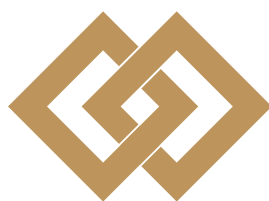




**2020
ANNUAL REPORT**



partners bank of california

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Independent Auditor's Report

RSM US LLP

To the Board of Directors
Partners Bank of California
Mission Viejo, California

Report on the Financial Statements

We have audited the accompanying financial statements of Partners Bank of California, which comprise the statements of financial condition as of December 31, 2020 and 2019, the related statements of income, comprehensive income, changes in stockholders' 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 Partners Bank of California as of December 31, 2020 and 2019, 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.

RSM US LLP

Irvine, California
February 22, 2021

Partners Bank of California

**Statements of Financial Condition
December 31, 2020 and 2019
(In Thousands, Except Share Data)**

| | 2020 | 2019 |
|---|-------------------|-------------------|
| Assets | | |
| Cash and cash equivalents | \$ 66,126 | \$ 61,961 |
| Investment securities available for sale | 2,663 | 5,542 |
| Loans, net | 330,588 | 236,535 |
| Federal Home Loan Bank (FHLB) and other stock, at cost | 1,601 | 1,265 |
| Premises and equipment | 439 | 369 |
| Deferred tax asset, net | 1,814 | 825 |
| Accrued interest and other assets | 3,297 | 1,266 |
| | <hr/> | <hr/> |
| Total assets | \$ 406,528 | \$ 307,763 |
| Liabilities and Stockholders' Equity | | |
| Liabilities: | | |
| Deposits: | | |
| Noninterest-bearing demand | \$ 147,707 | \$ 102,466 |
| Savings, negotiable order of withdrawal (NOW) and money market accounts | 144,256 | 106,628 |
| Time deposits under \$250,000 | 26,942 | 23,649 |
| Time deposits \$250,000 and over | 2,785 | 2,183 |
| Total deposits | 321,690 | 234,926 |
| | <hr/> | <hr/> |
| Borrowings | 46,000 | 38,000 |
| Accrued interest and other liabilities | 3,043 | 1,590 |
| Total liabilities | 370,733 | 274,516 |
| <hr/> | | |
| Commitments and contingencies (Note 10) | | |
| Stockholders' equity: | | |
| Common stock, no par value; 10,000,000 shares authorized; 4,302,494 shares issued and outstanding for the years 2020 and 2019 | 32,824 | 32,824 |
| Additional paid-in capital | 2,061 | 1,729 |
| Retained earnings (accumulated deficit) | 840 | (1,326) |
| Accumulated other comprehensive income | 70 | 20 |
| Total stockholders' equity | 35,795 | 33,247 |
| <hr/> | | |
| Total liabilities and stockholders' equity | \$ 406,528 | \$ 307,763 |
| <hr/> | | |

See notes to financial statements.

Partners Bank of California

Statements of Income
Years Ended December 31, 2020 and 2019
(In Thousands)

| | 2020 | 2019 |
|---|-----------------|-----------------|
| Interest income: | | |
| Interest and fees on loans | \$ 16,285 | \$ 12,336 |
| Interest on investment securities | 83 | 148 |
| Interest on federal funds sold and other | 146 | 417 |
| Total interest income | 16,514 | 12,901 |
| Interest expense: | | |
| Interest on savings deposits, NOW and money market accounts | 975 | 1,444 |
| Interest on time deposits | 402 | 557 |
| Interest on borrowings | 298 | 132 |
| Total interest expense | 1,675 | 2,133 |
| Net interest income before provision for loan losses | 14,839 | 10,768 |
| Provision for loan losses | 3,162 | 326 |
| Net interest income after provision for loan losses | 11,677 | 10,442 |
| Noninterest income: | | |
| Service charges, fees and other | 267 | 240 |
| Gain on sale of loans | - | 139 |
| | 267 | 379 |
| Noninterest expense: | | |
| Salaries and employee benefits | 6,116 | 5,329 |
| Occupancy and equipment expenses | 749 | 602 |
| Other expenses | 1,928 | 1,768 |
| | 8,793 | 7,699 |
| Income before income tax provision | 3,151 | 3,122 |
| Income tax provision | 985 | 1,058 |
| Net income available to common stockholders | \$ 2,166 | \$ 2,064 |
| Net income available to common stockholders, per share: | | |
| Basic | \$ 0.50 | \$ 0.51 |
| Diluted | 0.49 | 0.50 |

See notes to financial statements.

Partners Bank of California

Statements of Comprehensive Income
Years Ended December 31, 2020 and 2019
(In Thousands)

| | 2020 | 2019 |
|---|------------------------|------------------------|
| Net income | \$ 2,166 | \$ 2,064 |
| Other comprehensive income: | | |
| Unrealized holding gain arising during period, net of tax | <u>50</u> | <u>91</u> |
| Comprehensive income | <u>\$ 2,216</u> | <u>\$ 2,155</u> |

See notes to financial statements.

Partners Bank of California

Statements of Changes in Stockholders' Equity
 Years Ended December 31, 2020 and 2019
 (In Thousands, Except Share Data)

| | Common Stock | | Additional | Retained | Accumulated | Total |
|-----------------------------------|------------------|------------------|-----------------|---------------|---------------|------------------|
| | Number of | Amount | Paid-In | Earnings | Other | |
| | Shares | | Capital | (Accumulated | Comprehensive | |
| | | | | Deficit) | (Loss) Income | |
| Balance, December 31, 2018 | 3,876,173 | \$ 29,513 | \$ 1,661 | \$ (3,390) | \$ (71) | \$ 27,713 |
| Stock-based compensation | - | - | 251 | - | - | 251 |
| Stock options exercised | 82,571 | 593 | (183) | - | - | 410 |
| Stock issued, net | 343,750 | 2,718 | - | - | - | 2,718 |
| Net income | - | - | - | 2,064 | - | 2,064 |
| Other comprehensive income | - | - | - | - | 91 | 91 |
| Balance, December 31, 2019 | 4,302,494 | 32,824 | 1,729 | (1,326) | 20 | 33,247 |
| Stock-based compensation | - | - | 332 | - | - | 332 |
| Net income | - | - | - | 2,166 | - | 2,166 |
| Other comprehensive income | - | - | - | - | 50 | 50 |
| Balance, December 31, 2020 | 4,302,494 | \$ 32,824 | \$ 2,061 | \$ 840 | \$ 70 | \$ 35,795 |

See notes to financial statements.

Partners Bank of California

Statements of Cash Flows
Years Ended December 31, 2020 and 2019
(In Thousands)

| | 2020 | 2019 |
|---|-----------------|-----------------|
| Cash flows from operating activities: | | |
| Net income | \$ 2,166 | \$ 2,064 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 257 | 202 |
| Provision for loan losses | 3,162 | 326 |
| Recovery on unfunded commitments | (22) | (6) |
| Deferred income taxes | (995) | 85 |
| Stock-based compensation | 332 | 251 |
| Gain on sale of loans | - | (139) |
| Net amortization of premiums on investment securities | 12 | 29 |
| Change in net deferred loan fees | 422 | (12) |
| Change in accrued interest, other assets and liabilities | (579) | 467 |
| Net cash provided by operating activities | 4,755 | 3,267 |
| Cash flows from investing activities: | | |
| Proceeds from paydowns on investment securities | 2,940 | 3,579 |
| Net increase in loans | (97,637) | (28,792) |
| Proceeds from sales of loans | - | 3,120 |
| Purchase of FHLB stock | (336) | (303) |
| Purchases of premises and equipment | (321) | (292) |
| Net cash used in investing activities | (95,354) | (22,688) |
| Cash flows from financing activities: | | |
| Net proceeds from issuance of common stock | - | 2,718 |
| Proceeds received from stock options exercised | - | 410 |
| Net increase in demand deposits and savings accounts | 82,869 | 33,461 |
| Net increase in time deposits | 3,895 | 3,239 |
| Proceeds from borrowings | 8,000 | 7,000 |
| Net cash provided by financing activities | 94,764 | 46,828 |
| Increase in cash and cash equivalents | 4,165 | 27,407 |
| Cash and cash equivalents: | | |
| Beginning of year | 61,961 | 34,554 |
| End of year | \$ 66,126 | \$ 61,961 |
| Supplemental disclosures of cash flow information: | | |
| Cash payments for: | | |
| Interest | \$ 1,682 | \$ 2,238 |
| Income taxes | \$ 2,073 | \$ 748 |
| Measurement of lease liabilities - operating cash flows | \$ 250 | \$ 318 |
| Supplemental disclosure of noncash operating activities: | | |
| Net increase in unrealized gain (loss) on investment securities, net of tax | \$ 50 | \$ 91 |
| Right-of-use assets obtained in exchange for operating lease obligations | \$ 1,615 | \$ - |

See notes to financial statements.

Partners Bank of California

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies

Nature of banking activity: Partners Bank of California (the Bank) was incorporated in the state of California and organized as a single operating segment that operates one full-service office in Mission Viejo, California, and an additional remote branch in Beverly Hills, California. The Bank's primary source of revenue is providing loans to customers who are predominantly small and middle-market businesses and individuals. The Bank's business is concentrated in Orange County and Los Angeles County, California, and is subject to the general economic conditions of these areas. The accounting and reporting policies of the Bank conform to accounting principles generally accepted in the United States of America (U.S. GAAP) and general industry practices. Certain reclassifications were made to the prior-year financial statements to conform to the current presentation. These reclassifications had no effect on previously reported net income or stockholders' equity.

The Bank grants commercial, real estate and consumer loans to its customers, substantially all of whom are small and middle-market businesses or residents in the Bank's service area. Generally, those loans are collateralized by business assets and/or real estate. Concentration of credit risk is fully described in Note 3.

Use of estimates in the preparation of financial statements: The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. A material estimate that is particularly susceptible to significant change in the near term is the allowance for loan losses. Other estimates significant to the financial statements include the realization of deferred tax assets and the fair value of financial instruments.

Cash, cash equivalents and cash flows: For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks. Cash equivalents represent short-term, highly liquid investments and include any investment with an original maturity of three months or less at the date the Bank purchases the investment. Cash flows from loans and deposits are reported net.

Cash and due from banks: Banking regulations require that banks maintain a percentage of their deposits as reserves in cash or on deposit with the Federal Reserve Bank (FRB). At December 31, 2020 and 2019, the total required reserve was \$0 and \$2,457,000, respectively.

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

Investment securities: Securities classified as available-for-sale are those debt securities that the Bank intends to hold for an indefinite period of time, but not necessarily to maturity. Any decision to sell a security classified as available-for-sale would be based on various factors, including significant movements in interest rates, changes in the maturity mix of the Bank's assets and liabilities, liquidity needs, regulatory capital considerations and other similar factors. Securities available for sale are carried at fair value. Unrealized gains or losses, net of the related deferred tax effect, are reported as other comprehensive income or loss. The amortization of premiums and accretion of discounts, computed by the interest method over the contractual lives of the related securities, are recognized in interest income. Realized gains or losses, determined on the basis of the cost of specific securities sold, are included in earnings.

Partners Bank of California

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Management evaluates securities for other-than-temporary impairment (OTTI) at least quarterly, and more frequently when economic or market conditions 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, including an evaluation of credit ratings; (3) the impact of changes in market interest rates; (4) the intent of the Bank to sell a security; and (5) whether it is more likely than not that the Bank will have to sell the security before recovery of its cost basis.

If the Bank intends to sell an impaired security, it records an other-than-temporary loss in an amount equal to the entire difference between the fair value and amortized cost. If a security is determined to be other-than-temporarily impaired, but the Bank does not intend to sell the security, only the credit portion of the estimated loss is recognized in earnings with the other portion of the loss recognized in other comprehensive income.

Loans: Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at the amount of unpaid principal, reduced by net deferred loan origination costs and fees, discounts and an allowance for loan losses. Interest is accrued daily on the outstanding balances.

The Bank originates certain loans that may be sold, in part or whole, to the secondary market. Loans that are sold in part to the secondary market consist of the guaranteed portion of Small Business Administration (SBA) loans for which servicing is retained. When loans are sold with servicing retained, servicing assets are recognized as separate assets and initially recorded at fair value. Servicing assets are amortized in proportion to, and over the period of, estimated future net servicing income. Also, at the time of the loan sale, it is the Bank's policy to recognize the related gain on the loan sale in accordance with U.S. GAAP. The Bank uses industry repayment statistics and its own prepayment experience in estimating the expected life of the loans. Management periodically evaluates servicing assets for impairment utilizing a fair value approach. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions.

Allowance for loan losses: The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that collectibility of the principal is unlikely. Subsequent recoveries, if any, are credited to the allowance.

The determination of the balance in the allowance for loan losses is based on an analysis of the loan portfolio using a systematic methodology. The allowance is an amount that management believes will be adequate to absorb probable losses on existing loans that may become uncollectible, based on evaluation of the collectibility of loans and the Bank's historical loan losses and peer bank loss experience. While management uses the best information available to make its evaluation, future adjustments to the allowance may be necessary if there are significant changes in economic or other conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan losses and may require the Bank to make additions to the allowance based on their judgment about information available to them at the time of their examinations.

Note 1. Nature of Business and Significant Accounting Policies (Continued)

The component of the allowance that covers non-impaired loans is based on historical and peer bank loss experience adjusted for current qualitative factors. The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Bank or peer banks over the most recent five years. This actual loss experience is supplemented with other qualitative factors based on the risks present for each portfolio segment. These economic factors include consideration of the following: levels of and trends in delinquencies, impaired loans, charge-offs and recoveries; effects of any changes in risk selection, underwriting standards and volume of loans; other changes in lending policies, procedures and practices; experience, ability and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; effects of changes in credit concentrations; effects of changes in quality of loan review and monitoring system; effects of changes in values of underlying collateral for collateral dependent loans; and other external factors.

When establishing the allowance for loan losses, management categorizes loans into risk categories generally based on the nature of the collateral and the basis of repayment. These risk categories and the relevant risk characteristics are as follows:

Commercial real estate loans: Commercial real estate loans are primarily secured by apartment buildings, office and industrial buildings, warehouses, small retail shopping centers and various special purpose properties, including hotels, churches, restaurants and nursing homes. Although terms vary, commercial real estate loans generally have amortization periods of 15 to 30 years, as well as balloon payments due in five to 10 years from origination, and terms that may provide that the interest rates thereon may be adjusted annually (after a fixed-rate period of up to five years) at the Bank's discretion based on a designated index. Commercial real estate loans also include construction loans, which are secured by the underlying commercial or residential real estate being developed or improved. These loans are generally disbursed as the project progresses and are due within two years from origination.

Commercial real estate and multifamily real estate loan underwriting standards are governed by the loan policies in place at the time the loan is approved. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts, and repayment of these loans is generally largely dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. The properties securing the Bank's commercial real estate portfolio are diverse in terms of type and geographic location.

Commercial and industrial loans: Commercial and industrial loans are loans, or lines of credit, for commercial, corporate and business purposes, including issued letters of credit. The Bank's commercial business loan portfolio is composed of loans for a variety of purposes and generally is secured by receivables, equipment, machinery and other business assets. Commercial business loans generally have terms of 10 years or less and may have interest rates that float in accordance with a designated published index. Substantially all such loans are secured and backed by the personal guarantees of the owners of the business.

Commercial and industrial loans are underwritten after evaluating and understanding the borrower's ability to operate profitably and prudently expand its business. The Bank's management examines current and projected cash flows to determine the ability of the borrower to repay his/her obligations as agreed. Commercial and industrial loans are primarily made based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The actual cash flows from borrowers, however, may differ from projected amounts and the collateral securing these loans may fluctuate in value.

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Consumer loans: Consumer loans generally have higher interest rates than mortgage loans. The risk involved in consumer loans is based on the type and nature of the collateral and, in certain cases, the absence of collateral. Consumer loans include secured and unsecured loans that have been made for a variety of consumer purposes. Repayment of these loans can be dependent on the employment status of the borrower.

Impaired loans: The allowance includes a specific component that relates to loans that are classified as impaired. For such loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than its carrying value.

A loan is impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified, resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings (TDR) and classified as impaired.

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

Commercial and commercial real estate loans are individually evaluated for impairment. If a loan is impaired, generally a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of the underlying collateral if repayment is expected solely from the collateral. Large groups of smaller-balance homogeneous loans, such as consumer and residential real estate loans, may collectively be evaluated for impairment and, accordingly, are not separately identified for impairment disclosures.

The TDRs are separately identified for impairment disclosures and are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a TDR is considered to be a collateral-dependent loan, the loan is reported at the fair value of the collateral. For TDRs that subsequently default, the Bank determines the amount of reserve in accordance with the accounting policy for the allowance for loan losses.

Troubled debt restructurings: A TDR is a loan for which the Bank, for reasons related to a borrower's financial difficulties, grants a concession to the borrower that the Bank would not otherwise consider. The loan terms, which have been modified or restructured due to a borrower's financial difficulty, include, but are not limited to, a reduction in the stated interest rate, an extension of the maturity at an interest rate below market, or a reduction in the face amount of the debt.

The restructured loans may be classified as "substandard." Loans that were paid current at the time of modification may be upgraded in their classification after a sustained period of repayment performance, usually six months or longer.

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Loans that are past due at the time of modification are classified “substandard” and placed on nonaccrual status. Those loans may be upgraded in their classification and placed on accrual status once there is a sustained period of repayment performance (usually six months or longer) and there is a reasonable assurance that the repayment will continue. However, such loans continue to be considered impaired. Consistent with regulatory guidance, a TDR that is subsequently modified in another restructuring agreement but has shown sustained performance and classification as a TDR, will be removed from TDR status provided that the modified terms were market based at the time of modification.

The Bank has implemented various commercial loan modification programs to provide its borrowers relief from the economic impacts of the COVID-19 pandemic. In accordance with the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), the Bank has elected to not apply TDR classification to any COVID-19 related loan modifications that were performed after March 1, 2020, to borrowers who were current as of December 31, 2019. Accordingly, these restructurings are not classified as TDRs. For loan modifications that include a payment deferral and are not TDRs, the borrowers' past due and nonaccrual status have not been impacted during the deferral period. The Bank has continued to accrue interest during the deferral period using the contractual interest that accrued during the deferral period and is payable at the maturity of the loan. The Bank includes these amounts with the unpaid principal balance when computing its allowance for credit losses.

Paycheck Protection Program: The Bank is participating in the Paycheck Protection Program (PPP), which is a loan program that originated from the CARES Act and was subsequently expanded by the Paycheck Protection Program and Health Care Enhancement Act. The PPP is designed to provide U.S. small businesses with cash-flow assistance through loans fully guaranteed by the SBA. If the borrower meets certain criteria and uses the proceeds towards certain eligible expenses, the borrower's obligation to repay the loan can be forgiven up to the full principal amount of the loan and any accrued interest. Upon borrower forgiveness, the SBA pays the Bank for the principal and accrued interest owed on the loan. If the full principal of the loan is not forgiven, the loan will operate according to the original loan terms with the 100% SBA guaranty remaining. As of December 31, 2020, the Bank had approximately 298 PPP loans with outstanding balances totaling \$94.0 million. As compensation for originating the loans, the Bank received lender processing fees from the SBA, which are capitalized, along with the loan origination costs, and are being amortized over the loans' expected lives of anticipated forgiveness date and recognized as interest income. Upon forgiveness of a loan and repayment by the SBA, any unrecognized net capitalized fees and costs related to the loan will be recognized as interest income in that period.

Transfers of financial assets: Transfers of financial assets are accounted for as sales only when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when: (1) the assets have been isolated from the Bank, (2) the transferee obtains the right to pledge or exchange the assets it received, and no condition both constrains the transferee from taking advantage of its right to pledge or exchange and provides more than a modest benefit to the transferor, and (3) the Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets. In addition, for transfers of a portion of financial assets (for example, participations of loan receivables), the transfer must meet the definition of a participating interest in order to account for the transfer as a sale. Following are the characteristics of a participating interest:

Pro rata ownership in an entire financial asset.

From the date of the transfer, all cash flows received from entire financial assets are divided proportionately among the participating interest holders in an amount equal to their share of ownership.

Partners Bank of California

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

The rights of each participating interest holder have the same priority, and no participating interest holder's interest is subordinated to the interest of another participating interest holder. That is, no participating interest holder is entitled to receive cash before any other participating interest holder under its contractual rights as a participating interest holder.

No party has the right to pledge or exchange the entire financial asset unless all participating interest holders agree to pledge or exchange the entire financial asset.

Premises and equipment: Premises and equipment are carried at cost less accumulated depreciation and amortization. Depreciation is computed using the straight-line method over the estimated useful life, which ranges from three to seven years for furniture, equipment and computer equipment. Leasehold improvements are amortized using the straight-line method over the estimated useful lives of the improvements or the remaining lease term, whichever is shorter. Expenditures for betterments or major repairs are capitalized, and those for ordinary repairs and maintenance are charged to operations as incurred.

Effective January 1, 2019, the Bank adopted Accounting Standards Update (ASU) 2016-02, *Leases (Topic 842)*, and applied the transition approach outlined in ASU 2018-11. The Bank's leases are considered operating leases. The Bank recorded a lease liability, which represents the present value of lease payments that remain unpaid as of the lease commencement date. As the Bank's leases do not provide an implicit rate, the incremental borrowing rate was used. The Bank also recorded a right-of-use asset, which represents the Bank's right to use the underlying asset for the lease term, and excludes lease incentives. The Bank made an accounting policy election not to separate lease and non-lease components of an agreement as it elected the practical expedient under Topic 842. Lease terms may include options to extend or terminate the lease when it is reasonably certain the Bank will exercise that option.

Federal Home Loan Bank and other stock: The Bank is a member of the Federal Home Loan Bank (FHLB) of San Francisco and, as such, is required to maintain a minimum investment in stock of the FHLB that varies with the level of loans eligible to be pledged and advances outstanding with the FHLB. The stock is bought from and sold to the FHLB based upon its \$100 per share par value. The stock does not have a readily determinable fair value and, as such, is classified as restricted stock and is carried at cost.

Clearinghouse Community Development Financial Institutions (CDFI): The Bank's investment in Class A common stock of CDFI totaled \$50,500 and \$50,000, for the years ended December 31, 2020 and 2019, respectively. CDFI is a for-profit institution that provides affordable housing financing to low-income communities and families in California. For the investment, the Bank receives Community Reinvestment Act (CRA) investment and lending credits. The Bank carries the Class A common stock in CDFI at cost minus impairment. The investment is included in FHLB and other stock on the statements of financial condition. The Bank completed an assessment of its investment in CDFI Class A common stock as of December 31, 2020, and did not consider its investment in CDFI to be impaired.

Interest and fees on loans: Interest on loans is recognized over the terms of the loans and is calculated using the simple-interest method on principal amounts outstanding. The accretion of discounts on loans is computed using the interest method over the contractual lives of the related loans and is recognized in interest income.

Partners Bank of California

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

For impaired loans, accrual of interest is discontinued on a loan when management believes, after considering collection efforts and other factors that the borrower's financial condition is such that collection of principal and interest is doubtful. Cash collections on impaired loans are credited to the loan receivable balance, and no interest income is recognized on those loans until the principal balance has been collected.

The Bank considers a loan to be delinquent when payments have not been made according to contractual terms, typically evidenced by nonpayment of a monthly installment by the due date. The accrual of interest on loans is discontinued at the time the loan is 90 days delinquent, unless the credit is well secured and in the process of collection.

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

Loan origination and commitment fees and certain direct loan origination costs are deferred, and the net amount is amortized as an adjustment to the related loan's yield. The Bank is generally amortizing these amounts over the contractual life of the loans.

Effective January 1, 2019, the Bank adopted ASU 2014-09, *Revenue From Contracts With Customers (Topic 606)*, using the modified retrospective approach. The adoption of the standard did not have a significant impact on the measurement, recognition, or presentation of revenue as substantially all of the Bank's revenue (based on the 2019 audited financial results) is outside the scope of this guidance.

Fees and service charges on deposit accounts include charges for analysis, overdraft, wire and ATM activities executed by the Bank's deposit clients. Fees earned from the Bank's deposit clients are governed by contracts which provide for overall custody and access to deposited funds and other related services, and can be terminated at will by either party. Fees received from deposit clients for the various deposit activities are recognized as revenue once the performance obligations are met.

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

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

The Bank is subject to the guidance for accounting for uncertainty in tax positions taken or expected to be taken on a tax return. The tax effects from an uncertain tax position can be recognized in the financial statements only if, based on its merits, the position is more likely than not to be sustained on audit by the taxing authorities. Management believes that all tax positions taken to date are highly certain, and accordingly, no accounting adjustment has been made to the financial statements. Interest and penalties related to uncertain tax positions are recorded as part of income tax provision.

Comprehensive income: Accounting standards require the disclosure of comprehensive income and its components. Changes in unrealized gain and loss on available-for-sale securities are the only components of accumulated other comprehensive income for the Bank.

Partners Bank of California

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Other off-balance-sheet instruments: In the ordinary course of business, the Bank has entered into off-balance-sheet financial instruments consisting of commitments to extend credit as described in Note 10. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received.

Disclosure of fair value of financial instruments: Accounting standards require certain fair value disclosures of financial instruments for nonpublic entities. The carrying amounts and estimated fair values of financial instruments at December 31, 2020 and 2019, are disclosed in Note 14.

Stock-based compensation: Accounting Standards Codification (ASC) Topic 718 generally requires entities to recognize the cost of employee services received in exchange for awards of stock options or other equity instruments, based on the grant-date fair value of those awards. This cost is recognized over the period in which an employee is required to provide services in exchange for the award, generally the vesting period.

Preferred stock: The Bank had authorized 1,000,000 shares with no par value and there were no shares issued or outstanding for the year ended December 31, 2019. Upon approval from the Bank's Board of Directors, the Bank filed for revocation of the preferred stock and received state approval during the year ended December 31, 2020. As a result, there are no authorized or issued preferred stock for year ended December 31, 2020.

Common stock: The Bank issued additional common stock through Private Placement Memorandum offerings exempt from registration pursuant to Section 3(a)(2) of the Securities Act of 1933 for the year ended December 31, 2019. The closing of the offering resulted in the additional issuances of 343,750 at a price of \$8.00 per share for year ended December 31, 2019. Gross proceeds from issuances totaled \$2.75 million. The proceeds are reported net of \$32,000 of incurred costs directly related to the stock offerings in the statements of changes in stockholders' equity for the year ended December 31, 2019.

Earnings per share (EPS): Basic EPS excludes dilution and is computed by dividing net income available to common stockholders by the weighted-average number of common stock outstanding for the period. Diluted EPS reflects the potential dilution that could occur if stock options or other contracts to issue common stock were exercised or converted into common stock that would then share in the earnings of the Bank.

Accounting standards issued but not yet effective: In June 2016, the Financial Accounting Standards Board (FASB) issued ASU 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which creates a new credit impairment standard for financial assets measured at amortized cost and available-for-sale debt securities. The ASU requires financial assets measured at amortized cost (including loans, trade receivables and held-to-maturity debt securities) to be presented at the net amount expected to be collected, through an allowance for credit losses that are expected to occur over the remaining life of the asset, rather than incurred losses. The ASU requires that credit losses on available-for-sale debt securities be presented as an allowance rather than as a direct write-down. The measurement of credit losses for newly recognized financial assets (other than certain purchased assets) and subsequent changes in the allowance for credit losses are recorded in the statement of income as the amounts expected to be collected change.

Partners Bank of California

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

In November 2019, the FASB issued ASU 2019-10, *Financial Instruments—Credit Losses (Topic 326), Effective Dates*, which delays the effective date of ASU 2016-13 for certain entities. In November 2019, the FASB also issued ASU 2019-11, *Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, to address issues raised by stakeholders during the implementation of ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. ASU 2019-11 clarifies the treatment of expected recoveries for amounts previously written off on purchased receivables, provides transition relief for troubled debt restructurings, and allows for certain disclosure simplifications of accrued interest. The ASU is effective for fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. Early adoption is permitted for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The Bank does not intend to early adopt. The Bank engaged the services of a third party in August 2018 to assist the Bank with the transition in accounting for estimated credit losses under the Current Expected Credit Losses standard. As a result of the issuance of ASU 2019-10 resulting in a deferral of the effective date, the Bank adjusted its implementation timeline and is currently evaluating the impact of adopting this new guidance on its financial statements.

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*, which modifies the disclosure requirements for fair value measurements by removing, modifying or adding certain disclosures. ASU 2018-13 is effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. The adoption of the standard did not have a material impact on the measurement, recognition or presentation on the Bank's fair value instruments.

In December 2019, the FASB issued ASU 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*, which is intended to simplify various aspects related to accounting for income taxes. ASU 2019-12 removes certain exceptions to the general principles in ASC 740 and also clarifies and amends existing guidance to improve consistent application. ASU 2019-12 is effective for the Bank for fiscal years beginning after December 15, 2020, and for interim periods within those fiscal years. The Bank is currently evaluating the impact of this new guidance on its financial statements.

Note 2. Investment Securities

The amortized cost of available-for-sale securities and their approximate fair values at December 31 were as follows (dollars in thousands):

| | 2020 | | | |
|--|-------------------|------------------------------|-------------------------------|------------|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| U.S. government agency residential mortgage-backed securities | \$ 2,560 | \$ 103 | \$ - | \$ 2,663 |

Partners Bank of California

Notes to Financial Statements

Note 2. Investment Securities (Continued)

| | 2019 | | | Fair Value |
|---|-----------------|------------------------|-------------------------|-----------------|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | |
| U.S. government agency residential mortgage-backed securities | \$ 4,011 | \$ 33 | \$ (5) | \$ 4,039 |
| Corporate securities | 1,501 | 2 | - | 1,503 |
| | <u>\$ 5,512</u> | <u>\$ 35</u> | <u>\$ (5)</u> | <u>\$ 5,542</u> |

There were no investment securities pledged as collateral for the Bank's FHLB of San Francisco borrowing line and FRB borrowing line for both of the years ended December 31, 2020 and 2019. The Bank did not sell any investment securities during the years ended December 31, 2020 or 2019. The Bank's corporate securities matured during the year ended December 31, 2020.

The amortized cost and estimated fair value of available-for-sale investment securities at December 31, 2020, by contractual maturities, were as follows. Expected maturities may differ from contractual maturities, as certain mortgage-backed securities and corporate securities in the Bank's available-for-sale securities portfolio can be prepaid, called or refunded without penalty (dollars in thousands).

| | Amortized Cost | Fair Value |
|---------------------------------------|-----------------|-----------------|
| Due within one year | \$ - | \$ - |
| Due after one year through five years | 1,128 | 1,171 |
| Due from five years to 10 years | 600 | 624 |
| Due after 10 years | 832 | 868 |
| Total available-for-sale securities | <u>\$ 2,560</u> | <u>\$ 2,663</u> |

The Bank had no U.S. mortgage-backed securities with an estimated fair value below the Bank's amortized cost for greater than one year as of December 31, 2020. The Bank had two U.S. mortgage-backed securities totaling \$609,000, with an estimated fair value below the Bank's amortized cost for greater than one year as of December 31, 2019. Management evaluates investment securities whose estimated fair value is below the Bank's amortized cost for OTTI, taking into consideration the extent and length of time the fair value has been less than cost, the financial condition of the issuer, and whether the Bank has the intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in fair value. Management does not believe these unrealized losses represent OTTI based on their evaluation.

Partners Bank of California

Notes to Financial Statements

Note 3. Loans and Allowance for Loan Losses

The composition of the loan portfolio at December 31 is as follows (dollars in thousands):

| | 2020 | 2019 |
|---|------------------------|------------------------|
| Loans: | | |
| Commercial real estate | \$ 174,897 | \$ 169,723 |
| Commercial and industrial | 163,265 | 70,618 |
| Consumer | 36 | 166 |
| | <hr/> 338,198 | <hr/> 240,507 |
| Net deferred loan origination costs | (634) | (212) |
| Allowance for loan losses | (6,868) | (3,612) |
| Discount on Small Business Administration loans | (108) | (148) |
| | <hr/> <hr/> \$ 330,588 | <hr/> <hr/> \$ 236,535 |

The Bank's loan portfolio consists primarily of loans to borrowers within Orange and Los Angeles Counties. Although the Bank seeks to avoid concentrations of loans to a single industry or based upon a single class of collateral, real estate-secured loans make up approximately 52% and 71% of the Bank's loan and collateral portfolios as of December 31, 2020 and 2019, respectively.

Included in commercial real estate is approximately \$3.6 million and \$5.7 million of construction loans as of December 31, 2020 and 2019, respectively.

The Bank pledged certain loans as collateral for the FHLB and FRB borrowing lines to increase liquidity. As of December 31, 2020, the unpaid principal balance of loans pledged as collateral for the Bank's FHLB and FRB borrowing lines was \$135.6 million and \$60.3 million, respectively. As of December 31, 2019, the unpaid principal balance of loans pledged as collateral for the Bank's FHLB and FRB borrowing lines was \$108.4 million and \$72.8 million, respectively.

The Bank's loan portfolio breakdown by the type presented in some of the following tables is broken out in greater detail than in the previous table. The following tables present the breakdown and grouping of loan types consistent with how the Bank internally evaluates its loan portfolio for credit risk.

For the year ended December 31, 2020, the Bank had one past due loan greater than 30 days with a balance of \$259,000. For the year ended December 31, 2019, the Bank had one past due loan greater than 30 days with a balance of \$290,000.

The recorded investment in nonaccrual loans totaled \$529,000 and \$579,000 within its commercial and industrial portfolio as of December 31, 2020 and 2019, respectively.

As part of the ongoing monitoring of the credit quality of the Bank's loan portfolio, management categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt and comply with various terms of their loan agreements. The Bank considers current financial information, historical payment experience, credit documentation, public information and current economic trends. Generally, all sizeable credits receive a financial review no less than annually to monitor and adjust, if necessary, the credit's risk profile. Credits classified as "watch" generally receive a review more frequently than annually. For "special mention," "substandard" and "doubtful" credit classifications, the frequency of review is increased in order to determine potential impact on credit loss estimates.

Partners Bank of California

Notes to Financial Statements

Note 3. Loans and Allowance for Loan Losses (Continued)

The Bank categorizes loans into the following risk categories based on relevant information about the ability of borrowers to service their debt:

Pass: A pass asset, or risk rating of 1 to 5, is well protected by the current net worth and paying capacity of the borrower (or guarantors, if any) or by the fair value, less cost to acquire and sell of any underlying collateral in a timely manner. Pass assets also include certain assets considered “watch,” which are still protected by the net worth and paying capacity of the borrower, but deserve closer attention and a higher level of credit monitoring.

Special mention: A special mention asset, or risk rating of 6, is an asset that 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 the Bank’s credit position at some future date. While a higher level of loss reserves may be established, special mention loans are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification. Credits in this category display some potential weakness that merits further monitoring. The credit risk is relatively minor, yet constitutes an unwarranted risk.

Substandard: A substandard asset, or risk rating of 7, is an asset that is inadequately protected by the current sound worth and paying capacity of the obligor and/or of the collateral pledged, if any. Substandard credits have well-defined weaknesses that may jeopardize the liquidation or timely collection of the debt. There has generally been a material deterioration in the financial condition of the Bank and/or collateral. Substandard credits have a distinct possibility of loss if the deficiencies are not corrected. Although there may not be a specific potential loss apparent in any particular substandard credit, the Bank expects to suffer some loss on the overall portfolio of substandard loans.

Doubtful: A doubtful asset, or risk rating of 8, is an asset with the same characteristics as substandard credits, but those weaknesses are so much more severe that, based on current information available, collection or liquidation in full is highly improbable. The Bank must expect that interest income will be lost as well as some portion of principal repayment. All loans classified as doubtful are to be placed on nonaccrual status. Doubtful credits have a high probability of loss, but because there is a reasonable expectation that certain events may occur within an acceptable time period (not to exceed one year) that will cure the default, a classification of “loss” is deferred until its more exact status may be determined. There is no balance to report at December 31, 2020 or 2019.

Loss: An asset, or portion thereof, classified as loss, or risk rating of 9, is considered uncollectible and of such little value that its continuance on the Bank’s books as an asset is not warranted. This does not mean that they have no recovery value. Recovery, if any, may be long-term in nature and, therefore, it is not practical or desirable to defer writing off the asset. This classification is based upon current facts, not probabilities. Loans that are classified as loss are to be charged off. There is no balance to report at December 31, 2020 or 2019.

Partners Bank of California

Notes to Financial Statements

Note 3. Loans and Allowance for Loan Losses (Continued)

The following tables present the risk category of loans evaluated by internal asset classification based on the most recent analysis performed and the contractual aging as of December 31 (dollars in thousands):

| | 2020 | | | | | |
|---------------------------|------------------------------------|------------------|-----------------|-------------|-------------|-------------------|
| | Internal Risk Rating by Loan Class | | | | | |
| | Pass | Special Mention | Substandard | Doubtful | Loss | Total |
| Commercial real estate: | | | | | | |
| Owner occupied | \$ 46,519 | \$ 2,313 | \$ 2,097 | \$ - | \$ - | \$ 50,929 |
| Investor | 82,800 | 10,755 | - | - | - | 93,555 |
| Multifamily | 24,345 | 2,408 | - | - | - | 26,753 |
| Other | 260 | - | 3,400 | - | - | 3,660 |
| Commercial and industrial | 155,695 | 5,089 | 2,481 | - | - | 163,265 |
| Consumer | 36 | - | - | - | - | 36 |
| Total | <u>\$ 309,655</u> | <u>\$ 20,565</u> | <u>\$ 7,978</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 338,198</u> |
| | | | | | | |
| | 2019 | | | | | |
| | Internal Risk Rating by Loan Class | | | | | |
| | Pass | Special Mention | Substandard | Doubtful | Loss | Total |
| Commercial real estate: | | | | | | |
| Owner occupied | \$ 61,157 | \$ 3,388 | \$ - | \$ - | \$ - | \$ 64,545 |
| Investor | 73,547 | - | - | - | - | 73,547 |
| Multifamily | 25,914 | - | - | - | - | 25,914 |
| Other | 5,717 | - | - | - | - | 5,717 |
| Commercial and industrial | 67,693 | 1,253 | 1,672 | - | - | 70,618 |
| Consumer | 166 | - | - | - | - | 166 |
| Total | <u>\$ 234,194</u> | <u>\$ 4,641</u> | <u>\$ 1,672</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 240,507</u> |

The following tables present detail of impaired loans, segregated by class, as of December 31. The unpaid principal balance represents the recorded balance prior to any partial charge-offs. The recorded investment represents customer balances, net of any partial charge-offs recognized on the loans. The interest income recognized represents all interest income reported either on a cash or accrual basis after the loan became impaired (dollars in thousands).

| | 2020 | | | | |
|-----------------------------|--------------------------|---------------------|-------------------------------------|-----------------------------|----------------------------|
| | Impaired Loans | | | | |
| | Unpaid Principal Balance | Recorded Investment | Allowance for Loan Losses Allocated | Average Recorded Investment | Interest Income Recognized |
| With an allowance recorded: | | | | | |
| Commercial and industrial | \$ 619 | \$ 529 | \$ 313 | \$ 555 | \$ - |

Partners Bank of California

Notes to Financial Statements

Note 3. Loans and Allowance for Loan Losses (Continued)

| | 2019 | | | | |
|-------------------------------------|--------------------------|---------------------|-------------------------------------|-----------------------------|----------------------------|
| | Impaired Loans | | | | |
| | Unpaid Principal Balance | Recorded Investment | Allowance for Loan Losses Allocated | Average Recorded Investment | Interest Income Recognized |
| With no related allowance recorded: | | | | | |
| Commercial and industrial | \$ 300 | \$ 289 | \$ - | \$ 294 | \$ - |
| With an allowance recorded: | | | | | |
| Commercial and industrial | 347 | 290 | 163 | 312 | - |
| Total | \$ 647 | \$ 579 | \$ 163 | \$ 606 | \$ - |

There was no income recognized on a cash basis on impaired loans in 2020 or 2019.

The following tables provide additional detail of the activity in the allowance for loan losses, by portfolio segment, for the years ended December 31 (dollars in thousands):

| | 2020 | | | |
|---------------------------------------|--|---------------------------|----------|------------|
| | Allowance for Loan Losses and Unpaid Principal Balance and Recorded Balance of Loans | | | |
| | Commercial Real Estate | Commercial and Industrial | Consumer | Total |
| Allowance for loan losses: | | | | |
| Beginning balance | \$ 2,921 | \$ 691 | \$ - | \$ 3,612 |
| Charge offs | - | - | - | - |
| Recoveries | - | 94 | - | 94 |
| Provision | 2,068 | 1,094 | - | 3,162 |
| Ending balance | \$ 4,989 | \$ 1,879 | \$ - | \$ 6,868 |
| Allowance allocated to: | | | | |
| Individually evaluated for impairment | \$ - | \$ 313 | \$ - | \$ 313 |
| Collectively evaluated for impairment | 4,989 | 1,566 | - | 6,555 |
| Ending balance | \$ 4,989 | \$ 1,879 | \$ - | \$ 6,868 |
| Loans: | | | | |
| Individually evaluated for impairment | \$ - | \$ 313 | \$ - | \$ 313 |
| Collectively evaluated for impairment | 174,897 | 162,952 | 36 | 337,885 |
| Ending balance | \$ 174,897 | \$ 163,265 | \$ 36 | \$ 338,198 |

Partners Bank of California

Notes to Financial Statements

Note 3. Loans and Allowance for Loan Losses (Continued)

| | 2019 | | | |
|---------------------------------------|---|------------------------------|---------------|-------------------|
| | Allowance for Loan Losses and Unpaid Principal Balance and Recorded Balance of Loans | | | |
| | Commercial Real Estate | Commercial and Industrial | Consumer | Total |
| Allowance for loan losses: | | | | |
| Beginning balance | \$ 2,091 | \$ 1,121 | \$ 2 | \$ 3,214 |
| Charge offs | - | (37) | - | (37) |
| Recoveries | - | 109 | - | 109 |
| Provision | 830 | (502) | (2) | 326 |
| Ending balance | <u>\$ 2,921</u> | <u>\$ 691</u> | <u>\$ -</u> | <u>\$ 3,612</u> |
| Allowance allocated to: | | | | |
| Individually evaluated for impairment | \$ - | \$ 163 | \$ - | \$ 163 |
| Collectively evaluated for impairment | 2,921 | 528 | - | 3,449 |
| Ending balance | <u>\$ 2,921</u> | <u>\$ 691</u> | <u>\$ -</u> | <u>\$ 3,612</u> |
| Loans: | | | | |
| Individually evaluated for impairment | \$ - | \$ 579 | \$ - | \$ 579 |
| Collectively evaluated for impairment | 169,723 | 70,039 | 166 | 239,928 |
| Ending balance | <u>\$ 169,723</u> | <u>\$ 70,618</u> | <u>\$ 166</u> | <u>\$ 240,507</u> |

There were no modifications that were deemed new TDRs during the years ended December 31, 2020 or 2019. There was no principal forgiven on TDRs in 2020 or 2019. There are no commitments to lend additional funds to borrowers whose terms have been modified in TDRs as of December 31, 2020 or 2019. TDR loans at December 31, 2020 and 2019, totaled \$259,000 and \$290,000, respectively.

In accordance with the CARES Act, the Bank modified loan terms for borrowers that were adversely impacted by the COVID-19 pandemic. These modifications generally consisted of three to six months of payment deferrals. Total unpaid principal balance for borrowers that received these modifications was approximately \$67.4 million during the year ended December 31, 2020. The Bank elected to not apply TDR classification for these loans as permitted by the CARES Act.

Note 4. Premises, Equipment and Leases

A summary of premises and equipment as of December 31 is as follows (dollars in thousands):

| | 2020 | 2019 |
|--|---------------|---------------|
| Leasehold improvements | \$ 71 | \$ 122 |
| Furniture, fixtures and equipment | 1,138 | 1,368 |
| | <u>1,209</u> | <u>1,490</u> |
| Less accumulated depreciation and amortization | (770) | (1,121) |
| | <u>\$ 439</u> | <u>\$ 369</u> |

Partners Bank of California

Notes to Financial Statements

Note 4. Premises, Equipment and Leases (Continued)

The Bank leases its headquarters and a branch office under one lease that expired in October 2020. The Bank renewed the lease effective November 2020 that expires in April 2026. The Bank also has a lease agreement for an additional office location with a commencement date of December 15, 2018, that expires in January 2022. Both leases include provisions for periodic rent increases, as well as payment by the lessee of certain operating expenses that exceed the base year amount. The leases also include provisions for options to extend the lease, with renewal terms that can extend the lease term by up to five years.

For the years ended December 31, 2020 and 2019, the lease liability totaled \$1.6 million and \$411,000, respectively, with a right-of-use asset of \$1.5 million and \$357,000, respectively. For the years ended December 31, 2020 and 2019, the weighted average remaining lease term was 2.76 years and 0.77 years, respectively, with a weighted average discount rate of 3.26% and 5.17%, respectively. For years ended December 31, 2020 and 2019, lease liabilities are included in accrued interest and other liabilities while the right-of-use assets are included in accrued interest and other assets in the statements of financial condition. The recognition or measurement of lease expense on the statements of income and presentation on the statements of cash flows was not materially impacted.

At December 31, 2020, the future minimum lease payments under operating leases are as follows (dollars in thousands):

| | |
|-------------------------------------|------------------------|
| Years ending December 31: | |
| 2021 | \$ 325 |
| 2022 | 318 |
| 2023 | 320 |
| 2024 | 331 |
| 2025 and thereafter | 461 |
| Total future minimum lease payments | <u>1,755</u> |
| Less imputed interest | (133) |
| Total | <u><u>\$ 1,622</u></u> |

The minimum rental payments shown above are given for the existing lease obligations and are not a forecast of future rental expense. Total rental expense, recognized on a straight-line basis, at December 31, 2020 and 2019, was approximately \$368,000 and \$323,000, respectively.

Note 5. Deposits

At December 31, 2020, the scheduled maturities of time deposits are as follows (dollars in thousands):

| | |
|---------------------------|-------------------------|
| Years ending December 31: | |
| 2021 | \$ 14,922 |
| 2022 | 3,650 |
| 2023 | 220 |
| 2024 | 10,190 |
| 2025 | 745 |
| | <u><u>\$ 29,727</u></u> |

Partners Bank of California

Notes to Financial Statements

Note 5. Deposits (Continued)

As of December 31, 2020 and 2019, the Bank's brokered deposits totaled \$15.8 million and \$10.5 million, respectively. As of December 31, 2020 and 2019, there was one deposit relationship consisting of multiple trust accounts totaling \$47.9 million, or 14.9%, of total deposits, and \$46.9 million, or 19.9%, of total deposits, respectively. As of December 31, 2020 and 2019, there was one additional large deposit relationship in excess of 5% of total deposits, totaling \$28.9 million, or 9.0%, of total deposits and \$15.3 million, or 6.5%, of total deposits, respectively.

Note 6. Employee Benefit Plan

The Bank adopted a 401(k) plan for its employees in 2008. Under the plan, eligible employees may defer a portion of their salaries. The plan also provides for discretionary Bank profit sharing contributions. The Bank made \$145,000 and \$136,000 in contributions to the plan for the years ended December 31, 2020 and 2019, respectively.

Note 7. Borrowing Arrangements and Secured Borrowings

The Bank may borrow up to \$7.5 million overnight on an unsecured basis from its correspondent banks. The Bank may also borrow from the FHLB and the FRB, subject to providing adequate collateral and fulfilling other conditions of the credit facility. There was a combined \$188.5 million and \$101.1 million of available borrowings under the FHLB and FRB facilities as of December 31, 2020 and 2019, respectively.

The Bank had outstanding balances at FHLB as of December 31, 2020. The outstanding balances below by maturity and weighted average interest rates as of December 31, 2020, are as follows (in thousands):

| | 2020 | |
|------------------------------|------------------|--------------------------------|
| | Balance | Weighted-Average Interest Rate |
| Zero to one years maturity | \$ 16,000 | 0.12% |
| One to two years maturity | 15,000 | 1.33% |
| Two to three years maturity | 5,000 | 0.84% |
| Three to four years maturity | 5,000 | 0.76% |
| Four to five years maturity | 5,000 | 0.95% |
| | <u>\$ 46,000</u> | |

As of December 31, 2019, there was \$38 million of outstanding FHLB borrowings at an interest rate of 1.66% that matured and was repaid in full on January 2, 2020.

Partners Bank of California

Notes to Financial Statements

Note 8. Income Taxes

Income tax provision consists of the following for the years ended December 31 (dollars in thousands):

| | 2020 | 2019 |
|--------------------------------------|---------------|-----------------|
| Current provision: | | |
| Federal | \$ 1,240 | \$ 668 |
| State | 740 | 305 |
| Total current provision | <u>1,980</u> | <u>973</u> |
| Deferred provision: | | |
| Federal | (602) | 58 |
| State | (393) | 27 |
| Total deferred provision | <u>(995)</u> | <u>85</u> |
| Total current and deferred provision | <u>\$ 985</u> | <u>\$ 1,058</u> |

Deferred taxes are a result of differences between income tax accounting and U.S. GAAP with respect to income and expense recognition. The following is a summary of the components of the net deferred tax asset accounts recognized in the accompanying statements of financial condition at December 31 (dollars in thousands):

| | 2020 | 2019 |
|-------------------------------|-----------------|---------------|
| Deferred tax assets: | | |
| Pre-opening expenses | \$ 87 | \$ 117 |
| Allowance for loan losses | 1,781 | 840 |
| Stock-based compensation | 187 | 140 |
| Other | 144 | 136 |
| | <u>2,199</u> | <u>1,233</u> |
| Deferred tax liabilities: | | |
| Unrealized gain on investment | (15) | (9) |
| Other | (370) | (399) |
| | <u>(385)</u> | <u>(408)</u> |
| Net deferred tax assets | <u>\$ 1,814</u> | <u>\$ 825</u> |

The Bank has no net operating loss carryforwards at December 31, 2020, for federal income tax or California franchise tax purposes.

The Bank is subject to federal income tax and franchise tax of the state of California. Federal income tax returns for the years ended December 31, 2018, through 2020, are open to audit by the federal tax authorities, and the Bank's state tax returns for the years ended December 31, 2018, through 2020, are open to audit by the California state tax authorities.

Management believes that there is no valuation allowance required as of December 31, 2020 or 2019.

Partners Bank of California

Notes to Financial Statements

Note 9. Other Expenses

Other expenses as of December 31 consist of the following (dollars in thousands):

| | 2020 | 2019 |
|-----------------------------------|-----------------|-----------------|
| Legal and professional | \$ 667 | \$ 673 |
| Data processing | 405 | 360 |
| Marketing and business promotion | 119 | 221 |
| Regulatory assessments | 144 | 69 |
| Office expenses | 150 | 136 |
| Nonemployee stock compensation | 159 | 112 |
| Training and seminars | 17 | 25 |
| Recovery for unfunded commitments | (22) | (6) |
| Other | 289 | 178 |
| | <u>\$ 1,928</u> | <u>\$ 1,768</u> |

Note 10. Commitments and Contingencies

Financial instruments with off-balance-sheet risk: In the ordinary course of business, the Bank enters into financial commitments to meet the financing needs of its customers, primarily through commitments to extend credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk not recognized in the Bank's financial statements.

The Bank's exposure to loan loss in the event of nonperformance on 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 reflected in the financial statements.

As of December 31, the Bank had the following outstanding financial commitments whose contractual amount represents credit risk (dollars in thousands):

| | 2020 | 2019 |
|--|------------------|------------------|
| Commitments to extend credit | \$ 35,006 | \$ 37,305 |
| Commitments on standby letters of credit | 1,771 | 8,227 |
| | <u>\$ 36,777</u> | <u>\$ 45,532</u> |

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Standby letters of credit are conditional commitments to guarantee the performance of a Bank customer to a third party. Since many of the commitments and standby letters of credit are expected to expire without being drawn upon, the total amounts do not necessarily represent future cash requirements. The Bank evaluates each client's creditworthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Bank is based on management's credit evaluation of the customer. A reserve for commitments to extend credit has been established and totals \$92,000 and \$114,000 as of December 31, 2020 and 2019, respectively, and is included in accrued interest and other liabilities in the statements of financial condition.

Partners Bank of California

Notes to Financial Statements

Note 10. Commitments and Contingencies (Continued)

Contingencies: Because of the nature of its activities, the Bank may be subject to various pending and threatened legal actions, which may arise in the ordinary course of business. The Bank's management is not aware of any such matters that would result in a material exposure to the Bank as of December 31, 2020 or 2019.

Financial instruments with concentrations of credit risk: The Bank focuses on commercial and commercial real estate lending to customers primarily in Orange County and Los Angeles County. The Bank's loan portfolio includes credit exposure to the real estate market of these areas and upon the economic viability of these areas. The majority of real estate loans are secured by first liens with an initial loan-to-value ratio of generally not more than 70%.

Note 11. Related-Party Transactions

In the ordinary course of business, the Bank has granted loans to certain officers and directors and the companies with which they are associated. In the Bank's opinion, all loans and loan commitments to such parties are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time of comparable transactions with other persons. The total commitment of these loans for December 31, 2020 and 2019, was approximately \$6.2 million and \$5.4 million, and the outstanding balance was \$2.9 million and \$4.1 million as of December 31, 2020 and 2019, respectively. Advances for these loans for the years ended December 31, 2020 and 2019, were \$5.0 million and \$3.5 million, respectively, while repayments on these loans for the years ended December 31, 2020 and 2019, totaled \$5.8 million and \$6.3 million, respectively. For the years ended December 31, 2020 and 2019, former directors' loans with a combined outstanding balance of \$0.4 million and \$3.5 million, respectively, were not included in the related-party total. For the same loans, there were \$3.2 million and \$969,000 of repayments during the years ended December 31, 2020 and 2019, respectively, and \$3.1 million and \$1.0 million of advances during the years ended December 31, 2020 and 2019, respectively.

Note 12. Stock Option Plan

The Bank's 2007 Equity-Based Compensation Plan (the 2007 Plan) was approved by its stockholders in November 2007. During the year ended December 31, 2018, the 2007 Plan expired and the Bank issued a new 2018 Equity-Based Compensation Plan (the 2018 Plan) that was approved by its stockholders in May 2018. These plans will be collectively referred to as the Plans. The disclosures and tables below include awards issued and outstanding under both plans. Under the terms of the Plans, officers and key employees may be granted nonqualified stock options, incentive stock options and restricted stock awards, and directors and organizers, who are not also an officer or employee, may only be granted nonqualified stock options. Prior to its expiration, the 2007 Plan provided for options and restricted stock awards of 569,000 shares of common stock. The 2018 Plan provided for an additional 131,000 shares for a total of 700,000 shares of common stock. The Plans require stock options to have a price no less than 100% of the fair market value of the stock on the date of grant. During the year ended December 31, 2019, the 2018 Plan was amended to increase the maximum aggregate number of shares to 1,000,000.

For the years ended December 31, 2020 and 2019, the Bank had 80,532 and 209,216 shares of common stock available to be issued under the 2018 Plan combined for both stock options and restricted stock, respectively. Stock options for the Plans expire no later than 10 years from the date of grant and generally vest over three years. The Bank determines that recognizing compensation costs ratably over a three-year vesting period is appropriate with one-third of the value of the award recognized each year. The Plans provide for accelerated vesting if there is a change of control, as defined in the Plans. The Bank recognized stock-based compensation cost of \$332,000 and \$251,000 in 2020 and 2019, respectively, related to the Plans.

Partners Bank of California

Notes to Financial Statements

Note 12. Stock Option Plan (Continued)

Since the Bank has a limited amount of historical stock activity, the expected volatility is based on the historical volatility of similar banks that have a longer trading history. The expected term represents the estimated average period of time that the options remain outstanding. Since the Bank does not have sufficient historical data on the exercise of stock options, the expected term is based on the “simplified” method that measures the expected term as the approximate average of the vesting period and the contractual term. The risk-free rate of return reflects the grant-date interest rate offered for zero coupon U.S. Treasury bonds over the expected term of the options. The intrinsic value for the outstanding stock options that have been granted were \$1.7 million and \$1.4 million for the years ended December 31, 2020 and 2019, respectively.

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

| | 2020 | 2019 |
|--|-------------|-------------|
| Expected volatility | 23.8%-25.4% | 23.8%-28.8% |
| Expected term | 7 years | 7 years |
| Expected dividends | None | None |
| Risk-free rate | 0.37%-1.39% | 1.69%-2.23% |
| Weighted-average grant-date fair value | \$ 2.62 | \$ 2.65 |

A summary of the status of the Bank’s stock option grants as of December 31 and changes during the years ended thereon is presented below:

| | Shares | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term (Years) |
|--|----------|---------------------------------|---|
| Outstanding, December 31, 2018 | 602,175 | \$ 6.17 | 7.7 |
| Granted | 132,150 | 8.96 | - |
| Exercised | (82,571) | 5.02 | - |
| Forfeited or expired | (19,866) | 6.86 | - |
| Outstanding, December 31, 2019 | 631,888 | 6.86 | 7.5 |
| Granted | 147,000 | 9.57 | - |
| Exercised | - | - | - |
| Forfeited or expired | (18,316) | 8.57 | - |
| Outstanding, December 31, 2020 | 760,572 | \$ 7.34 | 7.2 |
| Options exercisable at December 31, 2020 | 485,585 | \$ 6.36 | 5.9 |

As of December 31, 2020, there was \$736,000 of total unrecognized compensation cost related to the outstanding stock options that will be recognized over a weighted-average period of 2.3 years.

Partners Bank of California

Notes to Financial Statements

Note 12. Stock Option Plan (Continued)

The Plans also allow for the granting of restricted stock awards. Under the Plans, grants may include vesting periods up to 10 years. There were no grants of restricted stock during the years ended December 31, 2020 or 2019, and there were no nonvested restricted stock as of December 31, 2020 or 2019.

Note 13. Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of 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.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum capital amounts and ratios (set forth in the table below, as defined in the regulations) of Total and Tier 1 capital to risk-weighted assets, Tier 1 capital to average assets and Common equity Tier 1 capital to risk-weighted assets. Management believes, as of December 31, 2020 and 2019, that the Bank met all capital adequacy requirements to which it was subject.

As of December 31, 2020, the most recent notification from the Federal Deposit Insurance Corporation (FDIC) categorized the Bank as well-capitalized under the regulatory framework for prompt corrective action (there are no conditions or events since that notification that management believes have changed the Bank's category). To be categorized as well-capitalized, the Bank must maintain minimum ratios as set forth in the table below. The following table also sets forth the Bank's actual capital amounts and ratios (dollars in thousands):

| | Actual | | For Capital Adequacy Purposes | | To be Well-Capitalized Under Prompt Corrective Action Provisions | |
|--|-----------|--------|-------------------------------|-------|--|-------|
| | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| As of December 31, 2020: | | | | | | |
| Total capital (to risk-weighted assets) | \$ 38,763 | 16.06% | \$ 19,309 | 8.0% | \$ 24,136 | 10.0% |
| Tier 1 capital (to risk-weighted assets) | 35,697 | 14.79% | 14,482 | 6.0% | 19,309 | 8.0% |
| Common equity Tier 1 capital ratio | 35,697 | 14.79% | 10,861 | 4.5% | 15,688 | 6.5% |
| Tier 1 capital (to average assets) | 35,697 | 8.80% | 16,221 | 4.0% | 20,275 | 5.0% |
| As of December 31, 2019: | | | | | | |
| Total capital (to risk-weighted assets) | \$ 36,286 | 14.64% | \$ 19,829 | 8.0% | \$ 24,786 | 10.0% |
| Tier 1 capital (to risk-weighted assets) | 33,180 | 13.39% | 14,872 | 6.0% | 19,829 | 8.0% |
| Common equity Tier 1 capital ratio | 33,180 | 13.39% | 11,154 | 4.5% | 16,111 | 6.5% |
| Tier 1 capital (to average assets) | 33,180 | 11.74% | 11,306 | 4.0% | 14,133 | 5.0% |

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

Note 13. Regulatory Matters (Continued)

In early July 2013, the Federal Reserve Board and the FDIC issued final rules implementing the Basel III regulatory capital framework and related Dodd-Frank Wall Street Reform and Consumer Protection Act changes. The rules revised minimum capital requirements and adjusted prompt correct action thresholds. The final rules revised the regulatory capital elements, added a new common equity Tier 1 capital ratio, increased the minimum Tier 1 capital ratio requirement and implemented a new capital conservation buffer. The rules also permitted certain banking organizations to retain, through a one-time election, the existing treatment for accumulated other comprehensive income. The final rules took effect for community banks on January 1, 2015, subject to a transition period for certain parts of the rules.

Note 14. Fair Value Information

ASC 820 defines fair value, establishes a framework for measuring fair value in U.S. GAAP and expands disclosures about fair value measurements. Fair value is defined as the price that would be received for an asset or paid to transfer a liability (an exit price) in the principal market for the asset or liability in an orderly transaction between market participants on the measurement date. In support of this principle, ASC 820 establishes a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

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

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

Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset and liability.

For the years ended December 31, 2020 and 2019, the application of valuation techniques applied to similar assets and liabilities has been consistent.

In determining the appropriate levels, the Bank performs a detailed analysis of the assets and liabilities subject to fair value measurement. At each reporting period, all assets and liabilities for which the fair value measurement is based on significant unobservable inputs are classified as Level 3.

The following is a description of the Bank's methodologies used to measure and disclose the fair value of its financial assets and liabilities on a recurring and nonrecurring basis:

Investment securities, including U.S. government agency mortgage-backed securities and corporate securities: The 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. The fair value of Level 2 investment securities is the market value based on market prices provided by an independent third-party pricing service whose methodologies are based on broker-provided pricings. When quoted market prices are not available, the fair values are estimated using third-party vendor pricing models that would be classified within Level 2 of the valuation hierarchy. However, the fair value reported may not be indicative of the amounts that could be realized in an actual market exchange.

Partners Bank of California

Notes to Financial Statements

Note 14. Fair Value Information (Continued)

Impaired loans: Impaired loans are generally measured using the fair value of the underlying collateral, which is determined based on the most recent appraisal information received. These loans fall within Level 2 of the fair value hierarchy. Appraised values may be adjusted based on factors such as the changes in market conditions from the time of valuation. These loans fall within Level 3 of the fair value hierarchy. For impaired loans for which the credit is substantially unsecured and not considered collateral dependent, the estimated future discounted cash flows of the business or borrower are used in evaluating the fair value. Impaired loans are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly, based on the same factors identified above.

The following tables present information about the Bank's assets and liabilities measured at fair value on a recurring and nonrecurring basis as of December 31 and indicates the fair value hierarchy of the valuation techniques utilized by the Bank to determine such fair value (dollars in thousands):

| | | 2020 | | | |
|--|----|--|--|---|--|
| | | Assets Measured at Fair Value on a Recurring Basis (Dollars in Thousands) | | | |
| | | Total | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| U.S. government agency residential mortgage-backed securities | \$ | 2,663 | \$ - | \$ 2,663 | \$ - |
| | | 2019 | | | |
| | | Assets Measured at Fair Value on a Recurring Basis (Dollars in Thousands) | | | |
| | | Total | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| U.S. government agency residential mortgage-backed securities | \$ | 4,039 | \$ - | \$ 4,039 | \$ - |
| Corporate securities | | 1,503 | - | 1,503 | - |
| | | \$ 5,542 | \$ - | \$ 5,542 | \$ - |

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Notes to Financial Statements

Note 14. Fair Value Information (Continued)

| | Assets Measured at Fair Value on a Nonrecurring Basis (Dollars in Thousands) | | | |
|--|---|--------------------------------------|-----------------------------------|---------------------|
| | Carrying Value at December 31 | Quoted Prices in | Significant | Significant |
| | | Active Markets | Other | Unobservable |
| | | for Identical Assets (Level 1) | Observable Inputs (Level 2) | Inputs (Level 3) |
| Cash flow- and collateral-dependent impaired loans, including loans with partial charge-offs, 2020 | \$ 529 | \$ - | \$ - | \$ 529 |
| Cash flow- and collateral-dependent impaired loans, including loans with partial charge-offs, 2019 | \$ 579 | \$ - | \$ - | \$ 579 |

The table below presents the carrying amounts and estimated fair values of financial instruments at December 31 (dollars in thousands):

| | 2020 | | 2019 | |
|---|--------------------|------------|--------------------|------------|
| | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| Financial assets: | | | | |
| Cash and cash equivalents | \$ 66,126 | \$ 66,126 | \$ 61,961 | \$ 61,961 |
| Investment securities available for sale | 2,663 | 2,663 | 5,542 | 5,542 |
| Loans, net | 330,588 | 331,902 | 236,535 | 236,300 |
| FHLB and other stock | 1,601 | 1,601 | 1,265 | 1,265 |
| Accrued interest receivable | 1,416 | 1,416 | 614 | 614 |
| Financial liabilities: | | | | |
| Noninterest-bearing demand deposit accounts | 147,707 | 147,707 | 102,466 | 102,466 |
| Savings, NOW and money market accounts | 144,256 | 144,256 | 106,628 | 106,628 |
| Time deposit accounts | 29,727 | 29,874 | 25,832 | 25,957 |
| Borrowings | 46,000 | 46,226 | 38,000 | 38,000 |
| Accrued interest payable | 49 | 49 | 56 | 56 |

Cash and cash equivalents: The carrying amounts reported in the statements of financial condition for cash and due from banks and interest-bearing deposits in other banks approximate their fair value.

Loans: For variable-rate loans that reprice frequently and have experienced no significant change in credit risk, fair value is based on the next repricing date relative to current market offerings by the Bank for such repricing period. Fair value for all other loans is estimated based on discounted cash flows, using interest rates currently being offered for loans with similar terms to borrowers with similar credit quality and for the same remaining maturities. Prepayments prior to the repricing date are not expected to be significant. Loans are expected to be held to maturity, and any unrealized gains or losses are not expected to be realized.

Note 14. Fair Value Information (Continued)

The fair value of loans on nonaccrual status has not been specifically estimated because it is not practicable to reasonably assess the credit risk adjustment that would be applied in the marketplace for such loans. As such, the estimated fair value of total loans at December 31, 2020 and 2019, includes the carrying amount of nonaccrual loans at each respective date, net of allowance for loan losses.

FHLB and other stock: The carrying amounts reported in the statements of financial condition for the Bank's investment in FHLB and CDFI nonmarketable common stock approximate fair value.

Deposit liabilities: Fair value disclosed for demand deposits equals their carrying amounts, which represent the amount payable on demand. The fair values disclosed for deposits with no defined maturities, which include the Bank's money market deposit accounts, NOW and savings accounts, are equal to their carrying amounts, which represent the amounts payable on demand. Fair value for fixed-rate certificates of deposit is estimated using a discounted cash flow calculation that applies interest rates currently being offered by the Bank as well as by a representative peer group on certificates to a schedule of aggregate expected monthly maturities on time deposits. Early withdrawal of fixed-rate certificates of deposit is not expected to be significant.

Borrowings: The fair value of borrowings is estimated using a discounted cash flow calculation that applies interest rates currently being offered to the Bank to a schedule of expected maturities of the respective borrowings.

Accrued interest receivable and payable: The fair values of accrued interest receivable and payable approximate their carrying amounts.

Fair value of commitments: The estimated fair value of fee income on letters of credit at December 31, 2020 and 2019, is insignificant. Loan commitments on which the committed interest rate is less than the current market rate are also insignificant at December 31, 2020 and 2019.

Interest rate risk: The Bank assumes interest rate risk (the risk that general interest rate levels will change) as a result of its normal operations. As a result, fair value of the Bank's financial instruments will change when interest rate levels change and that change may be either favorable or unfavorable to the Bank. Management attempts to match maturities of assets and liabilities to the extent believed necessary to minimize interest rate risk. However, borrowers with fixed-rate obligations are less likely to prepay in a rising rate environment and more likely to prepay in a falling rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by adjusting terms of new loans and deposits and by investing in securities with terms that mitigate the Bank's overall interest rate risk.

Partners Bank of California

Notes to Financial Statements

Note 15. Earnings Per Share

The following table shows how the Bank computed basic and diluted EPS for the years ended December 31 (in thousands, except per share data):

| | 2020 | 2019 |
|---|-----------------|-----------------|
| Numerator: | | |
| Net income | \$ 2,166 | \$ 2,064 |
| Dividends on preferred stock | - | - |
| Net income available to common stockholders | <u>\$ 2,166</u> | <u>\$ 2,064</u> |
| Denominator: | | |
| Basic weighted-average outstanding common stock | 4,302 | 4,059 |
| Dilutive effect of stock options | 80 | 60 |
| Diluted weighted-average common stock and equivalents | <u>4,382</u> | <u>4,119</u> |
| Basic net income per common share | <u>\$ 0.50</u> | <u>\$ 0.51</u> |
| Diluted net income per common share | <u>\$ 0.49</u> | <u>\$ 0.50</u> |

For the years ended December 31, 2020 and 2019, weighted-average shares totaling 194,000 and 182,000, respectively, had an antidilutive effect in the calculation of diluted net income per share and have been excluded from the computations above.

Note 16. Subsequent Events

Subsequent events have been evaluated for potential recognition and disclosure through February 22, 2021, the date the financial statements were available to be issued.

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