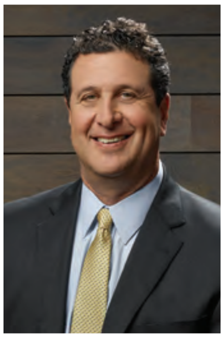
AMERICAN BUSINESS BANK

2019 ANNUAL REPORT

OUR SUCCESS IS YOUR SUCCESS



The year 2019 was a record-breaking year for American Business Bank in every way. For the year ended 2019, we posted increases in assets of 11 % or $244MM, loans outstanding of 19% or $237MM, and reported net income of $22.1MM. The Bank continues to be well capitalized.

But that was last year. Today, we are in the midst of something different, something no one saw coming. Back when a full blown pandemic was just an outside possibility, we opted to go "all in" for our employees, enabling a remote workforce for over 95% of our total employee population, sending them offsite to work in safe, and secure, environments. We believed that prioritizing their health and safety was the right thing to do; the result was that all banking and operational departments continued functioning at full capacity doing the work of the Bank for our customers who too were facing their own challenges.

With all the uncertainty surrounding the COVID-19 virus and the change in societal norms as we know them, collaboration between our Bank and our clients became ever more critical. It came naturally. For us, the term "our clients" doesn't refer to a list of customers. Instead, it means that we have an obligation to each of you - to do the right thing for you, particularly when it matters most. In everyday circumstances our aim is to be there for our clients, whatever that may entail. And when the going gets tough we are proud to be in a position to respond to you with urgency and thoughtfulness.

Doing the right thing starts with maintaining a strong bank. American Business Bank was made for times like these. Our fortress balance sheet and extraordinary culture of service were built and are maintained to assure you that we will be there when you need us the most. That has never been more true than it is today. This crisis will pass and together we will find our new normal. Some things will permanently change, but the fundamentals won't. It's important for us to remember now, more than ever, the importance of relationships – with our families, our friends and with our business associates. American Business Bank will continue to put clients at the center of every decision we make, and we want you to know that we appreciate our relationship with each and every one of you.

I wish you good health and thank you for your ongoing support.

in Your Service,
Leon Blankstein
President, Chief Executive Officer, Director

AMERICAN BUSINESS BANK

Financial Statements and Report of Independent Certified Public Accountants

December 31, 2019 and 2018

American Business Bank

Contents

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors
American Business Bank

We have audited the accompanying financial statements of American Business Bank, which comprise the balance sheets as of December 31, 2019 and 2018, and the related statements of income, comprehensive income, shareholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

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

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

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

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

Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of American Business Bank as of December 31, 2019 and 2018, 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.

Emphasis of matter

As discussed in Note A to the financial statements, American Business Bank has adopted new accounting guidance in 2019 related to the accounting for leases which requires a lessee to recognize a right of use asset and lease liability on the balance sheet. Our opinion is not modified with respect to this matter.

Grant Thornton LLP

Newport Beach, California
March 27, 2020

American Business Bank

BALANCE SHEETS

For the years ended December 31,

ASSETS	2019	2018
Cash and due from banks	$ 31,903,278	$ 26,911,365
Interest earning deposits in other financial institutions	44,471,527	76,110,728
Cash and cash equivalents	76,374,805	103,022,093
Certificates of deposit in other financial institutions	500,000	250,000
Securities available-for-sale, at fair value	684,492,717	658,354,332
Securities held-to-maturity, at amortized cost	86,707,383	87,526,084
Federal Home Loan Bank stock, at cost	10,356,200	10,356,200
Loans receivable	1,487,378,818	1,250,261,298
Allowance for loan losses	(20,823,570)	(17,503,154)
Loans receivable, net	1,466,555,248	1,232,758,144
Furniture, equipment and leasehold improvements, net	9,023,108	1,833,687
Bank/corporate owned life insurance	26,448,129	25,328,113
Deferred income tax assets, net	14,382,145	17,983,236
Accrued interest receivable and other assets	27,071,277	20,031,045
Total assets	$ 2,401,911,012	$ 2,157,442,934
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits		
Non-interest bearing demand deposits	$ 1,083,704,912	$ 983,283,654
Interest bearing transaction accounts	215,729,548	211,794,286
Money market and savings deposits	827,712,736	728,236,757
Certificates of deposit	37,712,153	50,443,414
Total deposits	2,164,859,349	1,973,758,111
Accrued interest payable and other liabilities	30,386,241	18,617,425
Total liabilities	2,195,245,590	1,992,375,536
Commitments and contingencies		
Shareholders' equity		
Common stock, no par value; authorized, 15,000,000 shares; issued and outstanding, 7,850,171 and 7,705,590 shares at December 31, 2019 and 2018, respectively	163,872,321	154,709,805
Accumulated other comprehensive loss	(3,991,355)	(17,096,863)
Retained earnings	46,784,456	27,454,456
Total shareholders' equity	206,665,422	165,067,398
Total liabilities and shareholders' equity	$ 2,401,911,012	$ 2,157,442,934

The accompanying notes are an integral part of these statements.

American Business Bank

STATEMENTS OF INCOME

For the years ended December 31,

	2019	2018
Interest income		
Interest and fees on loans	$ 64,834,582	$ 49,738,104
Investment securities	16,620,249	19,007,474
Interest earning deposits in other financial institutions	1,627,765	1,419,878
Total interest income	83,082,596	70,165,456
Interest expense		
Interest bearing transaction accounts	516,483	373,850
Money market and savings deposits	3,918,481	2,099,996
Certificates of deposits	338,793	331,456
Federal Home Loan Bank advances and other borrowings	14,520	329,292
Total interest expense	4,788,277	3,134,594
Net interest income	78,294,319	67,030,862
Provision for loan losses	3,279,000	3,811,000
Net interest income after provision for loan losses	75,015,319	63,219,862
Noninterest income		
Deposit fees	2,160,076	1,899,129
International fees	1,159,421	931,520
Gains (losses) on sale of investment securities, net	(267,405)	(627,074)
Gains on sale of SBA loans, net	391,373	885,671
Bank/corporate owned life insurance income	1,120,016	379,549
Other non-interest income	1,156,102	453,262
Total noninterest income	5,719,583	3,922,057
Noninterest expense		
Salaries and employee benefits	35,466,480	31,673,524
Occupancy and equipment	3,937,859	3,252,983
Professional services	5,766,208	4,657,950
Promotion expenses	1,371,357	1,335,522
Other expenses	4,268,559	4,582,809
Total noninterest expense	50,810,463	45,502,788
Income before income taxes	29,924,439	21,639,131
Income tax expense	7,847,120	5,245,689
NET INCOME	$ 22,077,319	$ 16,393,442
Earnings per share - basic	$ 2.77	$ 2.15
Earnings per share - diluted	$ 2.73	$ 2.09
Weighted average shares - basic	7,966,417	7,642,390
Weighted average shares - diluted	8,088,164	7,860,712

The accompanying notes are an integral part of these statements.

American Business Bank

STATEMENTS OF COMPREHENSIVE INCOME

For the years ended December 31,

	2019	2018
Net Income	$ 22,077,319	$ 16,393,442
Other Comprehensive Income:		
Unrealized gains (losses) on securities:		
Available-for-sale:		
Net change in unrealized gains (losses)	15,927,362	(5,601,846)
Reclassification of gains (losses) to net income	(267,405)	(627,074)
Net unrealized gains (losses) on securities	15,659,957	(6,228,920)
Tax effect	(4,629,647)	1,841,998
Net unrealized gains (losses) on securities, net of tax	11,030,310	(4,386,922)
Held-to-maturity:		
Net change in unamortized unrealized loss on securities available-for-sale that were transferred to held-to-maturity	2,946,202	(6,577,105)
Tax effect	(871,004)	1,944,429
Net unrealized gains (losses) on securities, net of tax	2,075,198	(4,632,676)
Total other comprehensive income (loss)	13,105,508	(9,019,598)
Comprehensive income	$ 35,182,827	$ 7,373,844

The accompanying notes are an integral part of these statements.

American Business Bank

STATEMENTS OF SHAREHOLDERS' EQUITY

For the years ended December 31, 2019 and 2018

	Shares outstanding	Common stock	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance at December 31, 2017	7,539,922	$ 149,819,034	$ 11,061,014	$ (8,077,265)	$ 152,802,783
Exercise of stock options	134,406	1,537,100	-	-	1,537,100
Restricted stock vested	32,909	-	-	-	-
Repurchase of restricted stock at vesting	(1,647)	(63,327)			(63,327)
Stock-based compensation	-	1,820,049	-	-	1,820,049
Sold stock held in trust	-	1,596,949	-	-	1,596,949
Net income for the year	-	-	16,393,442	-	16,393,442
Other comprehensive income					
Net change in unrealized losses on investment securities, net of tax	-	-	-	(9,019,598)	(9,019,598)
Comprehensive income	-	-	-	-	7,373,844
Balance at December 31, 2018	7,705,590	$ 154,709,805	$ 27,454,456	$ (17,096,863)	$ 165,067,398
Cumulative effect of adoption of ASU 2017-08	-	-	(2,747,319)	-	(2,747,319)
Reclassification of DCP liability to equity (1)	-	6,276,619	-	-	6,276,619
Exercise of stock options	101,488	1,082,102	-	-	1,082,102
Restricted stock vested	46,826	-	-	-	-
Repurchase of restricted stock at vesting	(3,733)	(128,296)	-	-	(128,296)
Stock-based compensation	-	1,932,091	-	-	1,932,091
Net income for the year	-	-	22,077,319	-	22,077,319
Other comprehensive income					
Net change in unrealized gains on investment securities, net of tax	-	-	-	13,105,508	13,105,508
Comprehensive income	-	-	-	-	35,182,827
Balance at December 31, 2019	7,850,171	$ 163,872,321	$ 46,784,456	$ (3,991,355)	$ 206,665,422

(1) DCP: Deferred Compensation Plan - see Note L

The accompanying notes are an integral part of these statements.

American Business Bank

STATEMENTS OF CASH FLOWS

For the years ended December 31,

	2019	2018
Cash flows from operating activities:		
Net income	$ 22,077,319	$ 16,393,442
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for loan losses	3,279,000	3,811,000
Provision for unfunded commitments	320,000	60,000
Depreciation and amortization of furniture, equipment and leasehold improvements	1,433,619	937,240
Net amortization of premium (discount) on securities	16,828,279	16,819,112
Amortization of operating lease right-of-use assets	2,085,870	-
Stock-based compensation expense	1,932,091	1,820,049
Increase in bank/corporate owned life insurance	(1,120,016)	(236,222)
Losses on sales of securities, net	267,405	627,074
Deferred income tax expense (benefit)	(1,899,560)	(1,179,112)
Deferred compensation expense	(190,994)	(226,569)
Post-retirement health benefits expense	(103,205)	(444,890)
Changes in assets and liabilities:		
Accrued interest receivable and other assets	6,638,217	549,969
Accrued interest payable and other liabilities	2,512,620	279,074
Net cash provided by operating activities	54,060,645	39,210,167
Cash flows from investing activities:		
Purchases of Federal Home Loan Bank stock	-	(418,600)
Purchases of securities available-for-sale	(234,206,464)	(86,492,921)
Proceeds from sales of available-for-sale securities	90,428,734	62,806,154
Proceeds from maturities and paydowns of available-for-sale securities	116,963,897	102,541,083
Net increase in certificates of deposits in other financial institutions	(250,000)	-
Net increase in loans receivable	(237,076,104)	(329,874,767)
Purchases of furniture, equipment and leasehold improvements	(8,623,040)	(1,497,950)
Net cash used in investing activities	(272,762,977)	(252,937,001)

The accompanying notes are an integral part of these statements.

American Business Bank

STATEMENTS OF CASH FLOWS - CONTINUED

For the years ended December 31,

	2019	2018
Cash flows from financing activities:		
Net increase in deposits	$ 191,101,238	$ 334,021,566
Repayment of Federal Home Loan Bank advances	-	(42,000,000)
Proceeds from (repayment of) other borrowings	-	(20,000,000)
Sale of stocks held in trust	-	1,596,949
Repurchase of restricted stock at vesting	(128,296)	(63,327)
Proceeds from exercise of stock options	1,082,102	1,537,100
Net cash provided by financing activities	192,055,044	275,092,288
Net increase (decrease) in cash and cash equivalents	(26,647,288)	61,365,454
Cash and cash equivalents at beginning of year	103,022,093	41,656,639
Cash and cash equivalents at end of year	$ 76,374,805	$ 103,022,093
Supplemental cash flow information:		
Cash paid during the year for:		
Interest	$ 4,798,132	$ 3,104,239
Income taxes	9,502,261	5,525,000
Supplemental noncash disclosures:		
Unrealized gains (losses) on investment securities, net of tax	13,105,508	(9,019,598)
Transfer of securities from available-for-sale to held-to-maturity	-	94,218,725
Lease liabilities arising from obtaining right-of-use assets	15,438,617	-
Reclassification of Deferred Compensation Plan liability to equity	6,276,619	-

The accompanying notes are an integral part of these statements.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

American Business Bank (the "Bank"), which commenced operations on October 1, 1998, is a California-chartered bank primarily engaged in the business of serving the banking needs of small and medium-sized firms, non-profits, along with the personal needs of business executives and professionals in Southern California. Since the Bank's emphasis is on business banking, it does not actively solicit consumer business from the general public. The Bank's revenues are derived principally from interest on loans and investments, and other fees. The operations and net interest income of the Bank are affected by general economic conditions and by the monetary and fiscal policies of the federal government. Lending activities are affected by the demand for business loans, commercial mortgage needs and other types of financing which is, in turn, affected primarily by interest rates and other general economic conditions. Deposit flows and cost of funds are influenced by interest rates on competing investments and by general market interest rates. The ability of the Bank's customers to honor their loan agreements is dependent, in part, upon the general economy of the Bank's market area and, to a lesser degree, upon the health of the local real estate market.

The accounting and reporting policies of the Bank are in accordance with accounting principles generally accepted in the United States of America ("US GAAP") and conform to general practices within the banking industry. A summary of the significant accounting policies consistently applied in preparation of the accompanying financial statements follows.

1. Use of Estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates.

Estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, the reserve for off-balance sheet credit commitments, valuation of stock options, investment securities impairment, the provision for income taxes and the valuation of financial assets and liabilities reported at fair value. The Bank has applied its critical accounting policies and estimation methods consistently in all periods presented in these financial statements.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

2. Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, federal funds sold, and interest earning deposits in other financial institutions, all of which mature within ninety days. Required reserves represent cash that is restricted to meet Federal Reserve Bank (Federal Reserve) requirements. Reserve balances of $1,493,000 and $382,000 were required by the Federal Reserve as of December 31, 2019 and 2018, respectively, and included in Cash and due from banks on the balance sheets.

3. Interest Earning Deposits in Other Financial Institutions

Interest earning deposits in other financial institutions represent short term interest earning deposits, which include money market deposit accounts with other financial institutions, and interest earning deposits with the Federal Reserve. These deposits can generally provide the Bank with immediate liquidity and generally can be liquidated the same day as is the case with the Federal Reserve and within seven days on money market deposit accounts with other financial institutions.

4. Investment Securities

Debt securities are classified based on management's intention on the date of purchase. Debt securities that management has the positive intent and ability to hold to maturity are classified as held–to-maturity and recorded at amortized cost. Securities classified as trading are recorded at fair value with changes in fair value recorded in earnings. Securities not classified as held-to-maturity or trading, are classified as available-for-sale and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income, net of tax. Interest and dividends are included in interest income. Realized gains and losses on sales of securities are recorded using the specific identification method.

Periodically, management may reassess the appropriateness of the classification of the Bank's investments in debt securities. Transfers of securities between categories of investments are accounted for at fair value as of the transfer date, and the accounting treatment of the unrealized holding gains and losses and the related income tax effects are determined by the category into which the security is transferred. For transfers of securities from available-for-sale to held-to-maturity, the unrealized gain or loss becomes part of the amortized cost basis at the date of transfer and is subsequently amortized over the remaining life of the security as a yield adjustment. The unrealized gain or loss at the date of transfer remains in accumulated other comprehensive income, but is amortized over the remaining life of the security as a yield adjustment.

Premiums or discounts on securities are amortized or accreted into income using the interest method over the expected lives of the individual securities except municipal securities premiums which are amortized to maturity date for the period ended December 31, 2018. Effective January 1, 2019 the Bank adopted Accounting Standards Update (ASU) 2017-08, which amended the amortization period for certain callable debt securities held at a premium, shortening such period

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

to the earliest call date. This guidance does not require any accounting changes for debt securities held at a discount. The Bank regularly performs an assessment to determine whether a decline in fair value below amortized cost is other-than-temporary. Amortized cost includes adjustments made to the cost of the security for accretion, amortization, collection of cash and previous other-than-temporary impairment recognized in earnings.

Other-than-temporary impairment exists when it is probable that the Bank will be unable to recover the entire amortized cost basis of the security. The classification of other-than-temporary impairment depends on whether the Bank intends to sell the security or it is more likely than not that it will be required to sell the security before recovery of its cost basis, and on the nature of the impairment. If the Bank intends to sell a security or it is more likely than not it will be required to sell a security prior to recovery of its cost basis, the entire amount of impairment is recognized in earnings. If the Bank does not intend to sell the security or it is not more likely than not it will be required to sell the security prior to recovery of its cost basis, the credit loss component of impairment is recognized in earnings and impairment associated with non-credit factors, such as market liquidity, is recognized in other comprehensive income net of tax. A credit loss is the difference between the cost basis of the security and the present value of cash flows expected to be collected, discounted at the security's effective interest rate at the date of acquisition. The cost basis of an other-than-temporarily impaired security is written down by the amount of impairment recognized in earnings. The new cost basis is not adjusted for subsequent recoveries in fair value.

5. Federal Home Loan Bank Stock

The Bank’s investment in the Federal Home Loan Bank stock represents an equity interest in the Federal Home Loan Bank of San Francisco. The investment is recorded at cost and periodically evaluated for impairment based on ultimate recovery of par value.

6. Loans Receivable

Loans receivable are stated at unpaid principal balance adjusted for deferred fees and costs on originated loans and the allowance for loan losses.

Loans on which the accrual of interest has been discontinued are designated as non-accrual loans. The accrual of interest on loans is discontinued when principal or interest is past due 90 days or when, in the opinion of management, there is reasonable doubt as to collectability. When loans are placed on non-accrual status, all interest previously accrued but not collected is reversed against current period interest income. Income on non-accrual loans is subsequently recognized only to the extent that cash is received and the loan’s principal balance is deemed collectable. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time and the ultimate collectability of the total contractual principal and interest is no longer in doubt. The past due status of loans receivable is determined based on contractual due dates for loan payments.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. 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. Income from impaired loans is recognized on an accrual basis unless the loan is on nonaccrual status.

Impairment is measured on a loan by loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price, or the fair value of the collateral if the loan is collateral dependent.

The estimated fair values of the real estate collateral are determined primarily through third-party appraisals. When a real estate secured loan becomes impaired, a decision is made regarding whether an updated certified appraisal of the real estate is necessary. The decision is based on various considerations, including the age of the most recent appraisal, the loan-to-value ratio based on the original appraisal and the condition of the property. Appraised values are discounted to arrive at the estimated selling price of the collateral, which is considered to be the estimated fair value. The discounts also include estimated costs to sell the property.

The estimated fair values of the non-real estate collateral, such as accounts receivable, inventory and equipment, are determined based on the borrower's financial statements, inventory reports, accounts receivable aging or equipment appraisals or invoices. Indications of value from these sources are generally discounted based on the age of the financial information or the quality of the assets.

Loans whose terms are modified are classified as troubled debt restructurings if the Bank grants such borrowers concessions and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring generally involve a reduction in interest rate or extension of a loan's stated maturity date. Non-accrual troubled debt restructurings are restored to accrual status if principal and interest payments, under the modified terms, are current for six consecutive months after modification. Loans classified as troubled debt restructurings are initially designated as impaired.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Nonrefundable fees and direct costs associated with the origination of loans are deferred and netted against outstanding loan balances. The net deferred loan fees and costs are recognized in interest income as an adjustment to yield over the loan term using a method that approximates effective yield.

Concentration of Credit Risk: The Bank has a concentration in commercial real estate loans generally collateralized by first deeds of trust on specific commercial properties. Most of the Bank's business activity is with customers located within Southern California. Therefore, the Bank's exposure to credit risk is significantly affected by changes in the economy in the Southern California region.

7. Allowance for Loan Losses

The allowance for loan losses (allowance) is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the collectability of the loan balance becomes unlikely. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance calculation methodology includes segregation of the total loan portfolio into segments. The Bank's loan portfolio is comprised of the following segments: construction, commercial real estate, residential real estate, commercial, and other loans.

The allowance consists of a specific and general component. The specific component relates to loans that are classified as impaired. For loans classified as impaired, an allowance is established when the discounted cash flows (or observable market price or collateral value) of the impaired loan is lower than the carrying value of that loan. The general component covers loans by loan portfolio segments. These loan portfolio segments are evaluated for loss exposure based upon historical loss rates for each of these classes of loans, adjusted for qualitative factors. The Bank utilizes a third party vendor to calculate the quantitative portion of the general allowance based on a methodology that uses probability of default ("PD") and loss given default ("LGD") factors to arrive at a loss rate for each risk grade and for each loan portfolio segment. The PD and LGD factors are based on average industry experience from the most recent 20 quarters. Loss rates are then applied to outstanding loan balances to arrive at the quantitative portion of the allowance. The allowance is further adjusted for qualitative factors and they are:

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

1. Lending policies and procedures, including underwriting standards and collection, charge-off, and recovery practices.
2. National, regional, and local economic and business conditions as well as the condition of various market segments, including the value of underlying collateral for collateral dependent loans.
3. Nature and volume of the portfolio and terms of loans.
4. Experience, ability, and depth of lending management and staff.
5. Volume and severity of past due, classified and nonaccrual loans.
6. Quality of the Bank's loan review system, and the degree of oversight by the Bank's Board of Directors.
7. Existence and effect of any concentrations of credit and changes in the level of such concentrations.
8. Effect of external factors, such as competition and legal and regulatory requirements.

8. Off-Balance Sheet Credit Related Financial Instruments

In the ordinary course of business, the Bank has entered into commitments to extend credit, including commitments under commercial letters of credit and standby letters of credit. Such financial instruments are recorded when they are funded. A separate allowance in other liabilities has been established using an estimated utilization percentage and loss rate from the allowance for loan losses methodology that is applied to unfunded commitments.

9. Furniture, Equipment and Leasehold Improvements

Furniture, equipment and leasehold improvements are stated at cost, less accumulated depreciation and amortization. Depreciation on furniture and equipment is computed on a straight-line method over the estimated useful lives of the assets. Leasehold improvements are capitalized and amortized on the straight-line method over the estimated useful life of the improvement or the term of lease, whichever is shorter. Furniture, equipment and leasehold improvements have the following estimated useful lives:

Asset classification	**Useful Life**
Wall Art/Lithographs	60 months
Bank Equipment	36 months
Office Equipment	60 months
Furniture	60 months
Computer Equipment	36 months
Network Equipment	60 months
Leasehold Improvement	Shorter of remaining lease term or estimated useful life

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

10. Bank/Corporate Owned Life Insurance

The Bank invests in Bank-Owned Life Insurance ("BOLI") and Corporate-Owned Life Insurance ("COLI"). BOLI and COLI involve the purchasing of life insurance by the Bank on a group of senior officers of the Bank. The Bank is the owner and beneficiary of these policies. BOLI and COLI are recorded as an asset at cash surrender value. Increases and decreases in cash value of these policies and insurance proceeds received, net of administrative charges, are recorded in noninterest income and are not subject to income tax, as long as the policies are held for the lives of the participants.

11. Derivatives Not Designated as Hedging Instruments

The Bank is a party to interest rate derivatives that are not designated as hedging instruments. All derivative instruments are recognized on the balance sheet at their current fair value. These derivatives relate to interest rate swaps that the Bank enters into with customers to allow customers to convert variable rate loans to a fixed rate. The Bank pays interest to the customer at a floating rate on a notional amount and receives interest from the customer at a fixed rate for the same notional amount. At the same time the interest rate swap is entered into with the customer, an offsetting interest rate swap is entered into with another financial institution. The Bank pays the other financial institution interest at the same fixed rate on the same notional amount as the swap entered into with the customer, and receives interest from the financial institution for the same floating rate on the same notional amount. The changes in the fair value of the swaps primarily offset each other and therefore should not have a significant impact on the Bank's results of operations. The notional value at December 31, 2019 and 2018 was $1,026,855 and $1,056,361, respectively.

Under the interest rate swap contracts, the Bank may be required to pledge and maintain collateral for the credit support based on certain threshold. At December 31, 2019 and 2018, the Bank was required to pledge cash collateral of $100,350 and $36,540.

12. Income Taxes

The Bank accounts for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using currently enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

The Bank believes that it is more likely than not that the deferred income tax assets as of December 31, 2019 will be utilized. In arriving at this conclusion the Bank is relying on projection of future

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

pretax income. The Bank evaluates all positive and negative evidence when projecting future taxable income from operations and gives more weight to evidence that is objectively verifiable. Management believes that it is more likely than not that the Bank will exceed these requirements.

Due to the adoption of ASU 2016-09 in 2017, the Bank recorded the related excess tax benefits/(deficiency) of $(12,162) and $100,592 for the years ended December 31, 2019 and 2018, respectively, through the income statement as an income tax benefit/(expense).

The Bank recognizes and measures uncertain tax positions using a two-step approach. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is more likely than not, that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount, which is more than 50% likely of being realized upon ultimate settlement. The Bank considers many factors when evaluating and estimating tax positions and tax benefits, which may require periodic adjustments. As of December 31, 2019, the Bank has identified no material uncertain tax position for which it is reasonably possible that the total amount of unrecognized tax benefits will significantly increase or decrease within 12 months.

Further, the Bank's policy is to record interest and penalties from underpayment of taxes when it is reasonably probable that the amounts will be incurred. The Bank is subject to federal income tax examinations for years beginning in 2016 and thereafter and California income tax examinations for years beginning in 2015 and thereafter. As of December 31, 2019, the tax examination by the State of California for tax years ended December 31, 2010, 2011 and 2012 concluded. There was no material impact to the financial statements as a result of the examination.

13. Stock-Based Compensation

The Bank measures the cost of employee and director services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost is recognized over the period during which an employee is required to provide service in exchange for the award – the requisite service period, on a straight-line basis. The Bank determines the grant-date fair value of employee share options granted using the Black-Scholes option-pricing model adjusted for the unique characteristics of these options. The Bank recognizes forfeitures as they occur.

14. Earnings Per Share

Basic earnings per share ("EPS") represent the net income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted EPS reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential dilutive common shares that may be issued by the Bank relate to outstanding stock options and restricted stock, and are determined using the treasury stock method. At December 31, 2019 and 2018, options to purchase 3,643 and 3,634 shares of

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

common stock were outstanding, respectively, but were not included in the computation of diluted earnings per share because the options were anti-dilutive.

	2019			2018		
	Net Income	Shares	Per Share Amount	Net Income	Shares	Per Share Amount
Basic EPS						
Net income available to common shareholders	$ 22,077,319	7,966,417	$ 2.77	$ 16,393,442	7,642,390	$ 2.15
Effect of dilutive shares	-	121,747	(0.04)	-	218,322	(0.06)
Diluted EPS	$ 22,077,319	8,088,164	$ 2.73	$ 16,393,442	7,860,712	$ 2.09

15. Reclassification

Certain amounts in the prior year's financial statements and related disclosures were reclassified to conform to the current year presentation with no effect on previously reported net income or shareholders' equity.

16. Recent Accounting Pronouncements

New Accounting Pronouncements Adopted in 2019:

On January 1, 2019, the Bank adopted ASU No. 2016-02, Leases (Topic 842) and subsequent amendments thereto, which requires a lessee to recognize most leases on the balance sheet. The new standard established a right-of-use model ("ROU") that requires a lessee to recognize a ROU asset and lease liability on the balance sheet. The Bank adopted the standard under the modified retrospective approach as of the date of adoption and elected to apply several of the available practical expedients, including (1) carry over of historical lease determination and lease classification conclusions in which the Bank was also not required to reassess if any expired or existing contracts are or contain leases; (2) carry over of historical initial direct cost balances for existing leases; and (3) the option to the lessee for not applying initial recognition requirements of setting up a right-of-use asset and a lease liability for short term leases with an original term of 12 months or less.

Adoption of the leasing standard resulted in the recognition of right-of-use assets of $14,047,584, and operating lease liabilities of $14,382,726 as of January 1, 2019. These amounts were determined based on the present value of minimum lease payments, discounted using the Bank's incremental borrowing rate as of the date of adoption. There was no material impact to the timing of expense or income recognition in the Bank's Statements of Income. The Bank did not have any amounts recorded for the cumulative adjustment to the opening balance of retained earnings. Prior periods were not restated and continue to be presented under legacy GAAP. Disclosures about the Bank's leasing activities are presented in Note E.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

On January 1, 2019, the Bank adopted ASU 2017-08, Receivables — Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities, which amended the amortization period for certain purchased callable debt securities held at a premium, shortening such period from the maturity date to the earliest call date. The guidance did not require any accounting changes for debt securities held at a discount. The discount continues to be amortized as an adjustment of yield over the contractual life (to maturity) of the instrument. We adopted the standard under the modified retrospective transition method, with the cumulative-effect adjustment recognized to retained earnings as of the beginning of the period of adoption. The adoption of this guidance resulted in a reduction of retained earnings by $2,747,319 as a cumulative-effect adjustment, with a corresponding offset to accumulated other comprehensive income and deferred tax assets.

Accounting Standards Issued but not yet Adopted:

In June 2016, the FASB issued ASU 2016-13, Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The new current expected credit loss (“CECL”) impairment model applies to most financial assets measured at amortized cost and certain other instruments, including trade and other receivables, loan receivables, available-for-sale and held-to-maturity debt securities, net investments in leases and off-balance sheet credit exposures. In addition, the amendments in this update require credit losses be presented as an allowance rather than as a write-down on available-for-sale debt securities. In November 2019, the FASB issued ASU 2019-10, Financial Instruments — Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842): Effective Dates. ASU 2019-10 defers the effective date of the new credit losses standard for all entities except SEC filers that are not smaller reporting companies to fiscal years beginning after December 15, 2022, including interim periods in those fiscal years, with early adoption permitted on January 1, 2019. The Bank is a public business entity that does not meet the definition of an SEC filer, and ASU 2016-13 is effective for the Bank on January 1, 2023. The guidance should be applied using a modified retrospective approach through a cumulative-effect adjustment to retained earnings as of the beginning of the reporting period of adoption. The Bank’s implementation efforts will include, but are not limited to, identifying key interpretive issues, assessing its processes, identifying the system requirements against the new guidance to determine what modifications may be required, evaluating modeling methodologies for its portfolio segments and assessing potential macroeconomic factors that will be used to determine the reasonable and supportable forecast period. We expect to recognize a one-time cumulative effect adjustment to the allowance for loan losses as of the beginning of the first reporting period in which the new standard is effective. We expect the adoption may result in an increase to the allowance for loan losses balance. The Bank is currently evaluating the impact on its financial statements.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

In August 2018, the FASB issued ASU 2018-13, Fair Value Measurement (Topic 820): Disclosure Framework - Changes to Disclosure Requirements for Fair Value Measurements, which changes the fair value measurement disclosure requirements of ASC 820. ASU 2018-13 must be applied prospectively and is effective for the Bank on January 1, 2020. Early adoption is permitted. The Bank does not expect ASU 2018-13 to have a material impact on its financial statements.

In August 2018, the FASB issued ASU 2018-15, Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract (a consensus of the FASB Emerging Issues Task Force), which aligns the requirements for capitalizing implementation costs in a cloud computing arrangement service contract with the requirements for capitalizing implementation costs incurred for an internal-use software license. The new guidance also prescribes the balance sheet, income statement, and cash flow classification of the capitalized implementation costs and related amortization expense, and requires additional quantitative and qualitative disclosures. ASU 2018-15 is effective for the Bank on January 1, 2020 and the Bank has the option to adopt the new standard either prospectively to eligible costs incurred on or after the date this guidance is first applied or retrospectively. Early adoption is permitted. The Bank is currently evaluating the impact on its financial statements.

NOTE B - INVESTMENT SECURITIES

The amortized cost and fair value of the Bank's investment securities as of December 31 are as follows:

	2019			
	Amortized cost	Unrealized gains	Unrealized losses	Fair value
Securities available-for-sale				
U.S. Treasury securities	$ 10,027,613	$ -	$ (18,238)	$ 10,009,375
U.S. SBA loan pool securities	290,521,280	120,743	(6,609,808)	284,032,215
Residential mortgage-backed securities	209,144,771	1,287,049	(968,671)	209,463,149
Commercial mortgage-backed securities	80,943,333	1,866,630	(147,252)	82,662,711
Corporate securities	19,945,252	35,578	(175,419)	19,805,411
Municipal securities	75,946,173	2,703,277	(129,594)	78,519,856
Total securities available-for-sale	$686,528,422	$ 6,013,277	$ (8,048,982)	$ 684,492,717
	Amortized cost	Unrealized gains	Unrealized losses	Fair value
Securities held-to-maturity				
Municipal securities	86,707,383	4,621,700	-	91,329,083
Total securities held-to-maturity	$ 86,707,383	$ 4,621,700	$ -	$ 91,329,083

	2018			
	Amortized cost	Unrealized gains	Unrealized losses	Fair value
Securities available-for-sale				
U.S. Treasury securities	$ 10,054,901	$ -	$ (195,526)	$ 9,859,375
U.S. SBA loan pool securities	449,318,669	44,127	(11,136,003)	438,226,793
Residential mortgage-backed securities	84,899,786	166,506	(2,821,150)	82,245,142
Commercial mortgage-backed securities	49,654,148	49,441	(1,111,587)	48,592,002
Corporate securities	2,000,000	-	(29,010)	1,970,990
Municipal securities	80,122,491	222,464	(2,884,925)	77,460,030
Total securities available-for-sale	$676,049,995	$ 482,538	$ (18,178,201)	$ 658,354,332
	Amortized cost	Unrealized gains	Unrealized losses	Fair value
Securities held-to-maturity				
Municipal securities	87,526,084	-	(585,147)	86,940,937
Total securities held-to-maturity	$ 87,526,084	$ -	$ (585,147)	$ 86,940,937

NOTE B - INVESTMENT SECURITIES – Continued

On September 1, 2018 the Bank reassessed its classification of certain investments and transferred $87,553,125 of municipal securities, at fair value, from available-for-sale to held-to-maturity. The related unrealized loss of $6,665,600 at the date of transfer included in accumulated other comprehensive income (AOCI) remained in AOCI, to be amortized out of AOCI with an offsetting entry to interest income as a yield adjustment through earnings to the remaining term of the securities for the year ended December 31, 2018. With the adoption of ASU 2017-08 on January 1, 2019, the amortization period was amended for these municipal securities that were held at a premium to the earliest call date. No gain or loss was recorded at the time of transfer. The remaining unamortized unrealized loss was $3,630,903 and $6,577,105 at December 31, 2019 and 2018, respectively.

The total gains and losses from sales of securities for each of the years ended December 31 are shown below:

	2019	2018
Gains from sales of securities	$ 334,346	$ 503,528
Losses from sales of securities	(601,751)	(1,130,602)
Net losses on sales of securities	$ (267,405)	$ (627,074)

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

	Available-for-sale		Held-to-maturity	
	Amortized cost	Estimated fair value	Amortized cost	Estimated fair value
Due within one year	$131,748,438	$130,659,800	$ -	$ -
Due in one to five years	281,196,176	278,944,035	10,929,690	11,435,550
Due in five to ten years	207,195,562	208,319,472	75,777,693	79,893,533
Due after ten years	66,388,246	66,569,410	-	-
Total	$686,528,422	$684,492,717	$ 86,707,383	$ 91,329,083

NOTE B - INVESTMENT SECURITIES – Continued

The total carrying value of securities pledged to secure borrowings, advances and for other purposes as required or permitted by law amount to $157,755,435 and $141,525,007 at December 31, 2019 and 2018, respectively.

The line of credit for overnight borrowings with the Federal Reserve Bank is collateralized with securities in the amount of $42,894,966 and $25,747,358 at December 31, 2019 and 2018, respectively.

Pursuant to collateral agreements with the Federal Home Loan Bank ("FHLB"), advances are collateralized by certain investment securities. The carrying value of the investment securities pledged were $53,693,773 and $81,528,844 at December 31, 2019 and 2018, respectively.

The Bank regularly monitors investments for significant declines in fair value. The Bank has determined that the decline in fair value of these investments below their amortized costs, as set forth in the table below, are temporary based on the following: (i) those declines are primarily due to interest rate changes and not due to a deterioration in the creditworthiness of the issuers of those investments securities, (ii) the Bank does not have the intent to sell these investment securities, and (iii) it is more likely than not the Bank will not have to sell these investment securities before recovery of their cost basis. The Bank determines other-than-temporary impairment based on the information available at the time of the assessment, with particular focus on the severity and duration of specific security impairments, but new information or economic developments in the future could result in recognition of an other-than-temporary impairment loss. The Bank did not identify any securities that were deemed to be other-than-temporarily impaired as of December 31, 2019 and 2018.

NOTE B - INVESTMENT SECURITIES – Continued

The following securities have been in a continuous unrealized loss position for less than and greater than twelve months at December 31:

	2019					
	Less than twelve months			Greater than twelve months		
	Number of Securities	Fair value	Unrealized loss	Number of Securities	Fair value	Unrealized loss
Securities available-for-sale						
U.S. Treasury securities	-	$ -	$ -	1	$ 10,009,375	$ (18,238)
U.S. SBA loan pool securities	2	3,629,031	(13,803)	80	274,618,834	(6,596,005)
Residential mortgage-backed securities	17	77,635,200	(401,792)	20	31,327,729	(566,879)
Commercial mortgage-backed securities	4	14,272,320	(147,252)	-	-	-
Corporate securities	7	11,848,999	(151,001)	1	1,975,582	(24,418)
Municipal securities	8	9,653,771	(92,353)	1	1,620,077	(37,241)
Total securities available-for-sale	38	117,039,321	(806,201)	103	319,551,597	(7,242,781)
Securities held-to-maturity						
Municipal securities	-	-	-	-	-	-
Total securities held-to-maturity	-	-	-	-	-	-
Total temporary impaired securities	38	$ 117,039,321	$ (806,201)	103	$ 319,551,597	$ (7,242,781)

	2018					
	Less than twelve months			Greater than twelve months		
	Number of Securities	Fair value	Unrealized loss	Number of Securities	Fair value	Unrealized loss
Securities available-for-sale						
U.S. Treasury securities	-	$ -	$ -	1	$ 9,859,375	$ (195,526)
U.S. SBA loan pool securities	6	26,916,913	(384,339)	99	406,926,169	(10,751,664)
Residential mortgage-backed securities	2	9,619,123	(96,308)	24	54,555,567	(2,724,782)
Commercial mortgage-backed securities	4	12,262,162	(201,941)	7	21,494,477	(909,645)
Corporate securities	1	1,970,990	(29,010)	-	-	-
Municipal securities	18	27,170,786	(543,166)	31	43,263,870	(2,341,759)
Total securities available-for-sale	31	77,939,974	(1,254,764)	162	536,099,458	(16,923,376)
Securities held-to-maturity						
Municipal securities	1	1,312,059	(1,772)	24	86,214,025	(583,375)
Total securities held-to-maturity	1	1,312,059	(1,772)	24	86,214,025	(583,375)
Total temporary impaired securities	32	$ 79,252,033	$ (1,256,536)	186	$ 622,313,483	$ (17,506,751)

NOTE C - LOANS AND ALLOWANCE FOR LOAN LOSSES

The following is a summary of the major components of loans outstanding at December 31:

	2019	2018
Construction loans	$ 31,325,293	$ 15,914,161
Commercial real estate loans	980,254,866	833,108,263
Residential real estate loans	60,127,156	49,373,450
Commercial loans	397,884,111	340,094,012
Other	19,104,538	12,726,424
	1,488,695,964	1,251,216,310
Deferred loan fees, net	(1,317,146)	(955,012)
Allowance for loan losses	(20,823,570)	(17,503,154)
	$ 1,466,555,248	$ 1,232,758,144

The Bank makes loans to borrowers in a number of different industries. As a normal practice in extending credit for real estate purposes, the Bank accepts trust deeds on real property as collateral for these loans. At December 31, 2019 and 2018, most of the Bank's loans secured by real estate were collateralized by properties in Southern California.

The following table presents the activity in the allowance for loan losses by portfolio segment for each of the years ending December 31:

	2019				
	Balance, beginning of year	Charge-offs	Recoveries	Provision for loan losses	Balance, end of year
Construction	$ 552,395	$ -	$ -	$ 532,761	$ 1,085,156
Commercial real estate	11,383,966	-	-	1,922,382	13,306,348
Residential real estate	423,217	-	-	(473)	422,744
Commercial	4,878,956	-	41,416	749,288	5,669,660
Other	264,620	-	-	75,042	339,662
	$ 17,503,154	$ -	$ 41,416	$ 3,279,000	$ 20,823,570

NOTE C - LOANS AND ALLOWANCE FOR LOAN LOSSES - Continued

	2018				
	Balance, beginning of year	Charge-offs	Recoveries	Provision for loan losses	Balance, end of year
Construction	$ 688,654	$ -	$ -	$ (136,259)	$ 552,395
Commercial real estate	9,222,650	-	-	2,161,316	11,383,966
Residential real estate	429,449	-	-	(6,232)	423,217
Commercial	3,192,028	-	53,435	1,633,493	4,878,956
Other	105,938	-	-	158,682	264,620
	$ 13,638,719	$ -	$ 53,435	$ 3,811,000	$ 17,503,154

The following tables present both the allowance for loan loss and the associated loan balance classified by loan portfolio segment and by credit evaluation methodology at December 31:

	2019				
	Individually evaluated for impairment	Allowance: Individually evaluated for impairment	Collectively evaluated for impairment	Allowance: Collectively evaluated for impairment	Total loans
Construction	$ -	$ -	$ 31,325,293	$ 1,085,156	$ 31,325,293
Commercial real estate	1,480,825	-	978,774,041	13,306,348	980,254,866
Residential real estate	-	-	60,127,156	422,744	60,127,156
Commercial	601,126	160,745	397,282,985	5,508,915	397,884,111
Other	-	-	19,104,538	339,662	19,104,538
	$ 2,081,951	$ 160,745	$ 1,486,614,013	$ 20,662,825	$ 1,488,695,964

	2018				
	Individually evaluated for impairment	Allowance: Individually evaluated for impairment	Collectively evaluated for impairment	Allowance: Collectively evaluated for impairment	Total loans
Construction	$ -	$ -	$ 15,914,161	$ 552,395	$ 15,914,161
Commercial real estate	1,100,210	-	832,008,053	11,383,966	833,108,263
Residential real estate	-	-	49,373,450	423,217	49,373,450
Commercial	357,097	139,342	339,736,915	4,739,614	340,094,012
Other	-	-	12,726,424	264,620	12,726,424
	$ 1,457,307	$ 139,342	$ 1,249,759,003	$ 17,363,812	$ 1,251,216,310

The Bank uses a ten point internal risk rating system to monitor the credit quality of the loans in the Bank's segments. The borrower's overall financial condition, repayment sources, guarantors and value of collateral, if appropriate, are evaluated annually or when credit deficiencies, such as

NOTE C - LOANS AND ALLOWANCE FOR LOAN LOSSES - Continued

delinquent loan payments arise. The criticized rating categories utilized by management generally follow bank regulatory definitions. Loans in the Pass category are those which are protected by the current net worth and paying capacity of the obligor or by the value of the underlying collateral. There are several different levels of Pass rated credits, including Watch, which includes credits that require heightened monitoring due to an identified potential weakness but demonstrates the ability to meet obligations and does not yet meet the criteria for Special Mention. The Special Mention category includes assets that show potential weaknesses or risks that deserve management's special attention. If uncorrected, the weaknesses may result in deterioration of the prospect for repayment. Loans classified Substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt and have a distinct possibility that some loss will be sustained if the weaknesses are not corrected. They include loans that are inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified Doubtful have all the weaknesses inherent in loans classified Substandard with the added characteristic that collection or liquidation in full, on the basis of current conditions and facts, is highly improbable. Loans classified as a Loss are considered uncollectible, or of such value that continuance as an asset is not warranted.

The following table presents the classes of loans summarized by the aggregate Pass and the criticized categories of Special Mention, Substandard, Doubtful and Loss within the internal risk rating system as of December 31:

	2019					
	Pass	Special Mention	Substandard	Doubtful	Loss	Total
Construction	$ 31,325,293	$ -	$ -	$ -	$ -	$ 31,325,293
Commercial real estate	960,920,437	17,853,604	1,480,825	-	-	980,254,866
Residential real estate	57,358,249	2,768,907	-	-	-	60,127,156
Commercial	380,314,983	16,936,016	633,112	-	-	397,884,111
Other	19,104,538	-	-	-	-	19,104,538
	$ 1,449,023,500	$ 37,558,527	$ 2,113,937	$ -	$ -	$ 1,488,695,964

	2018					
	Pass	Special Mention	Substandard	Doubtful	Loss	Total
Construction	$ 15,914,161	$ -	$ -	$ -	$ -	$ 15,914,161
Commercial real estate	805,515,158	24,993,059	2,600,046	-	-	833,108,263
Residential real estate	46,063,271	3,310,179	-	-	-	49,373,450
Commercial	323,131,730	16,605,185	357,097	-	-	340,094,012
Other	12,726,424	-	-	-	-	12,726,424
	$ 1,203,350,744	$ 44,908,423	$ 2,957,143	$ -	$ -	$ 1,251,216,310

NOTE C - LOANS AND ALLOWANCE FOR LOAN LOSSES - Continued

Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by the length of time a recorded payment is past due. The following table represents the classes of the loans receivable portfolio summarized by aging categories of performing loans and non-accrual loans as of December 31:

2019	30-59 Days past due	60-89 Days past due	90 or more Days past due	Total past due	Current	Total loans	Non-accrual loans
Construction	$ -	$ -	$ -	$ -	$ 31,325,293	$ 31,325,293	$ -
Commercial real estate	-	-	-	-	978,774,041	980,254,866	1,480,825
Residential real estate	-	-	-	-	60,127,156	60,127,156	-
Commercial	31,987	-	-	31,987	397,478,124	397,884,111	374,000
Other	-	-	-	-	19,104,538	19,104,538	-
	$ 31,987	$ -	$ -	$ 31,987	$ 1,486,809,152	$ 1,488,695,964	$ 1,854,825

2018	30-59 Days past due	60-89 Days past due	90 or more Days past due	Total past due	Current	Total loans	Non-accrual loans
Construction	$ -	$ -	$ -	$ -	$ 15,914,161	$ 15,914,161	$ -
Commercial real estate	1,499,835	-	-	1,499,835	830,508,218	833,108,263	1,100,210
Residential real estate	-	-	-	-	49,373,450	49,373,450	-
Commercial	-	-	-	-	339,972,329	340,094,012	121,683
Other	113,778	-	-	113,778	12,612,646	12,726,424	-
	$ 1,613,613	$ -	$ -	$ 1,613,613	$ 1,248,380,804	$ 1,251,216,310	$ 1,221,893

There was one commercial loan in the amount of $227,126 modified in a troubled debt restructuring as of December 31, 2019. There was one commercial loan in the amount of $235,413 modified in a troubled debt restructuring as of December 31, 2018.

The average recorded investment in impaired loans during the years ended December 31, 2019 and 2018 was $2,135,207 and $1,553,968, respectively. Interest income of approximately $103,122 and $72,982 was recognized on impaired loans during the years ended December 31, 2019 and 2018, respectively.

NOTE D - FURNITURE, EQUIPMENT AND LEASEHOLD IMPROVEMENTS, NET

The composition of the Bank's furniture, equipment and leasehold improvements at December 31 is as follows:

	2019	2018
Furniture and equipment	$ 6,094,431	$ 5,975,611
Leasehold improvements	6,874,148	3,723,030
Total	12,968,579	9,698,641
Less: Accumulated depreciation and amortization	(3,945,471)	(7,864,954)
	$ 9,023,108	$ 1,833,687

Depreciation and amortization expense was $1,433,619 and $937,240 for the years ended December 31, 2019 and 2018, respectively.

NOTE E – LEASES

The Bank enters into leases in the normal course of business primarily for its headquarters, back-office operations and loan production offices. The Bank's leases have remaining terms ranging from 3.42 to 10.50 years. Certain lease arrangements contain extension options which are typically around 5 years, while certain leases include lessee termination options. As these extension options are not generally considered reasonably certain of exercise, they are not included in the lease term. The Bank's leases do not include residual value guarantees or covenants. The Bank has elected not to recognize leases with original terms of 12 months or less on the balance sheets.

Leases are classified as operating or finance leases at the lease commencement date. Right-of-use assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. Right-of-use assets and lease liabilities are recognized at the lease commencement date based on the estimated present value of lease payments over the lease term. Lease incentives that are paid or payable to the lessee are deducted from lease payments and reduce the initial measurement of a lessee's right-of-use asset. Furthermore, the lease incentive is recognized on a straight-line basis as an offset to lease expense over the term of the lease beginning at the commencement date. The Operating lease expense, which is comprised of amortization of the ROU asset and the implicit interest accreted on the operating lease liability, is recognized on a straight-line basis over the lease term and is recorded in Occupancy and equipment expense in the Statements of Income. The Bank's

NOTE E – LEASES - Continued

occupancy expense also includes variable lease costs which is comprised of the Bank's share of common area maintenance that is not included in lease liabilities and expensed as incurred.

The Bank uses its incremental borrowing rate at lease commencement or at the lease amendment/modification date to calculate the present value of lease payments when the implicit rate is not known. The Bank's incremental borrowing rate is based on the FHLB amortizing advance rate, adjusted for the lease term and other factors.

As of December 31, 2019, operating lease right-of-use ("ROU") assets and related liabilities were $9,046,075 and $14,240,786, respectively. The Bank did not have any finance leases as of December 31, 2019. During the year ended December 31, 2019, the Bank had one new lease in June 2019, when the Bank moved its headquarters to its new location (also in Los Angeles). During the year ended December 31, 2019, the Bank also extended three leases and amended one lease to move location within the same building and extended the term. The Bank reassessed the ROU asset and liability related to these amended leases. The total lease cost was $2,120,709 for the year ended December 31, 2019.

The table below summarizes the maturity of remaining lease liabilities:

2020	$ 1,524,863
2021	1,573,644
2022	2,202,001
2023	2,165,764
2024	1,666,040
Thereafter	7,934,248
Total undiscounted lease payments	17,066,560
Less: imputed interest	(2,825,774)
Net lease liabilities	$ 14,240,786

The table below summarizes other information related to the Bank's operating leases for the year ended December 31, 2019:

Cash paid for amounts included in the measurement of lease liabilities	
Operating cash outflows from operating leases	$ 1,562,634
Right-of-use assets obtained in exchange for new operating lease liabilities	$ 15,438,617

NOTE E – LEASES - Continued

The table below summarizes other information relates to the Bank's operating leases as of December 31, 2019:

Operating lease weighted average remaining lease term (years)	8.75
Operating lease weighted average discount rate	3.00%

As of December 31, 2019, the Bank did not have any additional operating lease commitments that have not yet commenced.

Prior to the adoption of ASC Topic 842, the Bank's operating leases were not recognized on the balance sheet. The following table presents the undiscounted future minimum lease payments under the Bank's operating leases as of December 31, 2018:

2019	$	1,554,620
2020		1,350,705
2021		1,382,830
2022		2,005,317
2023		1,907,394
Thereafter		8,966,426
	$	17,167,292

NOTE F - DEPOSITS

At December 31, 2019, $37,455,263 out of total certificates of deposits of $37,712,153 mature within one year.

At December 31, 2019 and 2018, the Bank had certificates of deposit with balances of $250,000 or more of $32,861,510 and $43,880,415, respectively.

At December 31, 2019, the scheduled maturities for certificates of deposits were as follows:

Scheduled maturies in:		
2020	$	37,455,263
2021		256,890
2022 and thereafter		-
Total	$	37,712,153

NOTE G - ADVANCES FROM THE FEDERAL HOME LOAN BANK AND OTHER BORROWINGS

Federal Home Loan Bank ("FHLB") advances at December 31, 2019 and 2018 totaled $0. Pursuant to agreements with the FHLB, these advances are collateralized by certain investment securities. The carrying value of the investment securities pledged were $53,693,773 and $81,528,844 at December 31, 2019 and 2018, respectively.

In addition, the Bank is required to purchase FHLB common stock to support its FHLB advances. FHLB stock is carried at cost as it does not have a readily determinable fair value. At December 31, 2019 and 2018, the Bank had $10,356,200 of FHLB common stock.

The Bank has established a Standard Credit program with the FHLB and has $788,452,322 of its Real Estate loan portfolio pledged as collateral. This program gives the Bank a borrowing capacity of $542,612,887 as of December 31, 2019. The Bank has $50,981,828 of borrowing capacity supported by investment securities pledged with the FHLB. To reach a total borrowing capacity of $593,594,715 collateralized by the current level of pledged loans and securities, the Bank would be required to purchase additional FHLB stock.

Other Borrowings represent Federal funds purchased on an overnight basis. The Bank has a line of credit commitment with four correspondent banks and the Federal Reserve Bank for overnight borrowings up to $90,368,959 and $67,345,036 of which $0 was outstanding at December 31, 2019 and 2018.

NOTE H - INCOME TAXES

Income tax expense for the years ended December 31, includes the following:

	2019	2018
Current:		
Federal	$ 5,600,018	$ 3,672,908
State	4,146,662	2,751,893
	9,746,680	6,424,801
Deferred:		
Federal	(919,624)	(748,338)
State	(979,936)	(430,774)
	(1,899,560)	(1,179,112)
Total income tax expense	$ 7,847,120	$ 5,245,689

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets at December 31 are presented below:

	2019	2018
Deferred tax assets:		
Allowance for loan losses	$ 6,156,197	$ 5,174,562
Deferred lease liability	4,210,089	99,080
Accrued deferred compensation	4,175,650	3,653,967
Unrealized net loss on investment securities	1,675,253	7,175,904
State taxes	810,431	586,061
Accrued post-retirement health benefits	657,744	627,233
Stock-based compensation costs	467,743	396,871
Allowance for unfunded commitments	287,358	192,755
Depreciation and amortization	-	17,381
Other	372,973	295,398
Total deferred tax assets	$ 18,813,438	$ 18,219,212
Deferred tax liabilities:		
Depreciation and amortization	$ (1,615,235)	$ -
Lease right-of-use assets	(2,580,082)	-
Prepaid expenses and deferred loan costs	(235,976)	(235,976)
	$ (4,431,293)	$ (235,976)
Net deferred tax assets	$ 14,382,145	$ 17,983,236

NOTE H - INCOME TAXES - Continued

The income tax provisions for 2019 and 2018 differ from the amounts computed by applying the Federal statutory rate of 21% for 2019 and 2018, as follows:

	2019	2018
Federal statutory income tax rate	$ 6,284,132	$ 4,544,218
State taxes, net of federal benefit	2,562,609	1,853,089
Tax exempt interest, net of interest disallowed	(885,482)	(1,264,325)
Other	(114,139)	112,707
Effective income tax expense	$ 7,847,120	$ 5,245,689

NOTE I - FAIR VALUE MEASUREMENTS AND FAIR VALUE OF FINANCIAL INSTRUMENTS

Accounting guidance establishes a fair value hierarchy that distinguishes between assumptions based on market data (observable inputs) and the Bank's assumptions (unobservable inputs). Determining where an asset or liability falls within that hierarchy depends on the lowest level input that is significant to the fair value measurement as a whole. An adjustment to the pricing method used within either Level 1 or Level 2 inputs could generate a fair value measurement that effectively falls in a lower level in the hierarchy. The hierarchy consists of three broad levels as follows:

Level 1 – Quoted market prices in active markets for identical assets or liabilities

Level 2 – Observable inputs other than Level 1, including quoted prices for similar assets or liabilities in active markets, quoted prices in less active markets, or other observable inputs that can be corroborated by observable market data

Level 3 – Unobservable inputs developed using the Bank's estimates and assumptions, which reflect those that market participants would use

The determination of where an asset or liability falls in the hierarchy requires significant judgment. The Bank evaluates its hierarchy disclosures each quarter and based on various factors, it is possible that an asset or liability may be classified differently from quarter to quarter. However, the Bank expects that changes in classifications between different levels will be rare.

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Fair value is best determined based upon quoted market prices. However, in certain instances, there are no quoted market prices for the Bank's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using discounted cash flow method or other valuation

NOTE I - FAIR VALUE MEASUREMENTS AND FAIR VALUE OF FINANCIAL INSTRUMENTS – Continued

techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. The fair value estimates may not be realized in an immediate settlement of the instrument. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Bank.

The following methods and assumptions were used by the Bank in estimating fair value:

Securities available-for-sale and held-to-maturity: Fair value for securities categorized as Level 1, is based on readily available quoted prices. In determining the fair value of the securities categorized as Level 2, we obtain a report from a nationally recognized broker-dealer detailing the fair value of each investment security we hold as of each reporting date. The broker-dealer uses observable market information to value our securities, with the primary source being a nationally recognized pricing service. The Bank's securities portfolio is classified within Level 2, except for the Treasury securities which are classified within Level 1.

Impaired loans: The Bank typically adjusts the carrying amount of impaired loans when there is evidence of probable loss and when the expected fair value of the loan is less than its carrying amount. Impaired loans with specific reserves are classified as Level 3 assets. The following methods are used to determine the fair value of impaired loans:

(1) Discounted cash flows valuation techniques generally consist of developing an expected stream of cash flows over the life of the loans and then valuing the loans at the present value by discounting the expected cash flows based on the original effective interest rate on the loan.

(2) A specific reserve is established for an impaired loan based on the fair value of the underlying collateral, which may take the form of real estate, inventory or equipment. The fair value of the underlying collateral is generally based on third-party appraisals, or an internal evaluation if a third-party appraisal is not required by regulations, which utilized one or more valuation techniques such as income, market, and/or cost approaches.

NOTE I - FAIR VALUE MEASUREMENTS AND FAIR VALUE OF FINANCIAL INSTRUMENTS – Continued

Assets measured at fair value on a recurring basis at December 31, are as follows:

	Fair Value Measurements on a Recurring Basis at December 31, 2019 Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Financial assets:				
Securities available-for-sale				
U.S. Treasury securities	$ 10,009,375	$ -	$ -	$ 10,009,375
U.S. SBA loan pool securities	-	284,032,215	-	284,032,215
Residential mortgage-backed securities	-	209,463,149	-	209,463,149
Commercial mortgage-backed securities	-	82,662,711	-	82,662,711
Corporate securities	-	19,805,411	-	19,805,411
Municipal securities	-	78,519,856	-	78,519,856
Total recurring	$ 10,009,375	$ 674,483,342	$ -	$ 684,492,717

	Fair Value Measurements on a Recurring Basis at December 31, 2018 Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Financial assets:				
Securities available-for-sale				
U.S. Treasury securities	$ 9,859,375	$ -	$ -	$ 9,859,375
U.S. SBA loan pool securities	-	438,226,793	-	438,226,793
Residential mortgage-backed securities	-	82,245,142	-	82,245,142
Commercial mortgage-backed securities	-	48,592,002	-	48,592,002
Corporate securities	-	1,970,990	-	1,970,990
Municipal securities	-	77,460,030	-	77,460,030
Total recurring	$ 9,859,375	$ 648,494,957	$ -	$ 658,354,332

There were no transfers between Level 1 and Level 2 during 2019 or 2018.

NOTE I - FAIR VALUE MEASUREMENTS AND FAIR VALUE OF FINANCIAL INSTRUMENTS - Continued

Assets measured at fair value on a non-recurring basis at December 31 are as follows:

	Fair Value Measurements on a Non-Recurring Basis at December 31, 2019			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Impaired loans:				
Commercial real estate	$ -	$ -	$ 1,480,825	$ 1,480,825
Commercial	-	-	440,381	440,381
Total non-recurring	$ -	$ -	$ 1,921,206	$ 1,921,206

	Fair Value Measurements on a Non-Recurring Basis at December 31, 2018			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Impaired loans:				
Commercial real estate	$ -	$ -	$ 1,100,210	$ 1,100,210
Commercial	-	-	217,755	217,755
Total non-recurring	$ -	$ -	$ 1,317,965	$ 1,317,965

NOTE I - FAIR VALUE MEASUREMENTS AND FAIR VALUE OF FINANCIAL INSTRUMENTS – Continued

The following table presents the valuation methodology and unobservable inputs for Level 3 assets measured at fair value on a non-recurring basis at December 31:

		2019			
	Fair Value	Valuation Technique(s)	Unobservable input(s)	Range of input(s)	Weighted Average
Assets:					
Impaired loans	$ 164,936	Discounted cash flows	Discount rate	3.25%	3.25%
Impaired loans	1,756,270	Third party appraisals	Selling costs	10%	10%
Total impaired loans:	$1,921,206				

		2018			
	Fair Value	Valuation Technique(s)	Unobservable input(s)	Range of input(s)	Weighted Average
Assets:					
Impaired loans	$ 173,223	Discounted cash flows	Discount rate	3.25%	3.25%
Impaired loans	1,144,742	Third party appraisals	Selling costs	12% - 40%	13.09%
Total impaired loans:	$1,317,965				

NOTE I - FAIR VALUE MEASUREMENTS AND FAIR VALUE OF FINANCIAL INSTRUMENTS – Continued

On January 1, 2018, the Bank adopted ASU 2016-01 and has updated its valuation methods as necessary to conform to an "exit price" concept as required by ASU 2016-01. The carrying amounts of and estimated fair value of financial instruments not carried at fair value, at December 31 are as follows:

		Fair Value Measurements at December 31, 2019 Using			
	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Financial Assets:					
Cash and cash equivalents	$ 76,374,805	$ 76,374,805	$ -	$ -	$ 76,374,805
Securities held-to-maturity	86,707,383	-	91,329,083	-	91,329,083
Loans, net	1,466,555,248	-	-	1,461,582,986	1,461,582,986
Accrued interest receivable	9,953,397	-	9,953,397	-	9,953,397
Financial Liabilities:					
Non-interest bearing demand deposits	$ 1,083,704,912	$ -	$ 1,083,704,912	$ -	$ 1,083,704,912
Interest bearing transaction accounts	215,729,548	-	215,729,548	-	215,729,548
Money market and savings deposits	827,712,736	-	827,712,736	-	827,712,736
Certificates of deposit	37,712,153	-	37,766,599	-	37,766,599
Accrued interest payable	77,434	-	77,434	-	77,434

		Fair Value Measurements at December 31, 2018 Using			
	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Financial Assets:					
Cash and cash equivalents	$ 103,022,093	$ 103,022,093	$ -	$ -	$ 103,022,093
Securities held-to-maturity	87,526,084	-	86,940,937	-	86,940,937
Loans, net	1,232,758,144	-	-	1,219,490,392	1,219,490,392
Accrued interest receivable	10,560,308	-	10,560,308	-	10,560,308
Financial Liabilities:					
Non-interest bearing demand deposits	$ 983,283,654	$ -	$ 983,283,654	$ -	$ 983,283,654
Interest bearing transaction accounts	211,794,286	-	211,794,286	-	211,794,286
Money market and savings deposits	728,236,757	-	728,236,757	-	728,236,757
Certificates of deposit	50,443,414	-	50,526,247	-	50,526,247
Accrued interest payable	87,289	-	87,289	-	87,289

NOTE J - REGULATORY MATTERS

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 principles and practices. The Bank's capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. The Bank has elected to exclude accumulated other comprehensive income from regulatory capital.

Failure to meet minimal 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.

The Bank is subject to regulatory risk-based capital rules adopted by the federal banking agencies under Basel III. Beginning January 1, 2016, Basel III required all banking organizations to maintain a capital conservation buffer above the minimum risk-based capital requirements to avoid certain limitations on capital distributions, stock repurchases and discretionary bonus payments to executive officers. The capital conservation buffer is exclusively comprised of common equity tier 1 capital, and it applies to each of the three risk-based capital ratios but not to the leverage ratio. At December 31, 2019, the Bank was in compliance with the capital conservation buffer requirement for the common equity Tier 1, Tier 1 and total capital ratio minimums inclusive of the capital conservation buffer of 7.0%, 8.5% and 10.5%, respectively.

The quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total, Tier 1 and common equity Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined).

As of December 31, 2019, the most recent regulatory notifications categorized the Bank as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized" the Bank must maintain minimum total risk-based, Tier I risk-based, Tier I leverage ratios and Common Equity Tier I as set forth in the table. There are no conditions or events since that notification that management believe have changed the Bank's category. The following tables represent the amounts of regulatory capital and the capital ratios for the Bank, compared to its minimum regulatory capital requirements as of December 31, 2019 and 2018 ($ in thousands).

NOTE J - REGULATORY MATTERS - Continued

	Actual		For capital adequacy purposes		To be "well capitalized" under prompt corrective action provision	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2019:						
Total capital (to risk weighted assets)	$231,621	13.82%	$134,107	8.00%	$167,634	10.00%
Tier I capital (to risk weighted assets)	210,657	12.57%	100,581	6.00%	134,107	8.00%
Tier I leverage (to average assets)	210,657	8.66%	97,280	4.00%	121,599	5.00%
Common Equity Tier I (to risk weighted assets)	210,657	12.57%	75,435	4.50%	108,962	6.50%

	Actual		For capital adequacy purposes		To be "well capitalized" under prompt corrective action provision	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2018:						
Total capital (to risk weighted assets)	$199,905	14.09%	$113,506	8.00%	$141,883	10.00%
Tier I capital (to risk weighted assets)	182,164	12.84%	85,130	6.00%	113,506	8.00%
Tier I leverage (to average assets)	182,164	8.33%	87,426	4.00%	109,282	5.00%
Common Equity Tier I (to risk weighted assets)	182,164	12.84%	63,847	4.50%	92,224	6.50%

NOTE K - DEFINED CONTRIBUTION PLAN

On June 14, 1998, the Bank established a 401(k) plan. Under the 401(k) plan, eligible employees may contribute all or a portion of their compensation, up to the maximum dollar amount determined by the IRS each year. To be eligible to participate in the 401(k) plan, employees must have attained the age of 18. The Bank matches 50% of the first 8% of the participant's contribution. The Bank contributed $744,520 and $662,003 to the plan during the years ended December 31, 2019 and 2018, respectively.

NOTE L - DEFERRED COMPENSATION PLANS

Deferred Compensation Plan: The Bank has a deferred compensation plan (the "Plan") which covers the Bank's Directors and certain senior officers. Each covered employee may defer a portion of their base salary, as well as incentive/bonus payments for the Plan year. The directors may defer a portion or all of their director fee compensation. The amount of compensation deferred by each participant is determined in accordance with each participant's deferral election and the provisions of the Plan. The Plan provides for each participant to have their own deferral account and select measurement investment funds available under the terms of the Plan. The Plan also allows for the Bank, in its sole discretion or in accordance with employment or other agreements, to contribute amounts annually to each participants' account.

The Bank has established a rabbi trust to hold assets contributed under the Plan. These assets remain general assets of the Bank. Participants have the same rights with other unsecured and unsubordinated indebtedness of the Bank for any deficiency in the value of the assets.

The Bank has purchased life insurance policies on a selected group of current and former senior officers where the Bank is the owner and beneficiary of the policies. The BOLI and COLI are recorded as an asset at their cash surrender value. Changes in the cash surrender value of these policies, as well as a portion of the insurance proceeds received, are recorded in noninterest income and are not subject to income tax, as long as they are held for the life of the covered parties. At December 31, 2019 and 2018, the cash surrender value of the BOLI and COLI policies was $26,448,129 and $25,328,113, respectively, and is recorded as Bank/corporate owned life insurance on the balance sheets. At December 31, 2019, the insurance was allocated among four individual insurance companies, with balances ranging from approximately 7% to 41% of the Bank's outstanding BOLI balance.

Benefits in the Plan are payable starting at the scheduled distribution date, which is determined by the participant and must be no sooner than four years after the date of deferral, or upon the retirement or death of the participant. The benefits are payable in a lump sum or via installments over time. The amount of a participant's benefits is based on that individual's choice of measurement investment funds and how the funds performed. At December 31, 2019, there are sixteen measurement investment funds under the Plan.

NOTE L - DEFERRED COMPENSATION PLANS - Continued

For directors and the five founders of the Bank, deferrals may mirror investment in Bank shares (the ABB Stock Unit Measurement Fund) and the number of shares is determined based on which could be purchased based upon fair value of the shares on the date of deferral. The number of shares is adjusted for cash dividends, stock dividends, stock splits and other similar events. Prior to May 31, 2019, at the time of distribution, the participant may receive cash equal to the then current fair market value of the phantom deferred shares or Bank shares, as determined by the Plan Committee. Increases (decreases) in the fair value of the Bank's stock are included as a part of accrued interest and other liabilities with a corresponding charge (or credit) to salaries and employee benefits expense.

On May 31, 2019, the Bank made amendments to the Plan such that distributions from the ABB Stock Unit Measurement Fund can only be made in the form of Bank stock. As a result of this amendment, the Bank reclassified $6,276,619 or 176,557 unissued shares from deferred compensation liability to equity. Any subsequent increases or decreases in the fair value of the Bank's stock are no longer measured or recognized in the statement of income. Further, deferrals made into the ABB Stock Unit Measurement Fund after May 31, 2019 are only limited to stock-based compensation granted to the directors. For the five months ended May 31, 2019, the fair value of the ABB Stock Unit Measurement Fund increased by $607,135, with a corresponding charge to salaries and employee benefit expense. For the year ended December 31, 2018, the fair value of the ABB Stock Unit Measurement Fund (decreased) by $1,174,574, with a corresponding (credit) to salaries and employee benefit expense.

The deferred compensation obligation related to the Plan was $7,902,537 and $12,240,395 at December 31, 2019 and 2018, respectively, and is included in accrued interest and other liabilities. Compensation deferral elections by the participant and contributions from the Bank increase the deferred compensation obligation and are recorded as a charge to salaries and employee benefits expense. Contributions made by the Bank and participants were $846,990 and $808,924 for the years ended December 31, 2019 and 2018, respectively. The fair value of the participants' measurement investment funds, excluding the ABB Stock Unit Measurement Fund, increased by $901,801 and $114,452 for the years ended December 31, 2019 and 2018, respectively. Such change increased the deferred compensation obligation with a corresponding charge to salaries and employee benefits expense.

NOTE M - STOCK-BASED COMPENSATION PLANS

Stock Options

The Bank has established the 2014 Omnibus Plan (the Plan) which provides for the issuance of incentive stock options subject to the terms and conditions of the Plan. The incentive stock options issued under the plan allow employees the opportunity to purchase stock at not less than 100% of its fair value as of the grant date. Shares authorized for stock option grants under the Plan were 234,096 shares. At December 31, 2019 and 2018, 206,242 shares were available for future grants under the Plan.

Options granted to employees have a ten-year life and typically vest over a three to five year period beginning on the second anniversary from the grant date. It is the Bank's policy that shares issued upon the exercise of stock options come from authorized, but previously un-issued shares.

The fair value of each option grant was estimated on the date of the grant using the Black-Scholes option valuation model. The expected life was estimated based on the expected exercise activity of the grantee population. The volatility factors were based on the historical volatilities of the Bank's stock, and these were used to estimate volatilities over the expected life of the options. The risk-free interest rate was the implied yield available on zero coupons (U.S. Treasury Rate) at the grant date with a remaining term equal to the expected life of the options. Estimates of fair value are not intended to predict actual future events or the value ultimately realized by employees who receive stock incentive awards, and subsequent events are not indicative of the reasonableness of the original estimates of fair value made by the Bank. No options were granted during 2019 and 2018.

The Bank's pre-tax compensation expense for incentive stock options was $25,618 and $112,982 for the years ended December 31, 2019 and 2018, respectively.

NOTE M - STOCK-BASED COMPENSATION PLANS – Continued

The following table summarizes the stock option activity for the years ended December:

	2019	
Stock Options:	Shares	Weighted average exercise price
Outstanding, beginning of period	252,114	$14.96
Granted	-	-
Exercised	(101,488)	10.66
Forfeited	(6,382)	26.72
Outstanding, end of period	144,244	$17.46
Options exercisable at year end	140,371	$17.17

	2018	
Stock Options:	Shares	Weighted average exercise price
Outstanding, beginning of period	387,735	$13.77
Granted	-	-
Exercised	(134,406)	11.44
Forfeited	(1,215)	24.73
Outstanding, end of period	252,114	$14.96
Options exercisable at year end	240,498	$14.41

Total intrinsic value of options exercised was $2,477,489 and $3,861,380 for the years ended December 31, 2019 and 2018, respectively.

NOTE M - STOCK-BASED COMPENSATION PLANS - Continued

The following information applies to options outstanding at December 31:

2019					
	Options outstanding			Options exercisable	
Range of exercise prices	Number outstanding	Weighted average remaining life (years)	Weighted average exercise price	Number exercisable	Weighted average exercise price
\$13.60 - \$20.94	129,911	2.42	\$16.34	129,911	\$16.34
\$23.14 - \$36.14	11,240	5.53	24.57	8,127	24.20
\$38.64 - \$39.85	3,093	7.64	38.83	2,333	38.84
	144,244	2.78	17.46	140,371	17.17
Aggregate intrinsic value	\$2,633,509			\$2,601,875	

2018					
	Options outstanding			Options exercisable	
Range of exercise prices	Number outstanding	Weighted average remaining life (years)	Weighted average exercise price	Number exercisable	Weighted average exercise price
\$5.50 - \$10.00	73,308	0.56	\$8.99	73,308	\$8.99
\$10.01 - \$20.00	128,272	2.91	15.08	128,272	15.08
\$20.01 - \$39.85	50,534	5.64	23.31	38,918	22.39
	252,114	2.78	14.96	240,498	14.41
Aggregate intrinsic value	\$4,207,768			\$4,137,913	

NOTE M - STOCK-BASED COMPENSATION PLANS - Continued

Aggregate intrinsic value represents the difference between the Bank's closing stock price on the last trading day of the period, which was $35.65 and $31.55 as of December 31, 2019 and 2018, respectively, and the exercise price multiplied by the number of options outstanding or exercisable.

For the years ended December 31, 2019 and 2018, the total grant date fair value of options vested was $40,862 and $136,364, respectively. As of December 31, 2019 and 2018, the Bank had approximately $21,153 and $92,163 of unrecognized compensation costs related to unvested options. The Bank expects to recognize these costs over a weighted average period of 1.64 years.

Restricted Stock Awards/Units

The 2014 Omnibus Plan also provides for the issuance of Restricted Stock Awards/Units subject to the terms and conditions of the Plan. Under the Plan, 346,704 shares of restricted stock were authorized, and 91,465 and 155,854 shares were available for future awards as of December 31, 2019 and 2018, respectively. As of December 31, 2019 and 2018, a total of 255,239 and 190,850 shares, respectively, have been issued since the inception of the Plan. The Bank granted 64,389 and 67,013 Restricted Stock Awards/Units to employees and directors in 2019 and 2018, respectively.

The 2014 Omnibus Plan was amended in April 2018, whereby at the option of the employee, shares can be repurchased by the Bank, pursuant to net settlement by employees, in amounts necessary to cover income tax withholding obligations incurred through the vesting of restricted stock. Further, the 2014 Omnibus Plan was amended in May 2019, whereby Restricted Stock Units were added to the Plan as another equity instrument that may be granted to directors and employees.

Non-Participating Restricted Stock Units and Awards were granted to directors in 2019 and 2018, respectively, and they vest on the earlier of one year or the next annual shareholders' meeting. Restricted Stock Awards are granted to employees and typically begin vesting in the second year from the grant date over a three to five year period.

The Bank recognizes compensation expense over the vesting period of three to five years. The Bank recognized pre-tax compensation expense of $1,906,473 and $1,707,067 on restricted stock awards/units during the year ended December 31, 2019 and 2018, respectively. As of December 31, 2019 and 2018, the Bank had $4,447,543 and $4,227,687, respectively, of remaining unrecognized compensation costs related to the unvested portion of restricted stock awards/units which will be recognized over a weighted average period of 3.3 years.

NOTE M - STOCK-BASED COMPENSATION PLANS - Continued

The following table summarizes the restricted stock activity for the years ended December 31:

	2019	
Restricted Stock:	Shares	Weighted average grant price
Unvested, beginning of period	142,791	$38.11
Granted	64,389	36.21
Vested	(46,826)	35.59
Cancelled and forfeited	(1,592)	27.39
Unvested, end of period	158,762	$38.19

	2018	
Restricted Stock:	Shares	Weighted average grant price
Unvested, beginning of period	109,697	$34.41
Granted	67,013	40.31
Vested	(32,909)	30.68
Cancelled and forfeited	(1,010)	24.52
Unvested, end of period	142,791	$38.11

NOTE N - FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK

The Bank is a party to credit related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit and commercial letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheets.

The Bank's exposure to credit loss is represented by the contractual amount of these commitments. The Bank follows the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but may include cash collateral, accounts receivable, inventory, equipment, and income-producing commercial properties.

Commitments to extend credit and commercial letters of credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract.

Commitments generally have fixed expiration dates or other termination clauses and often require payment of a fee. Since many of the commitments and letters of credit are expected to expire without being drawn, the total commitment amounts do not necessarily represent future cash requirements.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing and similar transactions.

As of December 31, 2019 and 2018, the Bank established a reserve for estimated losses on off balance sheet commitments of $972,000 and $652,000, respectively. These balances are included in accrued interest and other liabilities on the balance sheets.

At December 31, the following financial instruments, whose contract amounts represent credit risk, were outstanding:

	2019	2018
Commitments to extend credit	$ 703,379,578	$ 590,435,853
Commercial letters of credit	2,226,154	4,310,674
Standby letters of credit	39,512,737	36,410,560

NOTE O - RELATED PARTY TRANSACTIONS

During 2019 and 2018, there were no existing transactions that are out of the ordinary course of business between the Bank and its executive officers, directors, principal stakeholders (beneficial owners of 5% or more of our Common Stock), or the immediate family or associates of any of the foregoing persons, or trust for the benefit of employees such as a 401(k) trust.

Some of the Bank's directors and executive officers, as well as the companies with which such directors and executive officers are associated, are customers of, and have had transactions with the Bank in the ordinary course of business. All such transactions are on substantially the same terms, including interest and collateral as those prevailing for comparable transactions with others.

The outstanding balances of related party loans at December 31, 2019 and 2018 are $14,921,647 and $550,522, respectively. Deposits from related parties held by the Bank at December 31, 2019 and 2018 amounted to $5,004,859 and $5,688,202, respectively.

The Bank has a liability for postretirement health benefits of $2,224,843 and $2,121,638 at December 31, 2019 and 2018, respectively. This accrual covers two directors who were former employees and are utilizing the benefits, and three executive officers of which two are retired and utilizing the benefits.

NOTE P – REVENUE FROM CONTRACTS WITH CUSTOMERS

All of the Bank's revenue from contracts with customers in the scope of ASC Topic 606, Revenue from Contracts with Customers, is recognized within Non-Interest Income. The following table presents the Bank's sources of revenue from contracts with customers within the scope of ASC 606 for the twelve months ended December 31:

	2019	2018
Noninterest income		
Revenue from contracts with customers		
Customer analysis charges	$ 2,075,247	$ 1,860,135
Other deposit fees	84,829	38,994
Foreign currency exchange fees	557,148	430,354
Other international fees	602,273	501,166
Credit Card / Interchange fees	437,102	144,773
Other sources of non-interest income [(a)]	1,962,984	946,635
Total noninterest income	$ 5,719,583	$ 3,922,057

(a) Not within the scope of ASC 606

NOTE Q - SUBSEQUENT EVENTS

The Bank evaluated subsequent events through March 27, 2020, the date the financial statements were available to be issued.

In December 2019, a novel strain of coronavirus (COVID-19) was reported in Wuhan, China. The World Health Organization has declared the outbreak to constitute a “Public Health Emergency of International Concern.” The COVID-19 outbreak is disrupting supply chains and affecting production and sales across a range of industries. The extent of the impact of COVID-19 on our operational and financial performance will depend on certain developments, including the duration and spread of the outbreak, impact on our customers, employees and vendors all of which are uncertain and cannot be predicted. At this point, the extent to which COVID-19 may impact our financial condition or results of operations is uncertain and the Bank will continue to evaluate any potential impact.

HEADQUARTERS

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American Business Bank has seven offices in strategic locations including: Los Angeles, Anaheim, Irvine, Torrance, Woodland Hills, Corona and Ontario.

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