation is satisfied and the related fee is earned when each payment is accepted by the processing network.

Note 18 – Revenue from Contracts with Customers (continued)

Credit card and interchange income and expenses – Credit card interchange income represent fees earned when a credit card issued by the Company is used. Similar to the debit card interchange, the Company earns an interchange fee for each transaction made with the Company's branded credit cards. The performance obligation is satisfied and the fees are earned when the cost of the transaction is charged to the cardholders' credit card. Certain expenses and rebates directly related to the credit card interchange contract are recorded net to the interchange income.

Note 19 – Subsequent Events

Subsequent to year end, the World Health Organization declared the spread of Coronavirus Disease ("COVID-19") a worldwide pandemic. The COVID-19 pandemic is having significant effects on global markets, supply chains, businesses, and communities. Specific to the Company, COVID-19 may impact various parts of its 2020 operations and financial results including but not limited to additional loan loss reserves, costs for emergency preparedness, or potential shortages of personnel. Management believes the Company is taking appropriate actions to mitigate the negative impact. However, the full impact of COVID-19 is unknown and cannot be reasonably estimated as these events occurred subsequent to year end and are still developing.

The Company recognizes in the consolidated financial statements the effect of all subsequent events (transactions or events that occur after the balance sheet date but before the consolidated financial statements are issued) that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing the consolidated financial statements. The Company's consolidated financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date and before consolidated financial statements are available to be issued. The Company has evaluated subsequent events through March 31, 2020, which is the date the consolidated financial statements were available to be issued.

Board of Directors

Tamara Gurney
President, CEO & Director of
Mission Valley Bancorp & Bank

Kathleen Kellogg
Director of Mission Valley Bancorp & Bank
Ms. Kellogg is an experienced banking executive and director.

John Miller
Director of Mission Valley Bancorp & Bank
Mr. Miller is an Executive Officer & Co-Founder of Lexicon Bank in organization, as well as an investment advisory professional and community bank consultant.

Jerold B. Neuman, ESQ
Director of Mission Valley Bancorp & Bank
Mr. Neuman is a partner with the law firm of DLA Piper, LLP.

Ara Oghoorian, CFA, CFP®, CPA
Director of Mission Valley Bancorp & Bank
Mr. Oghoorian is the Founder & President of ACap Advisors & Accountants, LLC

John Parker
Director of Mission Valley Bancorp & Bank
Mr. Parker is the Executive Officer and Co-Founder of Parker Brown Inc.

Eric Sato, CPA
Director of Mission Valley Bancorp & Bank
Mr. Sato is a Partner in the Certified Public Accounting firm of Edwards & Sato, CPAs.

Earle S. Wasserman
Director and Chairman of the Board of
Mission Valley Bancorp & Bank
Mr. Wasserman is the Chairman of the Hallmark Group Inc.

Senior Management

Tamara Gurney
President
Chief Executive Officer

Jeffrey Watson
Chief Operating Officer

Daniel Epstein
Executive Vice President
Chief Credit Officer

Steve Choe
Senior Vice President
Regional Sales Manager

Anthony Chuan
Senior Vice President
Chief Financial Officer

Linda Rousseau
Executive Vice President
Chief Administrative Officer

Roy Fisher
Senior Vice President
Operations Administrator

Administrative Officers

Arturo Andrade
Vice President
Core Systems Manager

Paula Bahamon
Vice President
Community Development Officer

Carrie Burrell
Vice President, CFMP
Marketing Manager

Maria Gonzalez
Vice President
Central Operations Manager

Jean Grall
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Vice President
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Sandy Konish
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Christina Ahn
Vice President
SBA Portfolio Manager

Yolanda Ortiz
Vice President
Compliance & Risk Manager

Ryan Roques
Vice President
SBA Business Development Officer

Sun Valley Corporate Office

Griselda De Mel
Vice President
Relationship Manager

Lola Forbis
Vice President
Relationship Manager

Tony Rodriguez
Vice President
Operations Manager

Santa Clarita Valley Business Banking Center

Steve Nuñez
Vice President
Relationship Manager

Welmer Jurado
Vice President
Relationship Manager

Laura Soto
Assistant Vice President
Operations Manager

South Bay Loan Production Office

By Appointment Only
Call (877) 394-2306

Investor Information

Common Stock:

Effective July 23, 2014, Mission Valley Bancorp's stock began trading on the OTCQX market under the symbol "MVLY". As of December 31, 2019 there were 156 shareholders of record and 3,233,365 shares of common stock outstanding.

Stock Information:

D.A. Davidson & Co.
Community Bank & Wealth Management Group
Michael R. Natzic, CWS® | Senior Vice President, Branch Manager
Katy E. Ehlers, CWS® | Associate Vice President
(909) 584-4500 | (800) 288-2811
cbwm@dadco.com

Stock Transfer Agent:

Shareholders with inquiries regarding accounts, lost stock certificates or changes of address, may contact Lisa Mora, Corporate Secretary of Mission Valley Bancorp at (818) 394-2300 during regular business hours or Computershare at (800) 962-4284 24 hours a day.

Written correspondence may be sent to:

> Computershare
> 462 South 4th Street, Suite 1600
> Louisville, KY 40202

MISSION VALLEY BANCORP

2019 FINANCIAL STATEMENTS

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