RIVER VALLEY
COMMUNITY BANK

Yuba City, California

FINANCIAL STATEMENTS
December 31, 2016 and 2015

Contents

INDEPENDENT AUDITOR'S REPORT

The Shareholders and
Board of Directors
River Valley Community Bank
Yuba City, California

Report on the Financial Statements

We have audited the accompanying financial statements of River Valley Community Bank, which comprise the balance sheets as of December 31, 2016 and 2015 and the related statements of income and comprehensive income, shareholders' equity and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

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

Crowe Horwath LLP

Crowe Horwath LLP

Sacramento, California
March 21, 2017

River Valley Community Bank
Balance Sheets
December 31, 2016 and 2015

	2016	2015
Assets		
Cash and noninterest bearing due from banks	$ 5,000,598	$ 9,080,595
Interest bearing deposits in banks	29,183,249	12,653,723
Total cash and cash equivalents	34,183,847	21,734,318
Interest bearing deposits in banks	8,682,000	8,436,752
Investment securities available-for-sale (Notes 2 and 6)	143,632,968	92,916,694
Real estate loans:		
Construction and development	5,352,122	7,082,514
Agriculture	7,488,986	7,371,895
1-4 family residential	13,164,274	12,899,556
Multifamily	12,792,470	10,981,210
Commercial	67,652,399	53,993,974
Agriculture production loans	4,093,054	3,602,925
Commercial and industrial loans	14,118,441	10,533,294
Consumer loans	516,488	616,687
Total loans, gross (Notes 3, 6, 8, and 12)	125,178,234	107,082,055
Deferred loan fees, net	(142,404)	(107,823)
Allowance for loan losses (Note 3)	(1,926,456)	(1,801,804)
Total loans, net	123,109,374	105,172,428
Premises and equipment, net (Note 4)	2,029,201	2,076,889
Cash surrender value of life insurance	5,523,032	4,390,243
Accrued interest receivable and other assets (Notes 7 and 11)	4,028,174	2,567,650
Total assets	$ 321,188,596	$ 237,294,974
Liabilities and Shareholders' Equity		
Liabilities:		
Demand deposits - noninterest bearing	$ 87,231,418	$ 75,796,584
Demand deposits - interest bearing	36,825,025	32,602,525
Money market and savings deposits	108,932,293	93,718,398
Time deposits - under $250,000 (Note 5)	6,517,740	6,978,345
Time deposits - $250,000 or more (Note 5)	4,443,980	4,137,146
Total deposits	243,950,456	213,232,998
Federal Home Loan Bank borrowings (Note 6)	50,000,000	-
Accrued interest payable and other liabilities (Note 11)	1,937,584	629,195
Total liabilities	295,888,040	213,862,193
Commitments and contingencies (Note 8)		
Shareholders' equity (Notes 9 and 10):		
Preferred stock – no par value; 5,000,000 shares authorized; no shares outstanding	-	-
Common stock – no par value; 50,000,000 shares authorized; 2,386,596 and 2,354,913 shares issued and outstanding in 2016 and 2015, respectively	16,154,907	15,946,552
Retained earnings	9,158,582	7,176,909
Accumulated other comprehensive income	(12,933)	309,320
Total shareholders' equity	25,300,556	23,432,781
Total liabilities and shareholders' equity	$ 321,188,596	$ 237,294,974

See accompanying notes to financial statements.

River Valley Community Bank
Statements of Income and Comprehensive Income
Years Ended December 31, 2016 and 2015

	2016	2015
Interest income:		
Interest and fees on loans	$ 5,301,722	$ 4,486,314
Interest on taxable investment securities	1,403,745	1,123,111
Interest on investment securities exempt from Federal taxes	646,127	626,287
Interest on interest bearing deposits in banks and other	343,282	191,125
Total interest income	7,694,876	6,426,837
Interest expense:		
Interest on demand deposits	9,069	9,473
Interest on money market and savings deposits	157,577	148,419
Interest on time deposits	56,909	56,752
Interest on Federal Home Loan Bank borrowings	43,483	-
Total interest expense	267,038	214,644
Net interest income	7,427,838	6,212,193
Provision for loan losses (Note 3)	590,000	210,000
Net interest income after provision for loan losses	6,837,838	6,002,193
Noninterest income:		
Service charges and fees	333,060	282,435
Earnings on cash surrender value of life insurance	132,789	112,864
Gain on sale of investment securities	55,005	63,296
Other	36,148	35,707
Total noninterest income	557,002	494,302
Noninterest expense:		
Salaries and employee benefits (Notes 3, 9, and 13)	2,417,782	2,201,002
Data processing and information technology	603,170	534,829
Occupancy and equipment (Note 4)	314,725	316,794
Insurance and assessments	200,572	174,124
Professional fees	240,778	162,229
Directors expense	152,639	97,531
Other	438,540	425,237
Total noninterest expense	4,368,206	3,911,746
Income before income tax expense	3,026,634	2,584,749
Income tax expense (Note 7)	1,044,961	854,899
Net income	$ 1,981,673	$ 1,729,850
Earnings per share - basic	$ 0.84	$ 0.76
Earnings per share - diluted	$ 0.83	$ 0.73
Comprehensive income:		
Net income	$ 1,981,673	$ 1,729,850
Other comprehensive loss:		
Investment securities available-for-sale:		
Unrealized losses arising during the year	(482,075)	(431,009)
Reclassification adjustments for net gains in earnings	(55,005)	(63,296)
Income tax benefit	214,827	197,727
Total other comprehensive loss	(322,253)	(296,578)
Total comprehensive income	$ 1,659,420	$ 1,433,272

See accompanying notes to financial statements.

River Valley Community Bank
Statements of Shareholders' Equity
Years Ended December 31, 2016 and 2015

	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance, January 1, 2015	2,216,170	$ 15,075,273	$ 5,447,059	$ 605,898	$ 21,128,230
Net income	-	-	1,729,850	-	1,729,850
Other comprehensive loss	-	-	-	(296,578)	(296,578)
Stock options exercises	138,743	783,338	-	-	783,338
Stock options expense	-	87,941	-	-	87,941
Balance, December 31, 2015	2,354,913	15,946,552	7,176,909	309,320	23,432,781
Net income	-	-	1,981,673	-	1,981,673
Other comprehensive loss	-	-	-	(322,253)	(322,253)
Stock options exercises	31,683	89,145	-	-	89,145
Stock options expense	-	119,210	-	-	119,210
Balance, December 31, 2016	2,386,596	$ 16,154,907	$ 9,158,582	$ (12,933)	$ 25,300,556

See accompanying notes to financial statements.

River Valley Community Bank
Statements of Cash Flows
Years Ended December 31, 2016 and 2015

	2016	2015
Cash flows from operating activities:		
Net income	$ 1,981,673	$ 1,729,850
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	590,000	210,000
Depreciation, amortization, and accretion, net	1,366,470	1,111,232
Earnings on cash surrender value of life insurance	(132,789)	(112,863)
Gain on sale of investment securities	(55,005)	(63,296)
Change in deferred loan fees, net	34,581	52,318
Deferred income tax (benefit) expense	(143,306)	11,896
Stock options expense	119,210	87,941
Change in accrued interest receivable and other assets	(1,102,391)	(643,054)
Change in accrued interest payable and other liabilities	84,144	269,292
Net cash from operating activities	2,742,587	2,653,316
Cash flows from investing activities:		
Interest bearing deposits		
Purchases	(992,248)	(5,205,752)
Maturities	747,000	-
Investment securities available-for-sale:		
Purchases	(82,903,929)	(36,530,397)
Maturities and calls	2,120,000	4,480,000
Principal payments	11,869,976	11,305,799
Sales	17,693,927	9,787,803
Change in loans, net	(18,561,527)	(25,155,375)
Purchase of premises and equipment	(72,860)	(27,124)
Purchase of insurance policies	(1,000,000)	-
Net cash from investing activities	(71,099,661)	(41,345,046)
Cash flows from financing activities:		
Change in non-time deposits, net	30,871,229	25,007,900
Change in time deposits, net	(153,771)	(1,200,744)
Proceeds from Federal Home Loan Bank borrowings	50,000,000	-
Stock options exercised	89,145	783,338
Net cash from financing activities	80,806,603	24,590,494
Change in cash and cash equivalents	12,449,529	(14,101,236)
Cash and cash equivalents, beginning of year	21,734,318	35,835,554
Cash and cash equivalents, end of year	$ 34,183,847	$ 21,734,318
Supplemental cash flow information:		
Interest paid	$ 228,584	$ 215,929
Income taxes paid	$ 870,000	$ 700,000

See accompanying notes to financial statements.

Note 1. Summary of Significant Accounting Policies

General – River Valley Community Bank (the "Bank") was approved as a state-chartered non-member bank on December 27, 2005 and is subject to regulation by the California Department of Business Oversight (the "DBO") and the Federal Deposit Insurance Corporation (the "FDIC"). The Bank's deposits are insured by the FDIC up to applicable legal limits. The Bank is headquartered in Yuba City, California with branches in Yuba City and Grass Valley, California. The Bank provides products and services to customers who are predominately small to middle-market businesses, professionals, and not-for-profit organizations located in Sutter, Yuba, Nevada and surrounding counties.

The accounting and reporting policies of the Bank conform to accounting principles generally accepted in the United States of America and prevailing practices within the banking industry.

Use of estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions based on available information. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Reclassifications – Certain items in the prior year financial statements were reclassified to conform to the current year presentation. The most significant reclassifications included the regrouping of loan categories to be consistent with the Bank's regulatory reporting classifications, as well as other less significant reclassifications. None of the reclassifications had an impact on prior year net income or shareholders' equity.

Cash and cash equivalents – Cash and cash equivalents consist of cash on hand, due from banks, and interest bearing deposits in banks that are due on demand.

Interest bearing deposits in banks – Interest bearing deposits in banks not included in cash and cash equivalents have original maturities exceeding ninety days, have remaining maturities through November 2020, and are carried at cost. Interest bearing deposits in banks are fully insured.

Investment securities – Investment securities are classified as available-for-sale and are reported at fair value, with unrealized gains and losses excluded from earnings and reported, net of taxes, as accumulated other comprehensive income. The Bank does not invest in marketable equity securities.

Gains or losses on the sale of investment securities are computed on the specific identification method at the trade date. Interest earned on investment securities is reported in interest income, net of applicable adjustments for accretion of discounts and amortization of premiums.

An investment security is impaired when its amortized cost is greater than its fair value. Investment securities that are impaired are evaluated on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation to determine whether such a decline in their fair value is other than temporary. Management utilizes criteria such as the magnitude and duration of the decline and the intent and ability of the Bank to retain its investment in the securities for a period of time sufficient to allow for an anticipated recovery in fair value, in addition to the reasons underlying the decline, to determine whether the loss in value is other than temporary. The term "other than temporary" is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value is determined to be other than temporary, and management does not intend to sell the security or it is more likely than not that the Bank will not be required to sell the security before recovery, only the portion of the impairment loss representing credit exposure is recognized as a charge to earnings, with the balance recognized as a charge to other comprehensive income. If management intends to sell the security or it is more likely than not that the Bank will be required to sell the security before recovering its forecasted cost, the entire impairment loss is recognized as a charge to earnings.

Note 1. Summary of Significant Accounting Policies (continued)

Loans – Loans are stated at principal balances outstanding, net of deferred loan fees and costs and an allowance for loan losses. Loans are grouped into four portfolio segments: (1) real estate loans, (2) agriculture production loans, (3) commercial and industrial loans, and (4) consumer loans. The real estate loan segment is further disaggregated into five classes: (1) construction and development, (2) agriculture, (3) 1-4 family residential, (4) multifamily, and (5) commercial. Interest is accrued daily based upon outstanding loan balances. However, when, in the opinion of management, loans are considered to be impaired and the future collectability of interest and principal is in doubt, loans are placed on nonaccrual status and the accrual of interest income is suspended. Interest income on all loans is discontinued at the time the loan is 90 days delinquent, unless the loan is well-secured and in process of collection. Any interest accrued but unpaid is charged against income. Payments received are applied to reduce principal to the extent necessary to ensure collection. Subsequent payments on these loans, or payments received on nonaccrual loans for which the ultimate collectability of principal is not in doubt, are applied first to earned but unpaid interest and then to principal. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. Loan origination fees, net of certain direct loan origination costs, are deferred and recognized as an adjustment of yield, to be amortized to interest income over the contractual term of the loan without anticipating prepayments.

Allowance for loan losses – The allowance for loan losses is an estimate of probable credit losses in the Bank's loan portfolio that have been incurred as of the balance sheet date. The allowance is established through a provision for loan losses, which is charged to expense. Additions to the allowance are expected to maintain the adequacy of the total allowance after credit losses and loan growth. Credit exposures determined to be uncollectible are charged against the allowance. Cash received on previously charged off amounts is recorded as a recovery to the allowance. The overall allowance consists of two primary components, specific reserves related to impaired loans and general reserves for inherent losses related to loans that are collectively evaluated for impairment.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the original agreement. Loans determined to be impaired are individually evaluated for impairment. When a loan is impaired, the Bank measures impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate, except that as a practical expedient, it may measure impairment based on a loan's observable market price or the fair value of the collateral if the loan is collateral dependent. A loan is collateral dependent if the repayment of the loan is expected to be provided solely by the operation or sale of the underlying collateral.

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the Bank for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. Restructured workout loans typically present an elevated level of credit risk, as the borrowers are not able to perform according to the original contractual terms. Loans that are reported as TDRs are considered impaired and measured for impairment as described above.

The determination of the general reserve for loans that are collectively evaluated for impairment is based on estimates made by management, to include, but not limited to, consideration of historical losses by portfolio segment and class, internal asset classifications, and qualitative factors to include economic trends in the Bank's service areas, industry experience and trends, geographic concentrations, estimated collateral values, the Bank's underwriting policies, the character of the loan portfolio, and probable losses inherent in the portfolio taken as a whole.

The Bank determines a separate allowance for each portfolio segment and class. The allowance for loan losses attributable to each portfolio segment and class, which includes both impaired loans and loans that are collectively evaluated for impairment, is combined to determine the Bank's overall allowance.

Note 1. Summary of Significant Accounting Policies (continued)

Allowance for loan losses (continued) – The Bank assigns a risk rating to all loans and periodically performs detailed reviews of all such loans over a certain threshold to identify credit risks and to assess the overall collectability of the portfolio. These risk ratings are also subject to examination by independent specialists engaged by the Bank and by the Bank's regulators. During these internal reviews, management monitors and analyzes the financial condition of borrowers and guarantors, trends in the industries in which borrowers operate, and the fair values of collateral securing these loans. These credit quality indicators are used to assign a risk rating to each individual loan. The risk ratings can be grouped into five major categories, defined as follows:

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

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

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

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

Loss – Loans classified as loss are considered uncollectible and charged off immediately.

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

Real estate loans – In general, real estate loans are underwritten to ensure the real estate collateral provides an adequate secondary source of repayment in the event of borrower nonperformance. However, downward trends in real estate property values after loan origination can threaten the Bank’s ability to liquidate collateral at amounts sufficient to extinguish the debt without incurring a loss. Certain real estate loan classes present a higher inherent risk of loss, including construction and development and commercial. Construction and development projects may not be completed within specified cost and time lines, which may impact the ability to service debt obligations. Commercial real estate loans are impacted by trends in vacancy rates on commercial properties. High vacancy rates reduce operating revenues and the ability for properties to produce sufficient cash flows to service debt obligations.

Agriculture – Loans secured by crop production and livestock are especially vulnerable to two risk factors that are largely outside the control of the Bank and borrowers: commodity prices and weather conditions, including drought conditions that threaten borrowers’ ability to obtain adequate water for their crops.

Note 1. Summary of Significant Accounting Policies (continued)

Allowance for loan losses (continued)

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

Consumer loans – Loans made to individuals to provide personal purchases for household and equipment items are impacted by trends in unemployment and income levels. General economic activity and concentrations in various job markets could adversely impact this segment given the loss or relocation of a major employer.

Although management believes the allowance to be adequate, ultimate losses may vary from its estimates. At least quarterly, management and the Board of Directors review the adequacy of the allowance, including consideration of the relative risks in the portfolio, current economic conditions and other factors. If the Board of Directors and management determine that changes are warranted based on those reviews, the allowance is adjusted. In addition, the Bank's primary regulators, the FDIC and the California Department of Business Oversight, as an integral part of their examination process, review the adequacy of the allowance. These regulatory agencies may require additions to the allowance based on their judgment about information available at the time of their examinations.

Allowance for credit losses on off-balance sheet credit exposures – The Bank also maintains a separate allowance for off-balance sheet commitments to extend credit. Management estimates anticipated losses using historical data and utilization assumptions. The allowance for commitments to extend credit is included in accrued interest payable and other liabilities on the balance sheet and is not significant.

Premises and equipment – Premises and equipment are carried at cost, less accumulated depreciation. Depreciation is determined using the straight-line method over the estimated useful lives of the related assets. The useful lives of premises are estimated to be 15 to 39 years. The useful lives of furniture, fixtures, and equipment are estimated to be 3 to 10 years.

When assets are sold or otherwise disposed of, the cost and related accumulated depreciation or amortization are removed from the accounts, and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is charged to expense as incurred. The Bank evaluates premises and equipment for financial impairment, as events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable.

Cash surrender value of life insurance – The Bank maintains life insurance policies on certain key executives. Life insurance is recorded at the amounts that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement. The Bank also maintains split dollar life insurance agreements with certain employees, whereby the employees' designated beneficiaries will receive a portion of life insurance benefits upon the employees' death while employed by the Bank. As the benefits do not extend beyond employment, a liability has not been recorded by the Bank.

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

Note 1. Summary of Significant Accounting Policies (continued)

Derivatives – The Bank periodically enters into interest rate swap agreements to offset volatility in earnings created by interest rate floors and caps embedded in certain variable rate loans. The terms of interest rate swap agreements are matched to those of the individual loans with floors and caps being hedged to achieve little to no ineffectiveness. The interest rate swaps are adjusted to fair value on a recurring basis with an offsetting change in fair value of the derivative created by the floors and caps. Net cash settlements related to the interest rate swaps are reported in interest income. Cash flows on derivatives are classified in the cash flow statement similar to the cash flows of the underlying loans.

Income taxes – Deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the reported amount of assets and liabilities and their tax basis. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. A valuation allowance is recognized if, based on the weight of available evidence, management believes it is more likely than not that some portion or all of the deferred tax assets will not be realized.

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

Interest and penalties associated with unrecognized tax benefits are classified as income tax expense in the statement of operations.

Earnings per share – Basic earnings per share (EPS), which excludes dilution, is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted earnings per share 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 of the Bank. The treasury stock method is applied to determine the dilutive effect of stock options in computing diluted earnings per share. Earnings per share are retroactively restated for stock dividends and stock splits through the date of issuance of the financial statements.

Stock options expense – Compensation cost is recognized for stock options issued to employees and directors based on their grant date fair value. A Black-Scholes model is utilized to estimate the grant date fair value. Compensation cost is recognized over the required service period, generally defined as the vesting period. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award, which is generally five years.

Comprehensive income – Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on securities available for sale, net of tax, which are also recognized as separate components of equity.

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

Retirement plans – Employee 401(k) expense is the amount of matching contributions provided by the Bank.

Note 1. Summary of Significant Accounting Policies (continued)

Fair value measurements – Fair values are estimated using relevant market information and other assumptions. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect these estimates. Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

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

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

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

The Bank uses the following methods and significant assumptions to estimate fair value:

Cash and Cash Equivalents – The carrying amounts of cash and short-term instruments approximate fair values, resulting in a Level 1 classification.

Interest Bearing Deposits in Banks – Fair values for interest bearing deposits in banks are estimated using a discounted cash flows calculation that applies interest rates currently being offered on instruments with similar remaining maturities, resulting in a Level 2 classification.

Investment Securities – Fair values for investment securities are determined by quotes received from an independent pricing service using matrix pricing, which is a mathematical technique widely used in the industry to value securities without relying exclusively on quoted market prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities, resulting in a Level 2 classification.

Loans – Fair values of loans are estimated as follows: For variable rate loans that re-price frequently and with no significant change in credit risk, fair values are based on carrying values, resulting in a Level 2 classification. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality resulting in a Level 3 classification.

FHLB Stock – Management determined that it is not practical to determine the fair value of FHLB stock due to restrictions placed on its transferability.

Deposits – The fair values disclosed for demand deposits, including interest and noninterest bearing checking, savings, and money market accounts are, by definition, equal to the amount payable on demand at the reporting date, resulting in a Level 1 classification. Fair values for fixed rate time deposits are estimated using a discounted cash flows calculation that applies interest rates currently being offered on instruments with similar remaining maturities, resulting in a Level 2 classification.

Accrued Interest Receivable and Payable – The carrying amounts of accrued interest approximate fair value, resulting in a Level 2 classification.

Derivatives – The fair values of derivatives are based on valuation models using observable market data as of the measurement date, resulting in a Level 2 classification.

Note 1. Summary of Significant Accounting Policies (continued)

Subsequent events – Management reviewed all events occurring from December 31, 2016 through March 21, 2017, the date the financial statements were available to be issued. No subsequent events require accrual or disclosure in the Bank's financial statements, except for the following.

In February 2017, River Valley Community Bancorp (the "Bancorp") and RVCB Merger Sub, Inc. (the "Merger Sub") were formed as corporations in the state of California, with the Merger Sub being a wholly owned subsidiary of the Bancorp. The Bank's Board of Directors and certain of its executive officers were appointed as directors and officers of the Bancorp and Merger Sub. On February 21, 2017, the Board of Directors approved an Agreement and Plan of Merger and Reorganization (the "Agreement"), which will affect a merger between the Bank and the Merger Sub with the Bank as the surviving entity. As a result of the Agreement, the Bank will become a wholly owned subsidiary of the Bancorp, and shareholders of the Bank will receive shares of the Bancorp in a one for one exchange for their shares in the Bank. The Agreement requires approval from the Bank's shareholders and regulators. The transaction is expected to be completed by the end of the second quarter of 2017.

New accounting standards – In June 2016, the Financial Accounting Standards Board (FASB) issued guidance to replace the current incurred loss model with an expected loss model, which is referred to as the current expected credit loss (CECL) model. The CECL model is applicable to the measurement of credit losses on financial assets measured at amortized cost, including loan receivables. The guidance also applies to certain off-balance sheet credit exposures, including commitments to extend credit, standby letters of credit, and other similar instruments. A cumulative effect adjustment will be recognized in retained earnings as of the beginning of the first reporting period in which the guidance is effective. The guidance will become effective for the Bank on March 31, 2021. The adoption of this standard is expected to have a material effect on the Bank's operating results and financial condition, as it is expected to require a larger allowance for loan losses than is currently recorded.

Note 2. Investment Securities Available-for-Sale

The amortized cost and estimated fair value of investment securities available-for-sale as of December 31, 2016 and 2015 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
December 31, 2016:				
U.S. Government sponsored entities and agencies	$ 43,291,550	$ 47,830	$ (275,828)	$ 43,063,552
Obligations of states and political subdivisions	24,989,912	462,248	(88,357)	25,363,803
U.S. Government sponsored entities and agencies collateralized by mortgage obligations	19,600,089	20,204	(194,316)	19,425,977
Residential mortgage-backed securities	11,004,842	38,235	(104,659)	10,938,418
Corporate debt securities	44,768,129	181,283	(108,194)	44,841,218
Total	$ 143,654,522	$ 749,800	$ (771,354)	$ 143,632,968
December 31, 2015:				
U.S. Government sponsored entities and agencies	$ 8,028,226	$ 13,848	$ (59,967)	$ 7,982,107
Obligations of states and political subdivisions	26,891,694	819,843	(67,730)	27,643,807
U.S. Government sponsored entities and agencies collateralized by mortgage obligations	18,846,328	76,030	(145,508)	18,776,850
Residential mortgage-backed securities	28,197,473	45,886	(142,639)	28,100,720
Corporate debt securities	10,437,447	17,275	(41,512)	10,413,210
Total	$ 92,401,168	$ 972,882	$ (457,356)	$ 92,916,694

Note 2. Investment Securities Available-for-Sale (continued)

The following table summarizes securities with unrealized losses as of December 31, 2016 and 2015, aggregated by major security type and length of time in a continuous unrealized loss position:

	Less Than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
December 31, 2016:						
U.S. Government sponsored entities and agencies	$ 32,154,903	$ (220,690)	$ 3,852,272	$ (55,138)	$ 36,007,175	$ (275,828)
Obligations of states and political subdivisions	3,232,603	(25,177)	5,182,109	(63,180)	8,414,712	(88,357)
U.S. Government sponsored entities and agencies collater-alized by mortgage obligations	2,537,255	(1,110)	13,550,508	(193,206)	16,087,763	(194,316)
Residential mortgage-backed securities	1,552,842	(10,308)	8,160,099	(94,351)	9,712,941	(104,659)
Corporate debt securities	16,538,907	(106,238)	1,287,636	(1,956)	17,826,543	(108,194)
Total	$ 56,016,510	$ (363,523)	$ 32,032,624	$ (407,831)	$ 88,049,134	$ (771,354)
December 31, 2015:						
U.S. Government sponsored entities and agencies	$ 4,743,686	$ (32,796)	$ 1,992,509	$ (27,171)	$ 6,736,195	$ (59,967)
Obligations of states and political subdivisions	6,461,798	(66,981)	261,460	(749)	6,723,258	(67,730)
U.S. Government sponsored entities and agencies collater-alized by mortgage obligations	18,665,453	(91,961)	3,492,354	(53,547)	22,157,807	(145,508)
Residential mortgage-backed securities	11,120,324	(126,656)	645,505	(15,983)	11,765,829	(142,639)
Corporate debt securities	7,582,527	(41,512)	-	-	7,582,527	(41,512)
Total	$ 48,573,788	$ (359,906)	$ 6,391,828	$ (97,450)	$ 54,965,616	$ (457,356)

As of December 31, 2016, the Bank's security portfolio consisted of 98 securities that were in an unrealized loss position, of which 37 had been in a loss position for greater than 12 months. The majority of unrealized losses are related to the Bank's investment in U.S. Government sponsored entities and agencies, U.S. Government sponsored entities and agencies collateralized by mortgage obligations, and agencies collateralized by residential mortgage obligations.

Unrealized losses for all securities have not been recognized into income because the issuers' bonds are of high credit quality (investment grade or higher), management does not intend to sell and it is likely that management will not be required to sell the securities prior to their anticipated recovery, and the decline in fair value is largely due to changes in interest rates and other market conditions. The fair value is expected to recover as the bonds approach maturity.

Note 2. Investment Securities Available-for-Sale (continued)

The amortized cost and estimated fair value of available-for-sale investment securities as of December 31, 2016 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because the issuers of the securities may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
Within one year	$ 2,688,979	$ 2,692,201
After one year through five years	17,986,300	18,162,334
After five years through ten years	44,842,318	45,108,309
After ten years	4,240,444	4,242,184
	69,758,041	70,205,028
Investment securities not due at a single maturity date:		
U.S. Government sponsored entities and agencies, including those collateralized by mortgage obligations and residential mortgage-backed securities	73,896,481	73,427,940
Total	$ 143,654,522	$ 143,632,968

Note 3. Loans and the Allowance for Loan Losses

The following tables present the activity in the allowance for loan losses by class for the years ended December 31, 2016 and 2015 and the recorded investments in loans and ending balance in the allowance for loan losses by class as of December 31, 2016 and 2015:

	Real Estate								
	Construct. & Develop	**Agriculture**	**1-4 Family Resident**	**Multifamily**	**Commercial**	**Agriculture Production**	**Commercial & Indust.**	**Consumer**	**Total**
December 31, 2016:									
Balance, beginning of year	$ 229,597	$ 103,358	$ 180,848	$ 140,569	$ 894,691	$ 37,337	$ 208,557	$ 6,847	$ 1,801,804
Provision for loan losses	(82,780)	(9,745)	(29,462)	(6,253)	22,837	5,640	691,908	(2,145)	590,000
Loans charged off	-	-	-	-	-	-	(479,645)	-	(479,645)
Loans recovered	-	-	-	-	-	-	14,297	-	14,297
Total	$ 146,817	$ 93,613	$ 151,386	$ 134,316	$ 917,528	$ 42,977	$ 435,117	$ 4,702	$ 1,926,456
December 31, 2015:									
Balance, beginning of year	$ 69,630	$ 84,013	$ 153,945	$ 65,816	$ 924,139	$ 36,628	$ 240,121	$ 11,912	$ 1,586,204
Provision for loan losses	159,967	19,345	26,903	74,753	(29,448)	709	(37,164)	(5,065)	210,000
Loans charged off	-	-	-	-	-	-	-	-	-
Loans recovered	-	-	-	-	-	-	5,600	-	5,600
Total	$ 229,597	$ 103,358	$ 180,848	$ 140,569	$ 894,691	$ 37,337	$ 208,557	$ 6,847	$ 1,801,804
December 31, 2016:									
Loans:									
Individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ -	$ 117,405	$ -	$ 117,405
Collectively evaluated for impairment	5,352,122	7,488,986	13,164,274	12,792,470	67,652,399	4,093,054	14,001,036	516,488	125,060,829
Total	$ 5,352,122	$ 7,488,986	$ 13,164,274	$ 12,792,470	$ 67,652,399	$ 4,093,054	$ 14,118,441	$ 516,488	$ 125,178,234
Allowance for Loan Losses:									
Related to loans individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Related to loans collectively evaluated for impairment	146,817	93,613	151,386	134,316	917,528	42,977	435,117	4,702	1,926,456
Total	$ 146,817	$ 93,613	$ 151,386	$ 134,316	$ 917,528	$ 42,977	$ 435,117	$ 4,702	$ 1,926,456

Note 3. Loans and the Allowance for Loan Losses (continued)

	Real Estate								
	Construct. & Develop	**Agriculture**	**1-4 Family Resident**	**Multifamily**	**Commercial**	**Agriculture Production**	**Commercial & Indust.**	**Consumer**	**Total**
December 31, 2015:									
Loans:									
Individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Collectively evaluated for impairment	7,082,514	7,371,895	12,899,556	10,981,210	53,993,974	3,602,925	10,533,294	616,687	107,082,055
Total	$ 7,082,514	$ 7,371,895	$ 12,899,556	$ 10,981,210	$ 53,993,974	$ 3,602,925	$ 10,533,294	$ 616,687	$ 107,082,055
Allowance for Loan Losses:									
Related to loans individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Related to loans collectively evaluated for impairment	229,597	103,358	180,848	140,569	894,691	37,337	208,557	6,847	1,801,804
Total	$ 229,597	$ 103,358	$ 180,848	$ 140,569	$ 894,691	$ 37,337	$ 208,557	$ 6,847	$ 1,801,804

The following table presents the loan portfolio by class allocated by management's internal risk ratings as of December 31, 2016 and 2015:

	Real Estate								
	Construct. & Develop	**Agriculture**	**1-4 Family Resident**	**Multifamily**	**Commercial**	**Agriculture Production**	**Commercial & Indust.**	**Consumer**	**Total**
December 31, 2016:									
Pass	$ 5,352,122	$ 7,463,652	$ 12,346,030	$ 12,792,470	$ 65,088,649	$ 3,781,668	$ 13,922,119	$ 516,488	$ 121,263,198
Special mention	-	-	599,097	-	2,563,750	-	78,917	-	3,241,764
Substandard	-	25,334	219,147	-	-	311,386	117,405	-	673,272
Total	$ 5,352,122	$ 7,488,986	$ 13,164,274	$ 12,792,470	$ 67,652,399	$ 4,093,054	$ 14,118,441	$ 516,488	$ 125,178,234
December 31, 2015:									
Pass	$ 7,082,514	$ 7,371,895	$ 12,802,217	$ 10,981,210	$ 52,620,308	$ 3,568,128	$ 9,752,899	$ 616,687	$ 104,795,858
Special mention	-	-	97,339	-	1,373,666	-	-	-	1,471,005
Substandard	-	-	-	-	-	34,797	780,395	-	815,192
Total	$ 7,082,514	$ 7,371,895	$ 12,899,556	$ 10,981,210	$ 53,993,974	$ 3,602,925	$ 10,533,294	$ 616,687	$ 107,082,055

Note 3. Loans and the Allowance for Loan Losses (continued)

The Bank has no past due loans greater than 30 days or nonaccrual loans as of December 31, 2016 and 2015. As of December 31, 2016, the Bank has one impaired loan, which is included in the commercial and industrial segment with a recorded investment and unpaid principal balance of $117,405 and no related allowance. The loan was modified as a troubled debt restructuring during 2016 to extend the maturity at a below market interest rate for a debtor experiencing financial difficulty. During the year ended December 31, 2016, this loan performed as agreed under the modified terms, had an average recorded investment of $134,201, and recognized interest income of $7,223. The Bank had no impaired loans as of December 31, 2015.

No specific reserves were allocated to customers whose loan terms have been modified in troubled debt restructurings as of December 31, 2016 and 2015. The Bank has not committed to lend additional amounts as of December 31, 2016 and 2015 to customers with outstanding loans that are classified as troubled debt restructurings. During the years ended December 31, 2016 and 2015, there were no modifications that were determined to be troubled debt restructurings, except the one impaired loan noted above. In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Bank's underwriting policy.

Salaries and employee benefits totaling $121,362 and $156,144 have been deferred as direct loan origination costs for the years ended December 31, 2016 and 2015, respectively.

Note 4. Premises and Equipment

Premises and equipment consisted of the following as of December 31, 2016 and 2015:

	2016	2015
Land	$ 774,631	$ 774,631
Building	1,561,211	1,561,211
Furniture, fixtures, and equipment	789,733	741,524
Leasehold improvements	18,526	18,526
In process	21,524	-
	3,165,625	3,095,892
Accumulated depreciation	(1,136,424)	(1,019,003)
Total	$ 2,029,201	$ 2,076,889

Depreciation included in occupancy and equipment expense totaled $120,548 and $132,274 for the years ended December 31, 2016 and 2015, respectively.

Note 5. Time Deposits

Aggregate annual maturities of time deposits are as follows for the years ending December 31:

2017	$	9,244,642
2018		1,407,923
2019		58,891
2020		36,024
2021		214,240
Total	$	10,961,720

Note 6. Borrowing Facilities

The Bank has unsecured Federal funds lines of credit with correspondent banks under which it can borrow up to $17,000,000. There were no borrowings outstanding under these arrangements as of December 31, 2016 and 2015, respectively.

In addition, the Bank has an arrangement with the FHLB under which it may borrow an amount not to exceed 25% of total assets, which must be fully secured by qualifying securities and loans. As of December 31, 2016 and 2015, the estimated fair value of investment securities pledged was approximately $71,550,000 and $44,059,000, respectively, and the recorded investment in loans pledged was approximately $26,482,000 and $20,985,000, respectively. As of December 31, 2016, available borrowings under this arrangement were approximately $23,362,000, and outstanding fixed rate borrowings were as follows:

Amount	Maturity	Interest Rate
$ 20,000,000	01/27/17	0.43%
20,000,000	01/20/17	0.53%
10,000,000	01/23/17	0.62%
$ 50,000,000		

All three borrowings outstanding as of December 31, 2016 were renewed upon their maturities in 2017. As of December 31, 2015, the Bank did not have borrowings outstanding with the FHLB.

Note 7. Income Taxes

Income taxes for the years ended December 31, 2016 and 2015 consist of the following:

	2016	2015
Current	$ 1,188,267	$ 843,003
Deferred	(143,306)	11,896
Income tax expense	$ 1,044,961	$ 854,899

Deferred tax assets and liabilities as of December 31, 2016 and 2015 consist of the following:

	2016	2015
Deferred tax assets:		
Allowance for loan losses	$ 740,887	$ 700,492
Future benefit of state tax deduction	107,267	-
Other	203,501	245,505
Unrealized loss on investment securities available-for-sale	8,621	-
Total	1,060,276	945,997
Deferred tax liabilities:		
Accrual to cash conversion	(207,049)	(276,074)
Deferred loan costs	(130,596)	(111,823)
Other	(70,589)	(57,985)
Unrealized gain on investment securities available-for-sale	-	(206,206)
Total	(408,234)	(652,088)
Deferred tax asset, net	$ 652,042	$ 293,909

The provision for income taxes differs from amounts computed by applying the statutory federal income tax rate to operating income before income taxes. The significant items comprising these differences consist of the following for the years ended December 31, 2016 and 2015:

	2016		2015	
	Amount	Rate	Amount	Rate
Federal income tax at statutory rates	$ 1,029,057	34.0%	$ 878,814	34.0%
State franchise tax, net of Federal benefit	216,405	7.2%	184,361	7.1%
Tax exempt investment securities, net	(219,340)	-7.2%	(211,057)	-8.2%
Non-deductible stock options expense	26,015	0.9%	22,595	0.9%
Bank owned life insurance	(45,148)	-1.5%	(38,374)	-1.5%
Enterprise zone State tax credits	(13,311)	-0.4%	(18,188)	-0.7%
Other	51,283	1.5%	36,748	1.5%
Total	$ 1,044,961	34.5%	$ 854,899	33.1%

The Bank is subject to U.S. Federal income tax and California state franchise tax. Federal tax returns for 2015, 2014, and 2013 are currently open for examination. California state franchise tax returns for 2015, 2014, 2013, and 2012 are currently open for examination. The Bank currently has no tax returns under examination.

Note 8. Commitments and Contingencies

Financial instruments with off-balance sheet risk – The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business in order to meet the financing needs of its customers. These financial instruments consist of the following as of December 31, 2016 and 2015:

	2016	2015
Commitments to extend credit	$ 36,080,643	$ 26,861,336
Standby letters of credit	$ 52,000	$ 21,000

The Bank's exposure to credit loss in the event of nonperformance by the other party for commitments to extend credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments as it does for loans included on the balance sheet.

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 some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, and deeds of trust on residential real estate and income-producing commercial properties.

Real estate loan commitments represent approximately 70% of total commitments and are generally secured by property with a loan-to-value ratio not to exceed 75%. Agricultural production loan commitments represent approximately 10% of total commitments and are generally secured by crop assignments, accounts receivable and farm equipment and have variable interest rates. Commercial and industrial loan commitments represent approximately 20% of total commitments and are generally unsecured or secured by collateral other than real estate and have variable interest rates.

Concentrations of credit risk – The Bank grants real estate loans to customers in Sutter, Yuba, Nevada and surrounding counties. In management's judgment, a concentration of loans exists in real estate secured loans with approximately 85% of the Bank's loans being real estate related. Although management believes the loans within this concentration have no more than the normal risk of collectability, a substantial decline in the performance of the economy in general or a decline in real estate values in the Bank's primary market area, in particular, could have an adverse impact on the collectability of these loans. Cash flows from commercial real estate properties and personal income represents the primary source of repayment for a majority of these loans.

Deposit concentration – The Bank has a limited number of deposit relationships that in the aggregate represents approximately 20% of the Bank's deposits as of December 31, 2016. These relationships are with related parties (see Note 12). The loss of these deposit relationships could have a material impact on the Bank's operations and liquidity. However, management mitigates this risk by maintaining sufficient liquidity to manage fluctuations in account balances.

Correspondent banking arrangements – The Bank maintains funds on deposit with other federally insured financial institutions under correspondent banking agreements. The Bank held $16,920,000 in overnight funds at the Federal Reserve Bank as of December 31, 2016.

Note 9. Stock Options

The Bank has two stock compensation plans, the River Valley Community Bank Equity Incentive Stock Option Plan (the "2006 Plan") and the River Valley Community Bank 2016 Equity Incentive Plan (the “2016 Plan”), which were approved by its shareholders. The 2006 Plan expired during 2016, and no new shares may be granted under that plan. Under the 2016 Plan, a total of 395,200 shares of common stock are reserved for grants of awards to employees, directors, and consultants under incentive and non-statutory stock option agreements. The amount, frequency, and terms of share-based awards may vary based on competitive practices, the Bank's operating results, and government regulations. Generally, stock options vest over a five year term and expire ten years after the date of grant. New shares are issued upon option exercise or restricted share grants. The Plan requires that the option price may not be less than the fair market value of the stock at the date the option is granted and that the stock must be paid in full at the time the option is exercised.

Restricted stock awards are grants of shares of common stock that are subject to forfeiture until specific conditions or goals are met. Conditions may be based on continuing employment or achieving specified performance goals. During the period of restriction, participants holding restricted stock may have full voting and dividend rights. The restrictions lapse in accordance with a schedule or with other conditions determined by the Board of Directors. No awards of restricted stock were made during the years ended December 31, 2016 and 2015.

A summary of stock option activity for the year ended December 31, 2016 is presented below:

	Shares	Weighted Avg. Exercise Price	Weighted Avg. Remaining Contract Term
Outstanding, beginning of year	$ 188,483	$ 8.77	
New grants	93,100	10.45	
Exercises	(46,529)	6.46	
Forfeitures	(40,676)	8.48	
Expired	(390)	6.40	
Outstanding, end of year	$ 193,988	$ 10.19	7.14
Exercisable, end of year	$ 78,063	$ 9.83	4.92

Information related to stock options granted during the years ended December 31, 2016 and 2015 and total compensation cost recognized for all outstanding stock options during the same periods is as follows:

	2016	2015
Weighted average grant date fair value per share	$ 3.88	$ 4.21
Significant fair value assumptions:		
Expected term	6.5 years	6.5 years
Expected annual volatility	29.6%	39.3%
Expected annual dividend yield	0.0%	0.0%
Risk-free interest rate	1.7%	1.8%
Total compensation cost included in salaries and employee benefits	$ 119,210	$ 87,941

Note 9. Stock Options (continued)

Information related to stock options exercised during the years ended December 31, 2016 and 2015 is as follows:

	2016	2015
Intrinsic value	$ 197,376	$ 611,512
Cash received	89,145	783,338

As of December 31, 2016, the unrecognized compensation cost related to non-vested stock option awards totaled $338,302, which is expected to be amortized on a straight-line basis over a weighted average period of 2.4 years and will be adjusted for subsequent changes in estimated forfeitures.

Note 10. Shareholders' Equity

Earnings per share – A reconciliation of the numerators and denominators of the basic and diluted earnings per share computations for the years ended December 31, 2016 and 2015 is as follows:

	Net Income Available to Common Shareholders	Weighted Average Shares Outstanding	Earnings per Common Share
December 31, 2016:			
Basic earnings per share	$ 1,981,673	2,371,383	$ 0.84
Dilution effect of stock options	-	24,991	(0.01)
Diluted earnings per share	$ 1,981,673	2,396,374	$ 0.83
December 31, 2015:			
Basic earnings per share	$ 1,729,850	2,282,677	$ 0.76
Dilution effect of stock options	-	74,342	(0.03)
Diluted earnings per share	$ 1,729,850	2,357,019	$ 0.73

Shares of common stock issuable under stock options for which the exercise prices are greater than average market prices are not included in the computation of diluted earnings per share due to their antidilutive effect. For the years ended December 31, 2016 and 2015, 25,875 and 26,562 stock options were excluded, respectively.

Dividends – Upon declaration by the Board of Directors, all shareholders of record will be entitled to receive dividends. The California Financial Code restricts the total dividend payment of any state banking association in any calendar year to the lesser of (1) the bank's retained earnings or (2) the bank's net income for its last three fiscal years, less distributions made to shareholders during the same three-year period. As of December 31, 2016, retained earnings of $4,214,296 were free of such restrictions.

Note 10. Shareholders' Equity (continued)

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

In 2013, the Board of Governors of the Federal Reserve System, the FDIC, and the Office of the Comptroller of the Currency issued final rules under Basel III (the "Basel III Capital Rules"), establishing a new comprehensive framework for regulatory capital for U.S. banking organizations. These rules implement the Basel Committee's December 2010 proposed framework, certain provisions of the Dodd-Frank Act, and revise the risk-based capital requirements applicable to bank-holding companies and depository institutions, including the Bank. These rules became effective for the Bank on January 1, 2015, and are subject to phase-in periods for certain of their components. The significant changes outlined under the Basel III Capital Rules that are applicable to the Bank include:

- A new Common Equity Tier I ("Tier 1 Common") capital measure, with a minimum ratio requirement of 4.5% for Tier 1 Common to risk-weighted assets, and for Prompt Corrective Action purposes 6.5% or greater to generally be considered "well-capitalized".
- A capital conservation buffer in addition to Tier 1 Common of 0.625% for 2016, 1.25% for 2017, 1.875% for 2018, and 2.5% for 2019. The capital conservation buffer begins phasing in on January 1, 2016.
- Changes to the calculation of risk-weighted assets from the current four categories (0%, 20%, 50% and 100%) to a much broader and risk-sensitive number of categories.
- The inclusion of certain changes in accumulated other comprehensive income ("AOCI") in the determination of regulatory capital measures; however, "non-advanced approaches banking organizations", including the Bank, were able to make a one-time permanent election, as of January 1, 2015, to exclude these changes in AOCI from the determination of regulatory capital. The Bank has made this election.
- An exclusion from Tier 1 Common of certain items on a phased-in basis, such as deferred tax assets and intangible assets.

When Basel III Capital Rules are fully phased-in on January 1, 2019, the Bank will be required to maintain a 2.5% "capital conservation buffer", which is designed to absorb losses during periods of economic stress. This capital conservation buffer will be comprised entirely of Tier 1 Common and will be in addition to minimum risk-weighted asset ratios outlined under the Basel III Capital Rules. If a banking organization fails to hold capital above minimum capital ratios, including the capital conservation buffer, it will be subject to certain restrictions on capital distributions and discretionary bonus payments.

As of December 31, 2016, the most recent notification from the FDIC categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the Bank's category. Management believes the Bank meets all capital adequacy requirements to which it is subject as of December 31, 2016.

Note 10. Shareholders' Equity (continued)

Regulatory capital (continued) – Actual and required capital amounts and ratios as of December 31, 2016 and 2015 are as follows:

	2016		2015	
	Amount	Ratio	Amount	Ratio
Tier 1 capital to average assets:				
The Bank	$ 25,314,000	8.5%	$ 23,124,000	9.8%
Minimum to be "Well-Capitalized"	$ 14,925,850	5.0%	$ 11,796,650	5.0%
Minimum regulatory requirement	$ 11,940,680	4.0%	$ 9,437,320	4.0%
Tier 1 common to risk weighted assets:				
The Bank	$ 25,314,000	13.2%	$ 23,124,000	15.2%
Minimum to be "Well-Capitalized"	$ 12,452,440	6.5%	$ 9,909,770	6.5%
Minimum regulatory requirement	$ 8,620,920	4.5%	$ 6,860,610	4.5%
Tier 1 capital to risk weighted assets:				
The Bank	$ 25,314,000	13.2%	$ 23,124,000	15.2%
Minimum to be "Well-Capitalized"	$ 15,326,080	8.0%	$ 12,196,640	8.0%
Minimum regulatory requirement	$ 11,494,560	6.0%	$ 9,147,480	6.0%
Total capital to risk weighted assets:				
The Bank	$ 27,349,000	14.3%	$ 24,996,000	16.4%
Minimum to be "Well-Capitalized"	$ 19,157,600	10.0%	$ 15,245,800	10.0%
Minimum regulatory requirement	$ 15,326,080	8.0%	$ 12,196,640	8.0%

Note 11. Derivatives

The notional amount of the interest rate swaps does not represent amounts exchanged by the parties involved. The amount exchanged is determined by reference to the notional amount and the other terms of the individual interest rate swap agreements. The Bank has six and five interest rate swap agreements as of December 31, 2016 and 2015, respectively. Summary information about these interest-rate swaps as of December 31, 2016 and 2015 is as follows:

	2016	2015
Total notional amounts	$ 4,496,732	$ 3,679,575
Weighted average maturity	12.9 years	14.7 years
Total fair value of interest rate swaps, net	$ (110,365)	$ (151,427)

The fair value of interest rate swaps as of December 31, 2016 and 2015 is reflected in accrued interest payable and other liabilities with changes in fair value recorded in noninterest income. Changes in the fair value of interest rate swaps are offset by contrasting changes in the fair value of derivatives created by interest rate floors and caps embedded in the loans being hedged, which are reflected in accrued interest receivable and other assets as of December 31, 2016 and 2015. The offsetting changes in fair value result in little to no impact on noninterest income.

Note 12. Related Party Transactions

During the normal course of business, the Bank enters into transactions with related parties, including directors and executive officers. The following is a summary of the aggregate activity involving related party borrowers for the years ended December 31, 2016 and 2015:

	2016	2015
Related party loans, beginning of year	$ 8,285,985	$ 4,180,267
Advances	2,041,117	5,372,514
Payments	(2,148,534)	(1,266,796)
Related party loans, end of year	$ 8,178,568	$ 8,285,985
Undisbursed commitments to related parties, end of year	$ 2,101,483	$ 1,046,381

As of December 31, 2016 and 2015 the Bank's deposits from related parties were approximately $48,951,000 or 20% and $50,260,000 or 24% of the Bank's total deposits, respectively. These related parties include directors, executive officers, and their affiliates and have strong relationships and connections with the Bank. As a result, management believes these circumstances mitigate the risk of unexpected volatility in deposit balances.

Note 13. Employee Benefit Plan

The Bank has a 401(k) profit sharing plan. All employees 18 years of age or older with 30 days of service are eligible to participate in the plan. Eligible employees may elect to make tax deferred contributions up to the maximum amount allowed by law. Safe harbor contributions of $65,494 and $54,432 were made for the years ended December 31, 2016 and 2015, respectively.

Note 14. Fair Value Measurements

Assets and liabilities measured at fair value on a recurring basis as of December 31, 2016 and 2015 and the level input used to determine the estimated fair value are summarized below:

	Level 1	Level 2	Level 3	Total
December 31, 2016:				
Investment securities available-for-sale:				
U.S. Government sponsored entities and agencies	$ -	$ 43,063,552	$ -	$ 43,063,552
Obligations of states and political subdivisions	-	25,363,803	-	25,363,803
U.S. Government sponsored entities and agencies collateralized by mortgage obligations	-	19,425,977	-	19,425,977
Residential mortgage-backed securities	-	10,938,418	-	10,938,418
Corporate debt securities	-	44,841,218	-	44,841,218
Total investment securities	$ -	$ 143,632,968	$ -	$ 143,632,968
Derivative asset	$ -	$ 110,365	$ -	$ 110,365
Derivative liability	$ -	$ (110,365)	$ -	$ (110,365)
December 31, 2015:				
Investment securities available-for-sale:				
U.S. Government sponsored entities and agencies	$ -	$ 7,982,107	$ -	$ 7,982,107
Obligations of states and political subdivisions	-	27,643,807	-	27,643,807
U.S. Government sponsored entities and agencies collateralized by mortgage obligations	-	18,776,850	-	18,776,850
Residential mortgage-backed securities	-	28,100,720	-	28,100,720
Corporate debt securities	-	10,413,210	-	10,413,210
Total investment securities	$ -	$ 92,916,694	$ -	$ 92,916,694
Derivative asset	$ -	$ 151,427	$ -	$ 151,427
Derivative liability	$ -	$ (151,427)	$ -	$ (151,427)

There were no assets measured at fair value on a non-recurring basis as of December 31, 2016 and 2015.

Note 14. Fair Value Measurements (continued)

The carrying amounts and estimated fair values of financial instruments not measured at fair value as of December 31, 2016 and 2015 and the level input used to determine the estimated fair value are summarized below:

	Carrying Amount	Estimate Fair Value			
		Level 1	Level 2	Level 3	Total
December 31, 2016:					
Financial assets:					
Cash and due from banks	$ 5,000,598	$ 5,000,598	$ -	$ -	$ 5,000,598
Interest bearing deposits in banks	37,865,249	29,183,249	8,681,856	-	37,865,105
Loans, net	123,109,374	-	-	122,419,000	122,419,000
Accrued interest receivable	1,257,502	-	1,257,502	-	1,257,502
FHLB stock	1,620,000	N/A	N/A	N/A	N/A
Financial liabilities:					
Deposits	243,950,456	232,988,736	10,940,000	-	243,928,736
Accrued interest payable	11,329	-	11,329	-	11,329
December 31, 2015:					
Financial assets:					
Cash and due from banks	$ 9,080,595	$ 9,080,595	$ -	$ -	$ 9,080,595
Interest bearing deposits in banks	21,090,475	12,653,723	8,436,752	-	21,090,475
Loans, net	105,172,428	-	-	105,861,000	105,861,000
Accrued interest receivable	841,731	-	841,731	-	841,731
FHLB stock	930,700	N/A	N/A	N/A	N/A
Financial liabilities:					
Deposits	213,232,998	202,117,507	11,096,000	-	213,213,507
Accrued interest payable	9,602	-	9,602	-	9,602