SANTA CRUZ COUNTY BANK

Santa Cruz County Bank 2015 Annual Report

ABOUT SANTA CRUZ COUNTY BANK

Founded by a group of local business people who share a common commitment to the Santa Cruz area, Santa Cruz County Bank first opened its doors on February 3, 2004. Santa Cruz County Bank is a locally owned and operated community bank, serving the needs of the residents and businesses of Santa Cruz County. We believe strongly in the importance of local decision making and responsive customer service. We offer a complete line of depository products and lending solutions for businesses and individuals, including business term loans and lines of credit, commercial real estate financing, agricultural loans, SBA and USDA government guaranteed loans, credit cards, merchant services, mobile banking, remote deposit capture, and online services, including bill payment and cash management. Santa Cruz County Bank operates five full service banking offices located in Aptos, Capitola, Santa Cruz, Scotts Valley, and Watsonville, and two free standing ATM and Night Depositories in Santa Cruz and Aptos.

SANTA CRUZ COUNTY BANK MISSION STATEMENT

We are committed to our community by building lasting relationships and being a trusted partner that together empowers growth and economic vitality.

SHAREHOLDER INFORMATION

Santa Cruz County Bank's common stock is listed on the OTCQX as SCZC. Shareholders with questions regarding their account, stock transfers and registration, lost certificates or change of address should contact their broker, or if held directly, contact the Bank's transfer agent listed below:

Computershare Investor Services P.O. Box 30170, College Station, TX 77842-3170

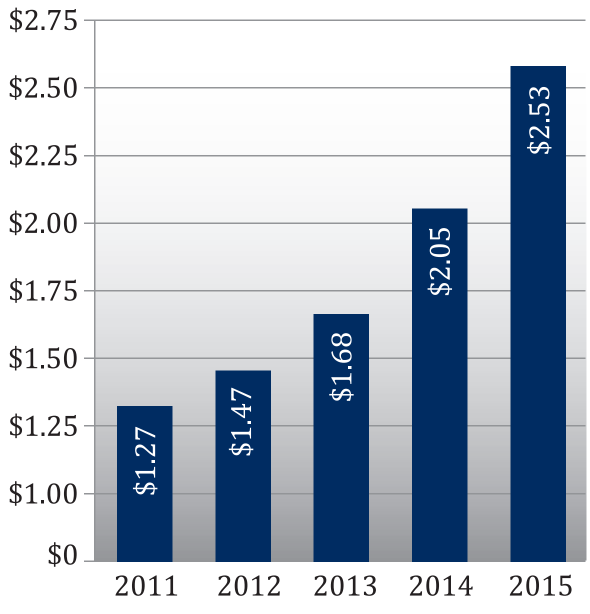
800.962.4284, www.computershare.com

BEST 50 OTCQX 2016

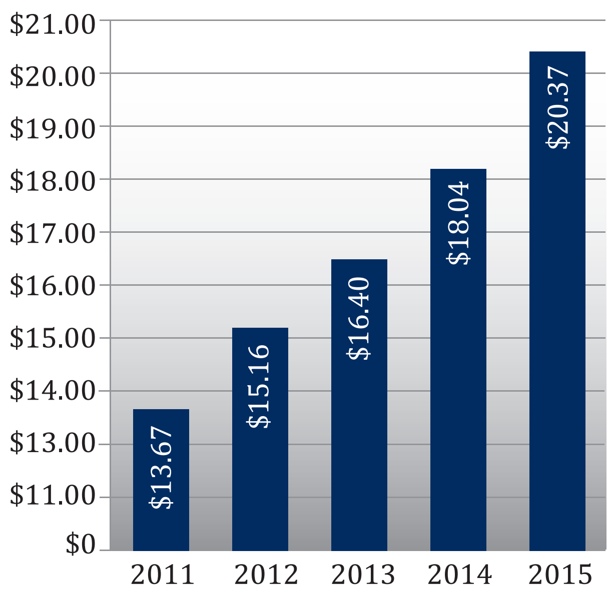
SCZC was named one of 50 best performing companies on OTCQX based on total return and growth in average daily dollar volume in 2015.

FIVE YEAR HISTORICAL PERFORMANCE

EARNINGS PER SHARE



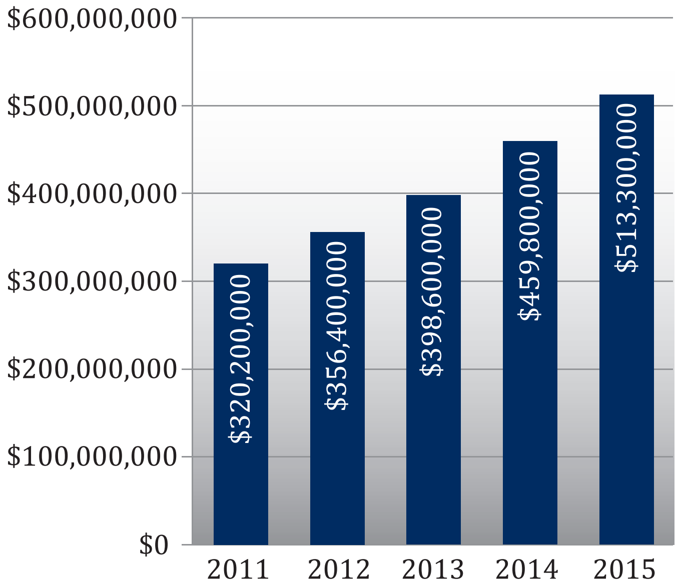
BOOK VALUE PER SHARE



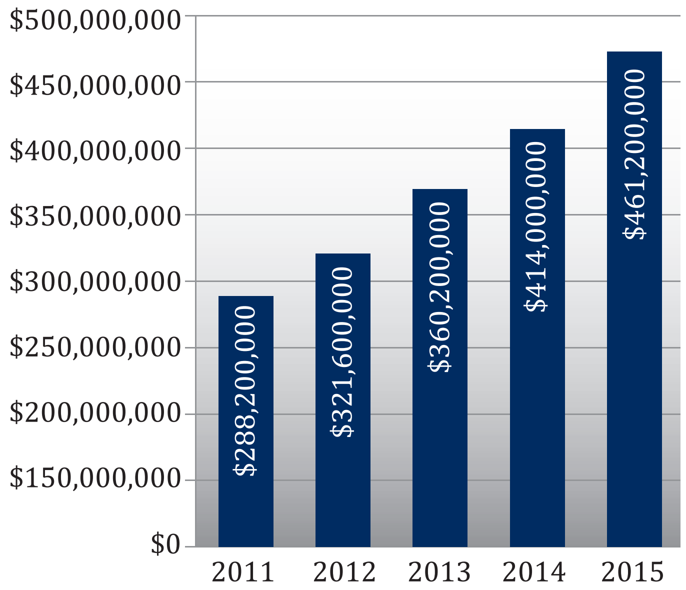
Santa Cruz County Bank ranked 75th in the Top 200 Performing Community Banks and Thrifts in the U.S. by American Banker based upon 3-year return on equity, its third consecutive year in the Top 200.

FIVE YEAR HISTORICAL PERFORMANCE

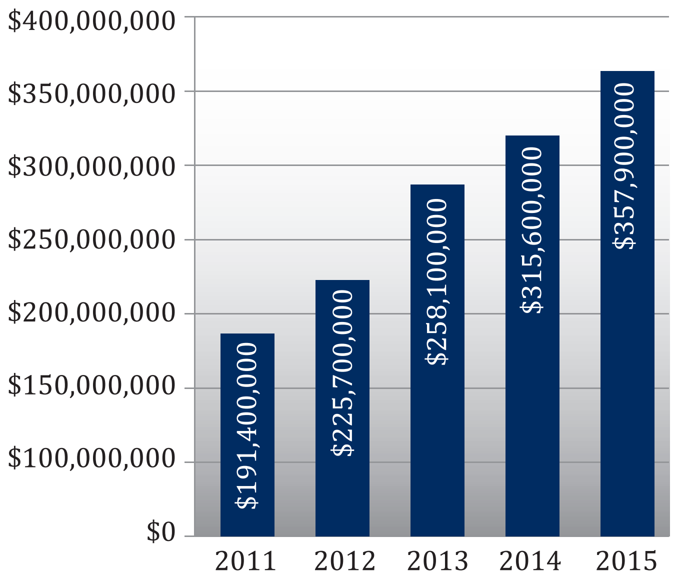
TOTAL ASSETS



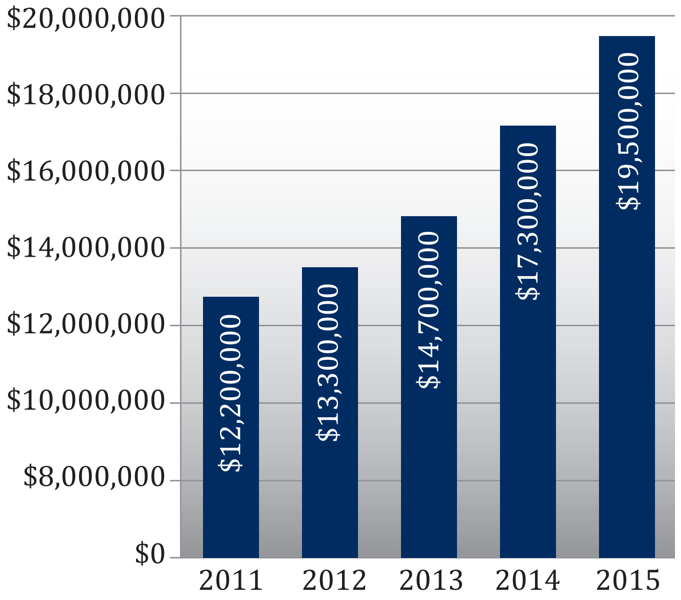
TOTAL DEPOSITS



GROSS LOANS



NET INTEREST INCOME



All numbers rounded to the nearest $100,000.

SANTA CRUZ COUNTY BANK
LETTER TO SHAREHOLDERS

To Our Shareholders,

On behalf of the Board of Directors and Bank Management team, we are pleased to present our Annual Report and 2015 financial highlights.

It was an exceptional year for your Bank. For a fourth consecutive year, we achieved double-digit percentage increases in assets, loans, deposits and net income year over year. For 2015, we posted a 24% increase in net income, which set a new record for earnings and has increased annually for seven consecutive years.

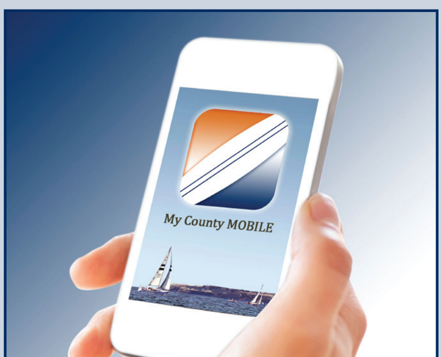
In 2015 we produced a net increase of $54 million in gross loans outstanding, a 13% increase to $358 million, while maintaining outstanding asset quality with zero non-performing or past due loans. Our overall number and volume of loan approvals through government guaranteed programs has consistently placed us in the top tier of local, regional and statewide lender rankings. For a ninth consecutive year, the Bank is the top SBA lender in Santa Cruz County. Moreover, the Bank ranked 6th in Silicon Valley and 46th in California for SBA loan production. Additionally, we rank as a top USDA lender in the state of California.

We are pleased that we can see the result of our continued commitment to building shareholder value. In January 2015, we qualified and commenced trading on the OTCQX marketplace, the top securities market for over the counter equities. Since joining the OTCQX marketplace, our stock was selected to the OTCQX Bank Index and was named to the 2016 OTCQX Best 50 Companies. The OTCQX Best 50 ranking of top performing U.S. and international companies traded on the OTCQX is based upon total return and growth in average daily dollar volume in 2015.

For a third year in a row, Santa Cruz County Bank was named in *American Banker's Top Performing 200 Community Banks and Thrifts* in the United States based upon 3-year average return on equity. The Bank placed 75th out of 750 institutions in the nation. In addition, Santa Cruz County Bank ranked 2nd in overall performance among 185 California banks in 2015 by Financial Management Consulting Group. The Bank ranked 1st (lowest) in non-performing assets and asset quality.

While the traditional model of brick and mortar banking has been around for hundreds of years and remains a relevant delivery channel, consumer demand for advanced technology remains at an all-time high. As a newly opened bank in 2004, we were fortunate to invest in systems and technology equal to or better than our competition. We are committed to keep pace with major bank products, services, and delivery. As we enter our thirteenth year of operations, we are pleased to offer more banking options for our customers than ever before.

NEW PRODUCTS, ADVANCED TECHNOLOGY



My County Mobile App

Mobile Deposit

Chip Card Security

We are pleased to offer more banking options than ever before.

To provide our customers secure *24/7* account access from wherever they may be - working, traveling or at home - with the best possible banking experience, we launched Mobile Banking, Text Alerts, Mobile person to person payments and Mobile Deposit in 2015. This year we commenced the rollout of chip enabled EMV or “Smart Card” technology to enhance the security of debit and credit card transactions for our customers. To further improve and streamline the customer experience outside our banking offices, we will embark on the installation of a replacement fleet of next generation or “Smart” ATMs at every branch location. This new technology will afford convenience and new features including the ability to deposit cash and checks through the ATM, without the need for deposit slips or envelopes.

Recent community awards publicly reconfirm our well recognized and highly respected Bank as a leader in community engagement and as the bank of choice for our community. In 2016, we received the United Way of Santa Cruz County’s Community Spirit Award for embodying workplace employee community engagement and the development of strategies that encourage our employees to give, advocate, and volunteer. For a fourth consecutive year, we were voted Best Bank in the Good Times readers’ poll and for a second year running, as Best Bank in the Santa Cruz Sentinel *Readers’ Choice* poll.

Please accept our sincere thanks for your investment in Santa Cruz County Bank and your referrals. We look forward to an even brighter future with many great returns.

George Gallucci
Chairman
of the Board

David Heald
President &
Chief Executive Officer

2015 HIGHLIGHTS

- Total assets surpassed $510 million.
- Total deposits surpassed $460 million.
- Pretax income exceeded $8.8 million.
- The Bank paid four quarterly $0.05 cash dividends to shareholders.
- Santa Cruz County Bank remained as the top SBA lender in Santa Cruz County, ranked 6th in Silicon Valley, and ranked 46th statewide among 248 lenders for the 2015 SBA fiscal year.
- As of June 30, 2015, the Bank ranked 5th largest in overall market share with 8.32% of deposits held by FDIC insured institutions in Santa Cruz County.
- The Bank received 4-Star “Excellent” ratings by Bauer Financial Inc. for its quarterly financial performance in 2015.
- Santa Cruz County Bank ranked 75th in the *Top 200 Performing Community Banks and Thrifts* in the U.S. by American Banker based upon 3-year return on equity, its third consecutive year in the *Top 200*.
- The Bank ranked 2nd in overall financial performance for 2015 among 185 California banks by Financial Management Consulting Group and 1st (lowest) in non-performing assets and asset quality.
- Independent Community Bankers of America ranked Santa Cruz County Bank in its *Top 25 Best Performing Community Banks* with the highest return on average assets and highest return on average equity ratios.

OUR CUSTOMERS SAY IT BEST

"Santa Cruz County Bank is a big part of what makes our multi-generational business viable. Being a seasonal business requires more than a bank, but a relationship. Santa Cruz County Bank understands our business, sees our vision and makes our success possible."

T. J. & Marcella Moran, Owners, Sun Shops & Millions of Memories

"Finding a small community bank with specialized lending programs and experienced lenders allowed me to finance my business through the USDA's Farm Service Agency loan program. The Bank listened to my needs and found the right solution to finance my farming operation when other banks could not. I'm grateful for their professionalism, lending expertise, and great service!"

Cynthia Sandberg, Owner, Love Apple Farms

"As a busy business owner, I need 21st century technology, backed by the human touch. With Santa Cruz County Bank, I have both, and my banking is easy as "pizza" pie."

Derek Rupp, Owner, Pleasure Pizza & East Side Eatery

INDEPENDENT AUDITOR'S REPORT

The Shareholders and Board of Directors
Santa Cruz County Bank
Santa Cruz, California

Report on the Financial Statements

We have audited the accompanying financial statements of Santa Cruz County Bank (the "Bank"), which comprise the balance sheets as of December 31, 2015 and 2014, and the related statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Santa Cruz County Bank as of December 31, 2015 and 2014, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Crowe Horwath LLP

Crowe Horwath LLP

San Francisco, California
March 15, 2016

SANTA CRUZ COUNTY BANK
BALANCE SHEETS
December 31, 2015 and 2014

	2015	2014
ASSETS		
Cash and due from financial institutions	$ 9,413,429	$ 9,504,355
Federal funds sold	865	615
Cash and cash equivalents	9,414,294	9,504,970
Interest-bearing deposits in other financial institutions	85,586,000	67,592,000
Securities available for sale	10,635,598	11,159,506
Securities held to maturity (fair value 2015-$40,422,906; 2014-$47,656,457)	39,216,658	46,380,219
Loans held for sale	42,091,432	32,937,632
Loans, net of allowance of $7,362,210 in 2015; $6,402,752 in 2014	310,286,559	277,571,975
Federal Home Loan Bank stock, at cost	1,708,000	1,420,900
Pacific Coast Bankers Bank stock, at cost	170,000	170,000
Loan servicing rights	728,482	720,690
Premises and equipment, net	534,722	767,009
Bank owned life insurance	5,736,771	5,557,518
Deferred income tax	4,072,370	3,469,226
Accrued interest receivable	1,612,484	1,410,876
Other assets	1,543,494	1,132,361
TOTAL ASSETS	$ 513,336,864	$ 459,794,882
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits		
Non-interest bearing	$ 208,935,959	$ 191,789,387
Interest bearing	253,299,071	222,196,946
Total deposits	462,235,030	413,986,333
Accrued interest payable	70,096	72,839
Other liabilities	6,936,715	7,106,310
Total liabilities	469,241,841	421,165,482
Commitments and contingent liabilities (Note 16)		
Shareholders' equity		
Preferred stock, no par value; 10,000,000 shares authorized; no shares issued or outstanding		
Common stock, no par value; 30,000,000 shares authorized; 2,164,651 shares issued at December 31, 2015 and 2,141,253 shares issued at December 31, 2014	23,529,241	23,346,191
Additional paid-in capital	1,494,878	1,281,755
Retained earnings	19,372,645	14,368,514
Accumulated other comprehensive loss	(301,741)	(367,060)
Total shareholders' equity	44,095,023	38,629,400
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 513,336,864	$ 459,794,882

See accompanying notes

SANTA CRUZ COUNTY BANK
STATEMENTS OF INCOME
Years ended December 31,

	2015	2014
Interest and dividend income		
Loans, including fees	$ 17,577,056	$ 15,589,081
Interest-bearing deposits in other financial institutions	827,455	685,778
Taxable securities	1,130,514	995,830
Tax-exempt securities	374,224	384,981
Federal funds sold	20,417	14,918
Total interest and dividend income	19,929,666	17,670,588
Interest expense		
Deposits	451,190	413,980
Federal Home Loan Bank advances and federal funds purchased	6,775	2,316
Total interest expense	457,965	416,296
Net interest income	19,471,701	17,254,292
Provision for loan losses	920,000	750,000
Net interest income after provision for loan losses	18,551,701	16,504,292
Noninterest income		
Service charges on deposits	561,120	623,203
Net gains on sales of loans	866,025	1,266,528
Loan servicing fees	565,882	507,478
Net gains on sales of securities (2015 includes $1,453 accumulated other comprehensive income reclassifications for unrealized net gains on available for sale securities)	1,453	-
Other	1,112,997	914,237
Total noninterest income	3,107,477	3,311,446
Noninterest expense		
Salaries and employee benefits	7,507,750	6,965,407
Occupancy	995,939	1,012,044
Furniture and equipment	468,827	410,333
Marketing and business development	331,425	333,054
Data and item processing	465,601	588,944
Professional services	378,973	848,474
Federal deposit insurance	309,581	277,051
Provision for off balance sheet commitments	7,593	-
Other	2,302,726	2,225,757
Total noninterest expense	12,768,415	12,661,064
Income before income taxes	8,890,763	7,154,674
Income tax expense	3,456,983	2,783,487
Net income	$ 5,433,780	$ 4,371,187
Earnings per share:		
Basic	$ 2.53	$ 2.05
Diluted	$ 2.49	$ 2.02

See accompanying notes

SANTA CRUZ COUNTY BANK
STATEMENTS OF COMPREHENSIVE INCOME
Years ended December 31,

	2015	2014
Net income	$ 5,433,780	$ 4,371,187
Other comprehensive income:		
Unrealized gains on securities:		
Unrealized holding gain arising during the period	27,065	(3,597)
Reclassification adjustment for gains included in net income	(1,453)	-
Tax effect	(10,540)	1,471
Net of tax	15,072	(2,126)
Defined benefit pension plans:		
Net gain arising during the period	76,907	238,188
Reclassification adjustment for amortization of prior service cost and net gain/loss included in net periodic pension cost	8,480	8,480
Tax effect	(35,141)	(101,516)
Net of tax	50,246	145,152
Total other comprehensive income	65,318	143,026
Comprehensive income	$ 5,499,098	$ 4,514,213

See accompanying notes

SANTA CRUZ COUNTY BANK
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Years ended December 31,

	Shares	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive (Loss)	Total
Balance at January 1, 2014	1,999,090	$ 21,904,069	$ 959,232	$ 10,423,089	$ (510,086)	$32,776,304
Net income				4,371,187		4,371,187
Other comprehensive loss					143,026	143,026
Exercise of stock options, including tax benefit	142,163	1,442,122	167,731			1,609,853
Restricted stock awards and related expense			27,859			27,859
Stock-based compensation			126,933			126,933
Cash dividends declared ($0.05 per share)				(425,762)		(425,762)
Balance at December 31, 2014	2,141,253	$ 23,346,191	$ 1,281,755	$ 14,368,514	$ (367,060)	$38,629,400
Net income				5,433,780		5,433,780
Other comprehensive Income					65,319	65,319
Exercise of stock options, including tax benefit	13,198	183,050	13,216			196,266
Restricted stock awards and						-
related expense	10,200		48,406			48,406
Stock-based compensation			151,501			151,501
Cash dividends declared ($0.05 per share)				(429,649)		(429,649)
Balance at December 31, 2015	2,164,651	$ 23,529,241	$ 1,494,878	$ 19,372,645	$ (301,741)	$44,095,023

See accompanying notes

SANTA CRUZ COUNTY BANK
STATEMENTS OF CASH FLOWS
Years ended December 31,

	2015	2014
Cash flows from operating activities		
Net income	$ 5,433,780	$ 4,371,187
Adjustments to reconcile net income to net cash from operating activities:		
Provision for loan losses	920,000	750,000
Depreciation and amortization of premises and equipment	268,737	339,510
Net amortization of securities	814,561	913,670
Net loan amortization and accretion	(391,615)	(374,536)
Deferred income tax benefit	(648,763)	(333,013)
Net realized gain on sales of securities	(1,453)	-
Net gain on sale of loans	(866,025)	(1,266,528)
Stock based compensation expense	199,907	154,792
Earnings on bank owned life insurance	(179,253)	(176,889)
Originations of loans held for sale	(21,654,675)	(27,630,208)
Proceeds from loans held for sale	12,652,354	17,898,211
Net loss on sale/disposal of assets	110	7,228
Provision for unfunded loan commitments	7,593	-
Gain on sale of OREO	-	(55,020)
Writedowns on OREO	-	200,000
Deferred benefit expense	203,586	290,215
Decrease in deferred loan fees, net of costs	(540,800)	(729,596)
Net change in accrued interest receivable	(201,608)	(98,104)
Decrease (Increase) in other assets	349,753	(477,413)
Net change in accrued interest payable and other liabilities	(2,743)	(16,210)
(Decrease) Increase in other liabilities	(818,973)	1,588,843
Net cash from operating activities	(4,455,527)	(4,643,861)
Cash flows from investing activities		
Redemption of certificates of deposit in other financial institutions	40,714,000	55,087,000
Purchase of certificates of deposit in other financial institutions	(58,708,000)	(55,963,000)
Available-for-sale securities:		
Maturities, prepayments and calls	75,000	-
Purchases	-	(11,374,202)
Principal repayments on securities available for sale	440,137	227,127
Held-to-maturity securities:		
Maturities, prepayments and calls	1,456,800	1,636,000
Purchases	-	(1,047,332)
Principal repayments on securities held to maturity	4,966,408	5,404,967
Loan originations and payments, net	(32,271,148)	(46,571,204)
Purchases of premises and equipment	(79,757)	(274,731)
Purchases of Federal Home Loan Bank stock	(287,100)	(236,600)
Net proceeds from sales of OREO	-	199,111
Proceeds from sale of assets	43,197	-
Net cash from investing activities	(43,650,463)	(52,912,864)
Cash flows from financing activities		
Net change in deposits	48,248,697	53,746,585
Cash dividends paid	(429,649)	(425,762)
Proceeds from exercise of stock options, including tax benefit	196,266	1,609,853
Net cash from financing activities	48,015,314	54,930,676
Net change in cash and cash equivalents	(90,676)	(2,626,049)
Beginning cash and cash equivalents	9,504,970	12,131,019
Ending cash and cash equivalents	$ 9,414,294	$ 9,504,970
Supplemental cash flow information		
Interest paid	$ 460,708	$ 432,506
Income taxes paid	4,435,000	3,120,000

See accompanying notes

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

NATURE OF OPERATIONS

Santa Cruz County Bank, referred to as “the Bank”, is a California state chartered bank which offers a full range of commercial and personal banking services to residents and businesses in Santa Cruz County, California, through its five full service offices located in Aptos, Capitola, Santa Cruz, Scotts Valley, and Watsonville. The Bank was incorporated on September 10, 2003 as Santa Cruz County Bank (In Organization) and commenced banking operations on February 3, 2004 (Inception), upon receipt of final regulatory approval. The Bank is subject to regulations and undergoes periodic examinations by the California Department of Business Oversight (“CDBO”) and the Federal Deposit Insurance Corporation (“FDIC”). The Bank’s deposits are insured by the FDIC up to applicable limits.

The majority of the Bank’s business is conducted with customers located in Santa Cruz County and adjacent counties. Its primary deposit products are checking, savings, and term certificate accounts, and its primary lending products are commercial, multi-family, agriculture, loans supported by single-family residential real estate, municipal loans, government guaranteed loans, and installment loans. Portions of said loans are secured by specific items of collateral including business assets, consumer assets, and commercial and residential real estate. Bank products are also supported by various government guarantee programs. Commercial loans are expected to be repaid from cash flow from operations of businesses. There are no significant concentrations of loans to any one industry or customer. However, the customers’ ability to repay their loans is dependent on the real estate and general economic conditions in the area.

SUBSEQUENT EVENTS: The Bank has reviewed all events occurring from December 31, 2015 through March 15, 2016, the date the financial statements were available to be issued and no subsequent events occurred requiring accrual or disclosure.

USE OF ESTIMATES: The preparation of financial statements, in conformity with U.S. generally accepted accounting principles, requires management to make estimates and assumptions based on available information that affect the reported amounts in the financial statements and the disclosures provided, and actual results could differ.

CASH FLOWS: For purposes of reporting cash flows, cash and cash equivalents include cash, deposits in other financial institutions with maturities fewer than 90 days, and federal funds sold. Federal funds are sold for a one day period and are highly liquid investments. Net cash flows are reported for customer loan and deposit transactions, interest-bearing deposits in other financial institutions, and federal funds purchased.

INTEREST-BEARING DEPOSITS IN OTHER FINANCIAL INSTITUTIONS: Interest bearing deposits in other financial institutions mature within five years and are carried at cost.

INVESTMENT SECURITIES: Debt securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Debt securities are classified as available for sale when they might be sold before maturity. Equity securities with readily determinable fair values are classified as available for sale. Available for sale securities are recorded at fair value with unrealized holding gains and losses reported in other comprehensive income, net of tax. At the time of purchase, the Bank designates securities as either held to maturity or available for sale based on its investment objectives, operational needs, and intent.

There were no additions to held to maturity or available for sale during 2015.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized on the level-yield method without anticipating prepayments, except for mortgage backed securities where prepayments are anticipated. Gains and losses on sales are recorded on the settlement date and determined using the specific identification method.

An investment security is impaired when its carrying value is greater than its fair value. Investment securities are evaluated for other-than-temporary impairment ("OTTI") on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the magnitude and duration of the decline and the intent and ability of the Bank to retain its investment in the securities for a period of time sufficient to allow for an anticipated recovery in fair value, in addition to the reasons underlying the decline, to determine whether the loss in value is other than temporary. The term "other than temporary" is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) other-than-temporary impairment (OTTI) related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. For equity securities, the entire amount of impairment is recognized through earnings.

LOANS HELD FOR SALE: Loans originated and intended for sale in the secondary market are carried at the lower of aggregate cost or fair value. Net unrealized losses, if any, are recorded as a valuation allowance and charged to earnings.

Loans held for sale are generally sold with servicing rights retained. The carrying value of loans sold is reduced by the amount allocated to the servicing right. If the loans are sold with servicing retained, the fair value of the servicing asset or liability is recorded on the balance sheet. Gains and losses on the sold portion of the loan is recognized at the time of sale based on the difference between the sale proceeds and the carrying value of the related loans sold.

LOANS: Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the amount of unpaid principal balances outstanding, net of deferred loan fees and costs, and an allowance for loan losses. Interest income is accrued on the unpaid principal balance daily and credited to income as it is earned. When a loan pays off or is sold, any unamortized balance of any related premiums, discounts, loan origination fees, and direct loan origination costs is recognized in income. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income over the expected life of the loan using a method that approximates the level yield method without anticipating prepayments.

Accrual of interest is generally discontinued on loans which are more than 90 days delinquent or when management believes, after considering economic and business conditions and collection efforts, that the borrower's financial condition is such that collection of interest is doubtful unless the loan is well-secured and in the process of collection. Past due status is based on the contractual terms of the loan. A loan is moved to non-accrual status in accordance with the Bank's policy, typically after 90 days of non-payment. In all cases, loans are placed on non-accrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. Non-accrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

When a loan is placed on non-accrual status, all interest previously accrued but not collected is reversed against current period interest income. Interest received on such loans is accounted for on the cash-basis method and recognized only to the extent that cash is received and where the future collection of principal is probable, until qualifying for return to accrual. Generally, loans will be restored to an accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

CONCENTRATION OF CREDIT RISK: Most of the Bank's business activity is with customers located within Santa Cruz County. Therefore, the Bank's exposure to credit risk is significantly affected by changes in the economy in the Santa Cruz County area.

ALLOWANCE FOR LOAN LOSSES: The allowance for loan losses is an estimate of probable credit losses in the Bank's loan portfolio that have been incurred as of the balance sheet date. The allowance is established through a provision for loan losses which is charged to expense. Additions to the allowance are expected to maintain the adequacy of the total allowance after credit losses and loan growth. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Cash received on previously charged-off amounts is recorded as a recovery to the allowance. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged-off.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Generally, the Bank identifies loans to be reported as impaired when such loans are in non-accrual status or classified in part or in whole as either doubtful or loss. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings (TDRs) and classified as impaired.

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

Commercial and commercial real estate loans over $100,000 are individually evaluated for impairment. Typically, loans below $100,000 from all class types are excluded from individual impairment analysis. When a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of expected future cash flows discounted at the loan's effective interest rate, except that as a practical expedient, it may measure impairment based on a loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. A loan is collateral dependent if the repayment of the loan is expected to be provided solely by the underlying collateral. Large groups of smaller balance homogeneous loans, such as consumer and residential real estate loans are collectively evaluated for impairment, and accordingly, they are not separately identified for impairment disclosures.

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the Bank, for economic or legal reasons related to the debtor's financial difficulties, grants a concession to the debtor that it would not otherwise consider. Restructured workout loans typically present an elevated level of credit risk as the borrowers are not able to perform according to the original contractual terms. Troubled debt restructurings are individually evaluated for impairment and included in the separately identified impairment disclosures. TDRs are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a TDR is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral less estimated costs to sell. For TDRs that subsequently default, the Bank determines the amount of the allowance on that loan in accordance with the accounting policy for the allowance for loan losses on loans individually identified as impaired. The Bank incorporates recent historical experience related to TDRs including the performance of TDRs that subsequently default into the calculation of the allowance by loan portfolio segment.

The determination of the general reserve for loans that are not impaired is collectively evaluated and based on estimates made by management, to include, but not limited to, consideration of historical losses by portfolio segment, internal asset classifications, and qualitative factors to include economic trends in the Bank's service areas, industry experience and trends, geographic concentrations, estimated collateral values, the Bank's underwriting policies, the character of the loan portfolio, and probable losses inherent in the portfolio taken as a whole. The historical loss experience is determined by portfolio segment and is based on considerations of both the Bank's actual historical loss history and losses of the peer group in which the Bank operates over the most recent 7 years.

The Bank maintains a separate allowance for each portfolio segment (loan type). These portfolio segments include commercial real estate, land and construction, commercial and industrial, agricultural land, real estate and production, and consumer loans (principally home equity loans). Portfolio classes are not distinguished from segments for reporting purposes. The allowance for loan losses attributable to each portfolio segment, which includes both impaired loans and loans that are not impaired, is combined to determine the Bank's overall allowance, hence, is included on the balance sheet.

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

Commercial real estate – Commercial real estate mortgage loans generally possess a higher inherent risk of loss than other real estate portfolio segments, except land and construction loans. Adverse economic developments or an overbuilt market impact commercial real estate projects and may result in troubled loans. Trends in vacancy rates of commercial properties impact the credit quality of these loans. High vacancy rates reduce operating revenues and the ability for properties to produce sufficient cash flow to service debt obligations.

Land and construction – Land and construction loans generally possess a higher inherent risk of loss than other real estate portfolio segments. A major risk arises from the necessity to complete projects within specified cost and time lines. Trends in the construction industry significantly impact the credit quality of these loans, as demand drives construction activity. In addition, trends in real estate values significantly impact the credit quality of these loans, as property values determine the economic viability of construction projects.

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

Agricultural land, real estate and production – Agricultural real estate mortgage loans generally possess a lower inherent risk of loss than other real estate portfolio segments, including land and construction loans. Adverse economic developments may result in troubled loans. Loans secured by crop production and livestock are especially vulnerable to two risk factors that are largely outside the control of Bank and borrowers: commodity prices and weather conditions.

Consumer – Comprised of single family residential real estate, home equity lines of credit, personal lines and installment loans. The degree of risk in residential real estate lending depends primarily on the loan amount in relation to collateral value, the interest rate and the borrower's ability to repay in an orderly fashion.

These loans generally possess a lower inherent risk of loss than other real estate portfolio segments. An installment loan portfolio is usually comprised of a large number of small loans scheduled to be amortized over a specific period. Most installment loans are made directly for consumer purchases, but business loans granted for the purchase of heavy equipment or industrial vehicles may also be included. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Weak economic trends indicate that the borrowers' capacity to repay their obligations may be deteriorating.

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

SERVICING RIGHTS: When loans are sold with servicing retained, servicing rights are initially recorded at fair value with the income statement effect recorded in gains on sales of loans. Fair value is based on market prices for comparable mortgage servicing contracts, when available or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. All classes of servicing assets are subsequently measured using the amortization method which requires servicing rights to be amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying loans.

Servicing rights are evaluated for impairment based upon the fair value of the rights as compared to carrying amount. Impairment is determined by stratifying rights into groupings based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual grouping, to the extent that fair value is less than the carrying amount. If the Bank later determines that all or a portion of the impairment no longer exists for a particular grouping, a reduction of the allowance may be recorded as an increase to income. Changes in valuation allowances are reported with loan servicing fees income on the income statement. The fair values of servicing rights are subject to significant fluctuations as a result of changes in estimated and actual prepayment speeds and default rates and losses.

Servicing fee income, which is reported on the income statement as loan servicing fees, is recorded for fees earned on servicing loans. The fees are based on a fixed amount per loan and recorded as income when earned. The amortization of servicing rights is netted against loan servicing fee income. Servicing fees totaled $565,882 and $507,478 for the years ended December 31, 2015 and 2014, respectively. Late fees and ancillary fees related to loan servicing are not material.

REAL ESTATE OWNED: Assets acquired through or instead of foreclosure are initially recorded at fair value of the property, less estimated selling expenses, establishing a new cost basis. Any write-down to fair value at the time of transfer to foreclosed real estate is charged to the allowance for loan losses. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. If fair value declines subsequent to foreclosure, a valuation allowance is recorded through expense. Operating costs incurred after acquisition and in conjunction with the maintenance of real estate acquired through foreclosure are charged to expense as incurred.

PREMISES AND EQUIPMENT: Premises and equipment are stated at cost less accumulated depreciation and amortization. Leasehold improvements are amortized over the shorter of the estimated useful life or the initial term of the respective leases. Certain operating leases contain incentives in the form of tenant improvement allowances or credits. Lease incentives are capitalized at the inception of the lease and amortized on a straight-line basis over the original lease term with useful lives ranging from 3 to 10 years. Furniture, fixtures and equipment are depreciated using the straight line method with useful lives ranging from 5 to 7 years. All other maintenance and repair expenditures are expensed as incurred.

FEDERAL HOME LOAN BANK STOCK: The Bank, as a member of the Federal Home Loan Bank ("FHLB") system, is required to maintain an investment in the capital stock of the FHLB of San Francisco based on the level of borrowings and other factors, and may invest in additional amounts. FHLB stock is carried at cost, classified as restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. The FHLB stock is redeemable at its par value of $100 per share at the discretion of the FHLB of San Francisco. The FHLB can suspend dividends and redemptions upon notification to its members. Both cash and stock dividends, if any, are reported as income.

PACIFIC COAST BANKERS BANK STOCK: Pacific Coast Bankers Bank stock is carried at cost, classified as restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends, if any, are reported as income.

BANK OWNED LIFE INSURANCE: The Bank has purchased life insurance policies on certain key executives. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

LOAN COMMITMENTS AND RELATED FINANCIAL INSTRUMENTS: Financial instruments include off balance sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

STOCK-BASED COMPENSATION: Compensation cost is recognized for stock options and restricted stock awards issued to employees and directors, based on the fair value of these awards at the date of grant. The Bank estimates the fair value of each stock option award as of the date of grant using a Black-Scholes-Merton model, while the market price of the Bank's common stock at the date of grant is used for restricted stock awards. Compensation cost is recognized over the required service period, generally defined as the vesting period.

INCOME TAXES: Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred income taxes are computed using the asset and liability method, which recognizes a liability or asset representing the tax effects, based on current tax law, of future deductible or taxable amounts attributable to events that have been recognized in the financial statements. A valuation allowance is established to reduce the deferred tax asset to the level at which it is "more likely than not" that the tax asset or benefits will be realized. Deferred tax assets and liabilities are calculated by applying current enacted tax rates against future deductible or taxable amounts. Realization of tax benefits of deductible temporary differences and operating loss carry forwards depends on having sufficient taxable income of an appropriate character within the carry forward periods.

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

The Bank recognizes interest and/or penalties related to income tax matters in income tax expense.

RETIREMENT PLANS: Pension expense is the net of service and interest cost, return on plan assets and amortization of gains and losses not immediately recognized. Employee 401(k) plan expense is the amount of matching contributions. Deferred compensation and supplemental retirement plan expense allocates the benefits over years of service.

EARNINGS PER COMMON SHARE: Basic earnings per common share are calculated by dividing net income by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share takes into account the potential dilutive impact of such instruments and uses the average share price for the period in determining the number of incremental shares to add to the weighted-average number of shares outstanding. There is no adjustment to the number of outstanding shares for potential dilutive instruments, such as stock options, when a loss occurs because the conversion of potential common stock is anti-dilutive or when stock options are not in-the-money.

COMPREHENSIVE INCOME: Comprehensive income consists of net income and other comprehensive (loss) income. Other comprehensive income includes the adjustment to fully recognize the liability associated with the supplemental executive retirement plan and unrealized gains and losses on securities available for sale, which are also recognized as separate components of equity.

LOSS CONTINGENCIES: Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated.

DIVIDEND RESTRICTION: Banking regulations require maintaining certain capital levels and may limit the dividends paid by the Bank to shareholders.

FAIR VALUE OF FINANCIAL INSTRUMENTS: The Bank's estimated fair value amounts have been determined by the Bank using relevant market information and other assumptions, as more fully disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect these estimates.

RECLASSIFICATIONS: Certain reclassifications have been made to prior period financial statements to conform to the current year presentation. These reclassifications had no impact on the Bank's previously reported financial statements.

ADOPTION OF NEW ACCOUNTING STANDARDS AND NEWLY ISSUED NOT YET EFFECTIVE ACCOUNTING STANDARDS

The following are descriptions of recently adopted or newly issued not yet effective accounting standards that could have a material effect on our financial statements:

ASU 2014-04, Receivables – Troubled Debt Restructurings by Creditors (Subtopic 310-40) – Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans Upon Foreclosure: In January 2014, the FASB amended existing guidance to clarify when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan such that the loan should be derecognized and the real estate recognized. These amendments clarify that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either: (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure, or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Additional disclosures are required. These amendments are effective for annual periods and interim periods within those annual periods beginning after December 15, 2014. Amendments in this standard can be applied using a modified retrospective and prospective transition method. Early adoption is permitted. The adoption of this standard did not have a material effect on the Bank's operating results or financial condition.

ASU 2014-09, Revenue From Contracts With Customers: In May 2014 the FASB amended existing guidance related to revenue from contracts with customers. This amendment supersedes and replaces nearly all existing revenue recognition guidance, including industry-specific guidance, establishes a new control-based revenue recognition model, changes the basis for deciding when revenue is recognized over time or at a point in time, provides new and more detailed guidance on specific topics and expands and improves disclosures about revenue. In addition, this amendment specifies the accounting for some costs to obtain or fulfill a contract with a customer. These amendments are effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early application is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that period. The amendments should be applied retrospectively to all periods presented or retrospectively with the cumulative effect recognized at the date of initial application. The Bank is currently evaluating the impact of this new accounting standard on the financial statements.

ASU 2014-14, Receivables – Troubled Debt Restructurings by Creditors (Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans Upon Foreclosure: In August 2014, the FASB amended existing guidance related to the classification of certain government-guaranteed mortgage loans, including those guaranteed by the FHA and the VA, upon foreclosure. It requires that a mortgage loan be derecognized and a separate other receivable be recognized upon foreclosure if the following conditions are met: 1) The loan has a government guarantee that is not separable from the loan before foreclosure; 2) At the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim; and 3) At the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. These amendments are effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. Early adoption is permitted if the amendments under ASU 2014-04 Receivables – Troubled Debt Restructurings by Creditors – Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans Upon Foreclosure has been adopted. The amendments may be applied using a prospective transition method in which a reporting entity applies the guidance to foreclosures that occur after the date of adoption, or a modified retrospective transition using a cumulative-effect adjustment (through a reclassification to a separate other receivable) as of the beginning of the annual period of adoption. Prior periods should not be adjusted. A reporting entity must apply the same method of transition as elected under ASU 2014-04. The adoption of this standard did not have a material effect on the Bank's operating results or financial condition.

NOTE 2. INVESTMENT SECURITIES

The following tables summarize the amortized cost and fair value of securities available for sale and held to maturity at December 31, 2015, and 2014 and the corresponding amounts of gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) and gross unrecognized gains and losses:

December 31, 2015	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available for sale:				
U.S. government sponsored agencies	$ 3,016,458	$ 11,362	$ -	$ 3,027,820
Collateralized mortgage obligations	7,094,029	53,556	(5,323)	7,142,262
State and political subdivision	349,522	11,418	-	360,940
Corporate	103,682	894	-	104,576
Total available for sale	$ 10,563,691	$ 77,230	$ (5,323)	$ 10,635,598

	Amortized Cost	Gross Unrecognized Gains	Gross Unrecognized Losses	Estimated Fair Value
Held to maturity:				
U.S. government sponsored agencies	$ 8,671,939	$ 115,381	$ -	$ 8,787,320
Mortgage backed securities: residential	6,169,926	111,732	(318)	6,281,340
Collateralized mortgage obligations	13,249,217	283,372	(6,044)	13,526,545
State and political subdivision	11,125,576	702,125	-	11,827,701
Corporate	-	-	-	-
Total held to maturity	$ 39,216,658	$ 1,212,610	$ (6,362)	$ 40,422,906

December 31, 2014	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available for sale:				
U.S. government sponsored agencies	$ 3,021,895	$ 6,699	$ (2,094)	$ 3,026,500
Collateralized mortgage obligations	7,570,920	41,921	(15,580)	7,597,261
State and political subdivision	422,318	3,028	(82)	425,264
Corporate	109,826	675	(20)	110,481
Total available for sale	$ 11,124,959	$ 52,323	$ (17,776)	$ 11,159,506

	Amortized Cost	Gross Unrecognized Gains	Gross Unrecognized Losses	Estimated Fair Value
Held to maturity:				
U.S. government sponsored agencies	$ 8,833,556	$ 116,264	$ -	$ 8,949,820
Mortgage backed securities: residential	8,323,655	181,060	-	8,504,715
Collateralized mortgage obligations	16,537,757	306,924	(9,517)	16,835,164
State and political subdivision	12,685,251	681,507	-	13,366,758
Corporate	-	-	-	-
Total held to maturity	$ 46,380,219	$ 1,285,755	$ (9,517)	$ 47,656,457

There were no transfers between available for sale and held to maturity during 2014 or 2015.

The proceeds from sales and calls of investment securities and the associated gains and losses during 2015 are listed below:

	2015
Proceeds	1,530,347
Gains	1,453
Losses	-

The tax provision related to the net realized gains and losses was $598 for year-end 2015. The bank did not recognize any gains or losses on securities during 2014.

The amortized cost and estimated fair value of debt securities are shown by contractual maturity. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately.

	2015	
	Amortized Cost	Estimated Fair Value
Available for sale:		
Within one year	$ -	$ -
One to five years	3,120,140	3,132,396
Five to ten years	349,522	360,940
Beyond ten years	-	-
Mortgage-backed securities	7,094,029	7,142,262
Total	$ 10,563,691	$ 10,635,598
Held to maturity:		
Within one year	$ 136,460	$ 136,842
One to five years	10,122,165	10,296,176
Five to ten years	4,968,647	5,236,773
Beyond ten years	4,570,243	4,945,229
Mortgage-backed securities	19,419,143	19,807,886
Total	$ 39,216,658	$ 40,422,906

Investment securities pledged to secure public deposits at year end December 31, 2015 and 2014 had a carrying amount of $18,197,000 and $20,993,000, respectively.

At year end 2015 and 2014, there were no holdings of securities of any one issuer, other than the U.S. Government and its agencies, in an amount greater than 10% of shareholders' equity.

The following table summarizes investment securities with unrealized losses at December 31, 2015 and 2014 aggregated by major security type and length of time in a continuous unrealized loss position:

December 31, 2015:	Less than 12 months		12 months or more		Total	
Held to maturity:	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mortgage backed securities: residential	$ 146,572	$ (318)	$ -	$ -	$ 146,572	$ (318)
U.S. government sponsored agencies	-	-	-	-	-	-
Collateralized mortgage obligations	899,223	(6,044)	-	-	899,223	(6,044)
State and political subdivision	-	-	-	-	-	-
Corporate	-	-	-	-	-	-
Total held to maturity:	$ 1,045,795	$ (6,362)	$ -	$ -	$ 1,045,795	$ (6,362)

	Less than 12 months		12 months or more		Total	
Available for sale:	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mortgage backed securities: residential	$ -	$ -	$ -	$ -	$ -	$ -
U.S. government sponsored agencies	-	-	-	-	-	-
Collateralized mortgage obligations	3,013,713	(5,323)	-	-	3,013,713	(5,323)
State and political subdivision	-	-	-	-	-	-
Corporate	-	-	-	-	-	-
Total available for sale:	$ 3,013,713	$ (5,323)	$ -	$ -	$ 3,013,713	$ (5,323)

December 31, 2014:	Less than 12 months		12 months or more		Total	
Held to maturity:	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Collateralized mortgage obligations	$ 1,343,623	$ (5,591)	$ 347,976	$ (3,927)	$ 1,691,599	$ (9,517)
Total held to maturity:	$ 1,343,623	$ (5,591)	$ 347,976	$ (3,927)	$ 1,691,599	$ (9,517)

	Less than 12 months		12 months or more		Total	
Available for sale:	Fair Value	Unrealized	Fair Value	Unrealized	Fair Value	Unrealized
U.S. government sponsored agencies	$ 1,003,760	$ (2,094)	$ -	$ -	$ 1,003,760	$ (2,094)
Collateralized mortgage obligations	4,832,812	(15,580)	-	-	4,832,812	(15,580)
State and political subdivision	50,976	(82)	-	-	50,976	(82)
Corporate	5,099	(20)	-	-	5,099	(20)
Total available for sale:	$ 5,892,647	$ (17,776)	$ -	$ -	$ 5,892,647	$ (17,776)

As of December 31, 2015, the Bank's security portfolio consisted of 101 investment securities, 6 of which were in an unrealized loss position less than twelve months and none over twelve months. The majority of unrealized losses are related to the Bank's collateralized mortgage obligations as discussed below.

Collateralized Mortgage Obligations: At December 31, 2015, 100% of the collateralized mortgage obligations held by the Bank were issued by U.S. Government or government-sponsored entities and agencies, primarily Fannie Mae and Freddie Mac, institutions which the government has affirmed its commitment to support. Because the decline in fair value is attributable to changes in interest rates and illiquidity, and not credit quality, and because the Bank does not have the intent to sell these mortgage backed securities and it is likely that it will not be required to sell the securities before their anticipated recovery, the Bank does not consider these securities to be other-than-temporarily impaired at December 31, 2015. The Bank's mortgage backed securities portfolio does not include non-agency collateralized mortgage obligations.

NOTE 3. LOANS RECEIVABLE

The outstanding loan portfolio balances at December 31, 2015 and 2014 are as follows:

	December 31,	
	2015	**2014**
Commercial and industrial	$ 88,263,714	$ 85,459,268
Commercial real estate	155,513,191	125,239,850
Land and construction	27,424,918	10,746,164
Agricultural land, real estate and production	11,913,756	19,103,279
Consumer	32,701,492	42,135,267
Gross loans receivable	315,817,071	282,683,829
Net deferred loan fees	1,831,698	1,290,898
Allowance for loan losses	(7,362,210)	(6,402,752)
Loans receivable, net	$ 310,286,559	$ 277,571,975

The following table shows the allocation of the allowance for loan losses by portfolio segment for the years ended December 31, 2015 and December 31, 2014:

December 31, 2015:	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Unallocated	Total
Allowance for loan losses:							
Beginning balance	$ 2,258,217	$ 2,080,960	$ 1,021,894	$ 107,894	$ 644,395	$ 289,392	$ 6,402,752
Provision for loan losses	(47,884)	257,411	1,127,545	(61,104)	(399,137)	43,169	920,000
Loans charged-off	(14,226)	-	-	(1)	(18,846)	-	(33,073)
Recoveries	600	66,259	-	-	5,672	-	72,531
Total ending allowance balance	$ 2,196,707	$ 2,404,630	$ 2,149,439	$ 46,789	$ 232,084	$ 332,561	$ 7,362,210

December 31, 2014:	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Unallocated	Total
Allowance for loan losses:							
Beginning balance	$ 2,016,912	$ 2,320,293	$ 661,037	$ 45,303	$ 512,672	$ 149,645	$ 5,705,862
Provision for loan losses	303,914	(246,832)	360,857	62,591	129,723	139,747	750,000
Loans charged-off	(66,666)	-			(500)	-	(67,166)
Recoveries	4,057	7,499	-	-	2,500	-	14,056
Total ending allowance balance	$ 2,258,217	$ 2,080,960	$ 1,021,894	$ 107,894	$ 644,395	$ 289,392	$ 6,402,752

The following table shows the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of December 31, 2015 and 2014:

December 31, 2015:	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Unallocated	Total
Allowance for loan losses							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	$ -	$ 33,812	$ -	$ -	$ -	$ -	$ 33,812
Collectively evaluated for impairment	2,196,707	2,370,818	2,149,439	46,789	232,084	332,561	7,328,398
Total ending allowance balance	$ 2,196,707	$ 2,404,630	$ 2,149,439	$ 46,789	$ 232,084	$ 332,561	$ 7,362,210
Loans							
Loans individually evaluated for impairment	$ -	$ 291,959	$ -	$ -	$ -	$ -	$ 291,959
Loans collectively evaluated for impairment	88,263,714	155,221,233	27,424,918	11,913,756	32,701,492		315,525,113
Total ending loans balance	$ 88,263,714	$ 155,513,192	$27,424,918	$ 11,913,756	$ 32,701,492	$ -	$ 315,817,072

December 31, 2014:	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Unallocated	Total
Allowance for loan losses							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	$ 578	$ 45,567	$ -	$ -	$ -	$ -	$ 46,145
Collectively evaluated for impairment	2,257,639	2,035,393	1,021,894	107,894	644,395	289,392	6,356,607
Total ending allowance balance	$ 2,258,217	$ 2,080,960	$ 1,021,894	$ 107,894	$ 644,395	$ 289,392	$ 6,402,752
Loans							
Loans individually evaluated for impairment	$ 2,862	$ 302,153	$ -	$ -	$ -	$ -	$ 305,015
Loans collectively evaluated for impairment	85,456,406	124,937,697	10,746,164	19,103,279	42,135,267		282,378,814
Total ending loans balance	$ 85,459,268	$ 125,239,850	$ 10,746,164	$ 19,103,279	$ 42,135,267	$ -	$ 282,683,829

The following table shows information related to impaired loans, by class of loans, as of and for the years ended December 31, 2015 and 2014:

	Unpaid Principal Balance	Recorded Investment	Allowance for loan losses allocated	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
With no related allowance recorded:						
Commercial real estate	$ 137,949	$ 137,949	$ -	$ 140,812	$ 6,337	$ -
Total	137,949	137,949	-	140,812	6,337	-
With an allowance recorded:						
Commercial real estate	154,010	154,010	33,812	156,351	10,554	-
Total	154,010	154,010	33,812	156,351	10,554	-
Total:						
Commercial real estate	291,959	291,959	33,812	297,163	16,890	-
Total	$ 291,959	$ 291,959	$ 33,812	$ 297,163	$ 16,890	$ -

Impaired Loans
For the Year ended December 31, 2014

	Unpaid Principal Balance	Recorded Investment	Allowance for loan losses allocated	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
With no related allowance recorded:						
Commercial real estate	$ 143,358	$ 143,358	$ -	$ 147,137	$ 6,787	$ -
Total	143,358	143,358	-	147,137	6,787	-
With an allowance recorded:						
Commercial and industrial	2,862	2,862	578	3,411	505	-
Commercial real estate	158,795	158,795	45,567	112,104	10,860	-
Total	161,657	161,657	46,145	115,515	11,365	-
Total:						
Commercial and industrial	2,862	2,862	578	3,411	505	-
Commercial real estate	302,153	302,153	45,567	259,241	17,648	-
Total	$ 305,015	$ 305,015	$ 46,145	$ 262,652	$ 18,153	$ -

The recorded investment in loans excludes accrued interest receivable and loan origination fees, net due to immateriality. For purposes of this disclosure, the unpaid principal balance is not reduced for partial charge-offs.

Non-accrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified as impaired loans.

The Bank had no past due or non-accrual loans as of December 31, 2015 and 2014.

TROUBLED DEBT RESTRUCTURINGS: As of December 31, 2015 and 2014, the Bank had no troubled debt restructurings.

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

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

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

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

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

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

The following table shows the loan portfolio by class allocated by management's internal risk ratings at December 31, 2015 and 2014:

December 31, 2015	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Total
Pass	$ 87,663,644	$ 144,932,724	$ 27,424,918	$ 11,913,756	$ 31,968,954	$ 303,903,996
Special Mention	578,067	10,288,508	-	-	732,538	11,599,113
Substandard	22,003	291,959	-	-	-	313,962
Doubtful	-	-	-	-	-	-
Total	$ 88,263,714	$ 155,513,191	$ 27,424,918	$ 11,913,756	$ 32,701,492	$ 315,817,071

December 31, 2014	Commercial and Industrial	Commercial Real Estate	Land and Construction	Agricultural Land, Real Estate and Production	Consumer	Total
Pass	$ 84,758,615	$ 123,358,806	$ 10,746,164	$ 19,103,279	$ 42,131,210	$ 280,098,074
Special Mention	668,633	1,540,016	-	-	-	2,208,649
Substandard	32,020	341,029	-	-	4,057	377,106
Doubtful	-	-	-	-	-	-
Total	$ 85,459,268	$ 125,239,851	$ 10,746,164	$ 19,103,279	$ 42,135,267	$ 282,683,829

NOTE 4. REAL ESTATE OWNED

The Bank currently owns one property with no recorded investment. There were no loans foreclosed during 2015. Real estate owned activity during 2014 was as follows:

	2014
Beginning balance	$ 358,584
Loans transferred to real estate owned	-
Capitalized expenditures	-
Direct Write-Downs / Recovery	(200,000)
Sales of real estate owned	(158,584)
End of year	$ 0

The funds spent over the last year have been to hold the property and consider its potential for sale in the future. Expenses related to real estate owned include:

	2015	2014
Net gain on sales	$ -	$ (55,020)
Write-downs	-	200,000
Operating expenses, net of rental income	7,918	28,799
	$ 7,918	$ 173,779

NOTE 5. FAIR VALUE

FAIR VALUE HIERARCHY:

The Bank groups its assets and liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. Valuations within these levels are based upon:

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

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

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

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

CASH AND CASH EQUIVALENTS: The carrying amount of cash and cash equivalents is a reasonable estimate of fair value and are classified as Level 1.

INTEREST-BEARING DEPOSITS IN OTHER FINANCIAL INSTITUTIONS: The fair values were calculated using discounted cash flow models based on market rates resulting in a Level 2 classification.

INVESTMENT SECURITIES: The fair values of securities classified as available for sale and held to maturity are based on quoted market prices, if available (Level 1) at the reporting date. For securities where quoted prices are not available, fair values are calculated based on market prices of similar securities (Level 2). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3).

LOANS HELD FOR SALE: Loans held for sale are carried at the lower of cost or fair value, which is evaluated on a pool-level basis. The fair value of loans held for sale is determined using quoted prices for similar assets, adjusted for specific attributes of that loan or other observable market data, such as outstanding commitments from third party investors (Level 2).

LOANS: The fair value of fixed rate loans is determined as the present value of expected future cash flows discounted at the interest rate currently offered by the Bank, which approximates rates currently offered by local lending institutions for loans of similar terms to companies with comparable credit risk resulting in a Level 3 classification. Variable rate loans which re-price frequently with changes in approximate market rates were valued using the outstanding principal balance resulting in a Level 3 classification. The estimated fair value of loan commitments and contingent liabilities at December 31, 2015 and December 31, 2014 approximate their current book values.

IMPAIRED LOANS: The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

BANKERS' BANK STOCK: Bankers' Bank Stock includes Federal Home Loan Bank Stock and Pacific Coast Bankers Bank Stock. The Federal Home Loan Bank investment is carried at cost and is redeemable at par with certain restrictions. It is not practical to determine fair value of bank stock due to restrictions placed on transferability.

ACCRUED INTEREST RECEIVABLE/PAYABLE: The carrying amounts of accrued interest approximate their fair value resulting in a Level 2 or Level 3 classification.

DEPOSITS: The fair values of demand deposits, savings deposits, and money market deposits without defined maturities were the amounts payable on demand resulting in a Level 1 classification. For variable rate deposits where the Bank has the contractual right to change rates, carrying value was assumed to approximate fair value resulting in a Level 1 classification.

CERTIFICATES OF DEPOSIT: For deposits with defined maturities, the fair values were calculated using discounted cash flow models based on market interest rates for different product types and maturity dates. The discount rates used were based on rates for comparable deposits resulting in a Level 2 classification.

ASSETS RECORDED AT FAIR VALUE

The Bank's assets and liabilities measured at fair value on a recurring and non-recurring basis as of December 31, 2015 and 2014 are summarized below:

RECURRING BASIS

The Bank is required or permitted to record the following assets at fair value on a recurring basis.

	December 31, 2015			
	Fair Value	Level 1	Level 2	Level 3
Securities available for sale:				
U.S. government sponsored agencies	$ 3,027,820	$ -	$ 3,027,820	$ -
Mortgage backed securities: residential	-	-	-	-
Collateralized mortgage obligations	7,142,262	-	7,142,262	-
State and political subdivision	360,940	-	360,940	-
Corporate	104,576	-	104,576	-
Total assets measured at fair value	$10,635,598	$ -	$10,635,598	$ -

	December 31, 2014			
	Fair Value	Level 1	Level 2	Level 3
Securities available for sale:				
U.S. government sponsored agencies	$ 3,026,500	$ -	$ 3,026,500	$ -
Mortgage backed securities: residential	-	-	-	-
Collateralized mortgage obligations	7,597,261	-	7,597,261	-
State and political subdivision	425,264	-	425,264	-
Corporate	110,481	-	110,481	-
Total assets measured at fair value	$11,159,506	$ -	$11,159,506	$ -

Fair values for available for sale investment securities are based on quoted market prices for similar securities. During the years ended December 31, 2015 and 2014, there were no transfers in or out of Levels 1 and 2.

There were no recurring Level 3 assets or liabilities measured at fair value during 2015 or 2014.

NON-RECURRING BASIS

The Bank may be required, from time to time, to measure certain assets at fair value on a non-recurring basis. These include assets that are measured at the lower of cost or market value that were recognized at fair value which was below cost at the reporting date:

	December 31, 2015:				
	Fair Value	Level 1	Level 2	Level 3	Total Gains and (Losses)
Impaired Loans:					
Commercial Real Estate	$ 120,198	$ -	$ -	$ 120,198	$ 11,755
Total ending loans balance	$ 120,198	$ -	$ -	$ 120,198	$ 11,755

	December 31, 2014:				
	Fair Value	Level 1	Level 2	Level 3	Total Gains and (Losses)
Impaired Loans:					
Commercial and Industrial	$ 2,284	$ -	$ -	$ 2,284	$ (525)
Commercial Real Estate	113,228	-	-	113,228	5,928
Total ending loans balance	$ 115,512	$ -	$ -	$ 115,512	$ 5,403

The impaired loans and real estate owned fair values are determined using independent appraisers. The Bank considers these third-party appraisals as Level 3 classifications due to the significant unobservable inputs used to measure the fair values of these properties. These unobservable inputs include adjustments for differences between comparable sales and discount rates.

The following table presents the carrying amounts and estimated fair values of the Bank's financial instruments at December 31, 2015 and December 31, 2014. The fair value of financial instruments does not represent actual amounts that may be realized upon any sale or liquidation of the related assets or liabilities. In addition, these values do not give effect to discounts to fair value which may occur when financial instruments are sold in larger quantities. The fair values presented represent the Bank's best estimate of fair value using the methodologies discussed below.

The respective carrying values of certain on-balance-sheet financial instruments approximated their fair values. These financial instruments include accrued interest receivable and accrued interest payable. Carrying values were assumed to approximate fair values for these financial instruments as they are short term in nature and their recorded amounts approximate fair values or are receivable or payable on demand. The Bank does not use derivative financial instruments.

December 31, 2015

(Dollars in thousands)	Carrying Amount	Level 1	Level 2	Level 3	Total
Financial Assets:					
Cash and cash equivalents	$ 9,414	$ 9,414	$ -	$ -	$ 9,414
Interest bearing deposits in other Financial Institutions	85,586	-	85,586	-	85,586
Debt and other securities	23,292	-	24,108	-	24,108
MBS and CMO securities	26,561	-	26,950	-	26,950
Loans held for sale	42,091	-	45,022	-	45,022
Loans, net	310,287	-	-	310,679	310,679
Bankers' Bank stock	1,878	N/A	N/A	N/A	N/A
Accrued interest receivable	1,612	74	312	1,226	1,612
Financial Liabilities:					
Noninterest-bearing demand deposits	$ 208,936	$ 208,936	$ -	$ -	$ 208,936
Interest-bearing demand deposits	58,796	60,659	-	-	60,659
Savings and money market deposits	123,888	123,802	-	-	123,802
Time certificates of deposit	70,615	-	69,621	-	69,621
Accrued interest payable	70	5	65	-	70

December 31, 2014

(Dollars in thousands)	Carrying Amount	Level 1	Level 2	Level 3	Total
Financial Assets:					
Cash and cash equivalents	$ 9,505	$ 9,505	$ -	$ -	$ 9,505
Interest bearing deposits in other Financial Institutions	67,592	-	67,580	-	67,580
Securities available-for-sale	11,160	-	11,160	-	11,160
Securities held-to-maturity	46,380	-	47,656	-	47,656
Loans held for sale	32,938	-	34,861	-	34,861
Loans, net	277,572	-	-	286,633	286,633
Bankers' Bank stock	1,591	N/A	N/A	N/A	N/A
Accrued interest receivable	1,411	56	338	1,017	1,411
Financial Liabilities:					
Noninterest-bearing demand deposits	$ 191,789	$ 191,789	$ -	$ -	$ 191,789
Interest-bearing demand deposits	45,904	46,888	-	-	46,888
Savings and money market deposits	111,600	111,514	-	-	111,514
Time certificates of deposit	64,693	-	64,707	-	64,707
Accrued interest payable	73	5	68	-	73

Management monitors the availability of observable market data to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period.

Management evaluates the significance of transfers between levels based upon the nature of the financial instrument and size of the transfer relative to total assets, total liabilities or total earnings.

NOTE 6. LOAN SERVICING

Activity for loan servicing rights follows:

	2015	2014
Loan servicing rights:		
Beginning of year	$ 720,690	$ 588,903
Additions	283,524	398,139
Disposals	-	(32,571)
Amortized to expense	(275,732)	(233,781)
End of year	$ 728,482	$ 720,690

The Bank reviews servicing rights for impairment periodically and there was no valuation allowance recorded in 2015 or 2014.

NOTE 7. PREMISES AND EQUIPMENT

The following presents the cost of premises and equipment including leasehold improvements and the related accumulated depreciation and amortization at December 31, 2015 and 2014:

	December 31, 2015	December 31, 2014
Leasehold improvements	$ 1,747,411	$ 1,747,411
Furniture, fixtures and equipment	1,735,066	1,751,204
Software and capitalized data & item processing	234,425	234,425
Computer equipment	710,667	732,114
Construction-in-progress	6,250	-
Total premises and equipment	4,433,819	4,465,154
Less accumulated depreciation and amortization	(3,899,098)	(3,698,145)
Premises and equipment, net	$ 534,722	$ 767,009

Depreciation expense was $268,737 and $339,510 for 2015 and 2014, respectively.

OPERATING LEASES: The Bank leases various branch properties and equipment under long-term operating lease agreements. These leases expire on various dates through 2020 and have various renewal options of five years each. Some leases may include a free rent period or have net operating costs associated with them.

In addition to the office building leases, the Bank has two leases for ATM & night depository kiosks. The operating leases had initial terms of five years each and various renewal options of three years each.

Building and kiosk rent expense for the years ended December 31, 2015 and 2014, was approximately $607,000 and $590,000, respectively. Lease commitments, before considering renewal options that generally are present, for future years are as follows:

Year ending December 31,	
2016	$ 610,000
2017	559,000
2018	376,000
2019	123,000
2020	61,000
	$ 1,729,000

NOTE 8. DEPOSITS

Interest-bearing deposits consisted of the following:

	December 31, 2015	December 31, 2014
NOW accounts	$ 58,796,110	$ 45,904,073
Money Market	99,096,629	85,151,918
Time Deposits	70,614,984	64,693,201
Savings	24,791,348	26,447,754
	$ 253,299,071	$222,196,946

Time deposits that meet or exceed the FDIC Insurance limit of $250,000 at year end 2015 and 2014 were $27,264,866 and $16,815,802, respectively.

The scheduled maturities for all time deposits for the next 5 years were as follows:

	2015
2016	$ 68,819,984
2017	767,622
2018	345,929
2019	488,224
2020	188,000

As of December 31, 2015, the Bank had brokered deposits totaling $3,250,358 and $5,100,130 at December 31, 2014.

NOTE 9. BORROWED FUNDS

At December 31, 2015, the Bank had federal funds borrowing guidance lines with its correspondent banks in an aggregate amount of $11.0 million on an unsecured basis. In addition, the Bank has established a secured borrowing arrangement, secured by loans totaling approximately $220,551,221, with the Federal Home Loan Bank of San Francisco (“FHLB”). As of December 31, 2015, the Bank had $116,811,311 in borrowing capacity available through the FHLB under which overnight and term advances were available. These advances are secured by assets including the Bank’s ownership interest in the capital stock of the FHLB, securities and loans.

The Bank had no borrowed funds outstanding at December 31, 2015 and December 31, 2014 under these arrangements.

NOTE 10. PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS

Effective October 1, 2004, the Bank established the Supplemental Executive Retirement Plan (SERP), an unfunded noncontributory defined benefit pension plan. The SERP provides retirement benefits to a select group of key executives and senior officers based on years of service and final average salary. The Bank uses December 31 as the measurement date for this Plan. The following table reflects the accumulated benefit obligation and funded status of the SERP for the years ended December 31, 2015 and 2014.

	2015	2014
Change in benefit obligation		
Beginning benefit obligation	$ 2,345,665	$ 2,402,470
Service cost	110,243	109,659
Interest cost	84,862	112,076
Actuarial gain	(76,907)	(238,188)
Benefits paid	(41,361)	(40,352)
Ending benefit obligation	2,422,502	2,345,665
Funded status at end of year	(2,422,502)	(2,345,665)
Unrecognized net actuarial (gain)/loss	(152,849)	(75,942)
Unrecognized prior service cost	4,490	12,970
Net liability recognized in earnings	(2,570,861)	(2,408,637)
Accrued benefit liability	(2,422,502)	(2,345,665)
Accumulated other comprehensive (loss) income	(148,359)	(62,972)
Net amount recognized	$ (2,570,861)	$ (2,408,637)

The components of net periodic benefit cost for the years ended December 31, 2015 and 2014 and forecasted net periodic benefit cost during the year ended December 31, 2016 are as follows:

	Year ended December 31,		
	2016	2015	2014
Components of net periodic benefit cost	(forecast)		
Service cost	$ 111,418	$ 110,243	$ 109,659
Interest cost	95,332	84,862	112,076
Amortization of prior service cost	4,490	8,480	8,480
Net periodic benefit cost	$ 211,240	$ 203,585	$ 230,215

Assumptions

Weighted average assumptions to determine benefit obligation as of December 31:

	2015	2014
Discount rate used to determine net periodic benefit	3.65%	4.50%
Discount rate used to determine benefit obligations	3.97%	3.65%
Future salary increases	N/A	N/A

NOTE 11. EMPLOYEE BENEFIT PLANS

401(K) PLAN: All employees of the Bank are eligible to participate in the Bank's 401(k) Plan, which is a tax-deferred savings plan designed to assist employees in preparing for their retirement years. The 401(k) Plan allows employees to contribute to the Plan up to certain limits prescribed by the Internal Revenue Service. The Bank implemented a matching program during 2013 and matches up to 25% of contributions up to 2% of compensation in 2014 and up to 3% of compensation beginning late May 2015. Total expense for the years ended December 31, 2015 and December 31, 2014 was $78,500 and $69,694, respectively.

The Bank accounts for split-dollar life insurance in accordance with ASC 715-60, Compensation - Nonretirement Postemployment Benefits, which requires that endorsement split-dollar life insurance arrangements which provide a postretirement benefit to an employee be recorded based on the substance of the agreement with the employee. If the employer has effectively agreed to provide the employee with a death benefit, the employer should accrue, over the service period, a liability for the actuarial present value of the future death benefit as of the employee's expected retirement date. The total liability recorded as of years ended December 31, 2015 and December 31, 2014 was $998,531 and $714,702, respectively. Total expense recognized during the years ended December 31, 2015 and December 31, 2014 was $283,829 and $60,000, respectively.

NOTE 12. INCOME TAXES

The provision for income taxes is as follows for the years ended December 31, 2015 and 2014:

	2015	2014
Current expense:		
Federal	$ 2,912,208	$ 2,282,829
State	1,193,538	833,671
Total current	4,105,746	3,116,500
Deferred expense:		
Federal	$ (494,467)	$ (280,221)
State	(154,296)	(52,792)
Total deferred	(648,763)	(333,013)
Total provision	$ 3,456,983	$ 2,783,487

The effective tax rates differ from the federal statutory rate of 34% applied to income before income taxes due to the following for the years ended December 31, 2015 and 2014:

	2015	2014
Federal statutory rate	34.00%	34.00%
State income tax, net of federal effect	7.71%	7.20%
Tax exempt interest	(2.96%)	(2.97%)
Bank owned life insurance	(0.69%)	(0.84%)
Split dollar expense	1.09%	0.29%
Stock based compensation	0.56%	0.51%
Other	(0.83%)	0.72%
Net	38.88%	38.90%

Deferred income taxes are the result of differences between income tax accounting and accounting principles generally accepted in the United States of America, with respect to income and expense recognition. The tax effects of temporary differences that gave rise to deferred tax assets and deferred tax liabilities at December 31, 2015 and 2014 are as follows:

	2015	2014
Allowance for loan losses	$ 2,665,674	$ 2,287,050
Deferred compensation	1,058,022	991,260
Accruals	1,155,978	944,265
Current state income tax	380,654	286,008
Premises and equipment	22,574	36,520
Unrealized (gain) loss on available for sale securities and pension		18,017
Other deferred tax assets	205,716	65,720
Gross deferred tax assets	5,488,618	4,628,840
Deferred loan costs	(1,304,952)	(1,079,408)
Unrealized (gain) loss on available for sale securities and pension	(27,602)	
Other deferred tax liabilities	(83,694)	(80,206)
Gross deferred tax liabilities	(1,416,248)	(1,159,614)
Net deferred tax asset	$ 4,072,370	$ 3,469,226

Management believes that it is more likely than not that the deferred tax assets will be realized as a result of expected continued profitability. Accordingly, no valuation allowance has been established as of December 31, 2015 or December 31, 2014.

The Bank files income tax returns in the United States and California jurisdictions. Unrecognized tax benefits are not expected to significantly increase or decrease within the next twelve months. The Bank's federal and state tax returns for the years 2012 to 2015 and 2011 to 2015, respectively, are currently open for examination.

The bank did not have any interest and penalties recorded in the income statement for the year ended December 31, 2015 and $1,063 for the year ended December 31, 2014.

NOTE 13. RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Bank makes loans to directors, officers, shareholders and their associates. At December 31, 2015 and 2014, no related party loans were on nonaccrual or classified for regulatory reporting purposes.

Loan related activity to directors, officers, and principal shareholders and their associates for the years ended December 31, 2015 and 2014 is as follows:

	2015	2014
Beginning balance	$ 1,242,736	$ 891,362
New loans or disbursements	253,423	502,863
Principal repayments	(441,408)	(151,489)
Ending balance	$ 1,054,751	$1,242,736

Deposits from principal officers, directors, and their affiliates at year end 2015 and 2014 were $815,489 and $1,362,924, respectively.

NOTE 14. STOCK-BASED COMPENSATION

The Bank has three share based compensation plans as described below. Total compensation cost that has been charged against income for those plans was $199,907 and $154,792 for 2015 and 2014, respectively. The total income tax benefit recorded to additional paid in capital was $13,216 and $166,012 for 2015 and 2014, respectively.

2003 Stock Option Plan: The Bank adopted a qualified stock option plan (the "Option Plan") for employees, non-employee directors and Bank founders, under which a maximum of 500,202 shares of Bank's common stock may be issued. The Option Plan calls for the exercise prices of the options to be equal to or greater than the fair market value of the stock at the time of grant. Options granted to Bank founders who are not also Bank directors or Bank officers were fully vested upon the date of grant. All other options shares granted have daily vesting over the first four years of the option contract. All option contracts for founders who are not also Bank directors or Bank officers have expiration dates of 10 years from the date of grant. All director and employee option contracts have expiration dates on the earlier of termination of service or 10 years from the date of grant. The Option Plan expired during 2014 and was replaced with the 2014 Omnibus Plan (the "Omnibus Plan").

All options granted under the Option Plan have a 10 year term and have been issued with exercise prices at the fair market value of the underlying shares at the date of grant. The non-qualified stock option awards to the organizers vested 100% immediately, whereas regular stock option awards to directors and employees vest over a four year period from the date the options were granted.

The Bank estimates the fair value of each option award as of the date of grant using a Black-Scholes-Merton option pricing formula and the following assumptions. Expected volatility is based on historical volatility of similar entities over a preceding period commensurate with the expected term of the option because the Bank's common stock has been publicly traded for a shorter period than the expected term for the options. The "simplified" method described in the Securities and Exchange Commission's Staff Accounting Bulletin No. 110 is used to determine the expected term of the options due to the lack of sufficient historical data. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant with substantially the same term as the expected term of the option. There were no options granted during the years ended 2015 and 2014.

The following is a summary of the activity relating to the Bank's stock option plan for the year ended December 31, 2015 as presented below:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Options outstanding at beginning of year	91,357	$14.89		
Granted	-	-		
Exercised	(13,398)	$14.00		
Forfeited or expired	(1,000)	$17.00		
Options outstanding at end of year	76,959	$15.02	5.57 years	$1,045,151
Options fully vested and expected to vest	75,504			$1,027,809
Exercisable at end of year	62,705	$14.66	5.15 years	$874,048

Information related to the stock option plan during the year follows:

		2015
Intrinsic value of options exercised	$	142,579
Cash received from option exercises		183,050
Tax benefit realized from option exercises		10,246
Weighted average fair value of options granted		-

As of December 31, 2015, there was $99,606 of total unrecognized compensation cost related to nonvested stock options granted under the plan. The cost is expected to be recognized over a weighted average period of 1.45 years.

2014 Omnibus Plan: The Bank adopted a new stock option plan (the "Omnibus Plan") for employees and non-employee directors, which will continue in effect until February 19, 2024. The maximum number of shares of common stock that may be issued under this plan is 427,246 unless amended by the Board or the shareholders of the Bank.

The Omnibus Plan permits the grant of stock options to directors and employees of the Bank. Options granted under the Omnibus Plan may be incentive stock options or non-statutory stock options, as determined by the plan administrator at the time of grant of an option, however incentive stock options may be granted only to employees. In addition, restricted stock awards may be granted under the Omnibus Plan to directors and employees.

The per share exercise price for the shares to be issued upon exercise of any option shall be such price as is determined by the plan administrator, but no less than 100 percent of the fair market value per share on the date of grant. All option contracts have expiration dates on the earlier of termination of service or 10 years from the date of grant.

The Bank estimates the fair value of each option award as of the date of grant using a Black-Scholes-Merton option pricing model and the following assumptions. Expected volatility is based on historical volatility of similar entities over a preceding period commensurate with the expected term of the option because the Bank's common stock is not actively traded. The "simplified" method described in the Securities and Exchange Commission's Staff Accounting Bulletin No. 110 is used to determine the expected term of the options due to the lack of sufficient historical data. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant with substantially the same term as the expected term of the option.

The following weighted average assumptions as of grant date used for 2015 and 2014 are as follows:

	2015	2014
Expected life (yrs.)	6.00	6.00
Volatility	43.47% - 46.48%	49.85% - 51.53%
Risk-free rate of return	1.37% - 1.63%	1.59% - 1.77%
Dividend yield	0.05%	0.05%

The following is a summary of the activity relating to the Bank's stock option plan for the year ended December 31, 2015 as presented below:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Options outstanding at beginning of year	22,000	$19.92		
Granted	15,200	$8.13		
Exercised	-	-		
Forfeited or expired	-	-		
Options outstanding at end of year	37,200	$15.10	8.97 years	$502,070
Options fully vested and expected to vest	34,457			$463,100
Exercisable at end of year	8,946	$20.25	8.61 years	$74,715

As of December 31, 2015, there was $360,504 of total unrecognized compensation cost related to non-vested stock options granted under the plan. The cost is expected to be recognized over a weighted average period of 2.81 years.

Restricted Stock Award Plan: The Bank adopted a non-qualified restricted stock award plan (the "Award Plan") for executive officers and non-employee directors under which the lesser of (i) 218,390 shares or (ii) the difference between 500,202 and the sum of the number of shares underlying stock options outstanding or granted after April 11, 2011 and the number of shares of Restricted Stock Awards granted that may be issued. Restricted Stock Awards vest at 25% per year on the anniversary date of the award over the first four years of the contract, except in the event of a qualifying Terminating Event.

The following is a summary of the activity relating to the Bank's restricted stock award plan as of December 31, 2015 as presented below:

	December 31, 2015	
Nonvested Shares	Shares	Weighted Average Grant Date Fair Value
Nonvested at January 1, 2015	2,500	$11.14
Granted	-	-
Vested	(2,500)	$11.14
Forfeited	-	-
Nonvested at December 31, 2015	-	$0.00

As of December 31, 2015, there was no unrecognized compensation cost related to nonvested shares granted under the plan. The total fair value of shares vested during the year ended December 31, 2015 was $27,862.

NOTE 15. REGULATORY CAPITAL MATTERS

REGULATORY CAPITAL: The Bank is subject to various regulatory capital adequacy requirements administered by the banking regulatory agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, would have a direct material effect on the Bank's financial statements. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. The net unrealized gain or loss on available for securities is included in computing regulatory capital. Capital amounts and ratios for December 31, 2014 are calculated using Basel I rules. Management believes as of December 31, 2015, the Bank meets all capital adequacy requirements to which they are subject.

Prompt corrective action regulations define five capital tiers for depository institutions: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At year end 2015 and 2014, the most recent regulatory notifications categorized the Bank as well-capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the institution's category.

Actual and required capital amounts and ratios are presented below at year end.

(Dollars in thousands)	Actual		For Capital Adequacy Purposes:		To Be Well Capitalized Under the FDICIA Prompt Corrective Action	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2015						
Total capital (to risk weighted assets)	$48,925	13.61%	$28,752	8.00%	$35,940	10.00%
Tier 1 capital (to risk weighted assets)	$44,396	12.35%	$21,564	6.00%	$28,752	8.00%
Common equity tier 1 (to risk weighted assets)	$44,396	12.35%	$16,173	4.50%	$23,361	6.50%
Tier 1 capital (to average assets) leverage ratio	$44,396	8.42%	$21,089	4.00%	$26,361	5.00%

(Dollars in thousands)	Actual		For Capital Adequacy Purposes:		Capitalized Under the FDICIA Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2014						
Total capital (to risk weighted assets)	$ 43,148	13.08%	$ 26,383	8.00%	$ 32,979	10.00%
Tier 1 capital (to risk weighted assets)	$ 38,996	11.82%	$ 13,192	4.00%	$ 19,787	6.00%
Tier 1 capital (to average assets) leverage ratio	$ 38,996	8.39%	$ 18,583	4.00%	$ 23,229	5.00%

DIVIDEND RESTRICTIONS: The Board of Directors may, to the extent of such earnings and the Bank's net capital requirements and subject to the provisions of the California Financial Code, declare and pay a portion of such earnings to its shareholders as dividends. No cash dividend will be declared without a complete analysis of capital impact, current economic assessment, and current risk analysis.

NOTE 16. LOAN COMMITMENTS AND OTHER DISCLOSURES

RESTRICTIONS ON CASH AND DUE FROM BANKS: Santa Cruz County Bank is subject to Federal Reserve Act Regulation D, which requires banks to maintain average reserve balances with the Federal Reserve Bank. Reserve requirements are offset by usable cash reserves. The Bank had no reserve requirement at December 31, 2015 and December 31, 2014.

At times, the Bank maintains deposit amounts at corresponding banks that exceed federally insured limits. The Bank has not experienced any losses on amounts exceeding the insured limits.

LOAN COMMITMENTS: The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit, overdraft protection and financial guarantees. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheets. The contract amounts of those instruments reflect the extent of involvement the Bank has in particular classes of financial instruments.

The Bank's exposure to credit loss in the event of nonperformance by the other party for commitments to extend credit, standby letters of credit, and financial guarantees is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's credit worthiness 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. Collateral held varies but may include cash, securities, accounts receivable, inventory, property, plant and equipment, residential real estate and income-producing commercial properties.

Standby letters of credit and financial guarantees written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

Financial instruments whose contract amounts represent credit risk at December 31, 2015 and December 31, 2014 are as follows:

	December 31,	
	2015	2014
Commitments to extend credit	$ 95,893,559	$ 89,081,921
Standby letters of credit	1,033,366	1,618,262
	$ 96,926,925	$ 90,700,183

NOTE 17. EARNINGS PER SHARE

EARNINGS PER SHARE: A reconciliation of the numerators and denominators of the basic and diluted earnings per share computation is as follows:

	Net Income	Weighted Average Number of Shares	Per Share Amount
December 31, 2015			
Basic earnings per share	$ 5,433,780	2,148,648	$ 2.53
Effect of dilutive stock based compensation	-	30,274	
Diluted earnings per share	$ 5,433,780	2,178,922	$ 2.49
December 31, 2014			
Basic earnings per share	$ 4,371,187	2,128,437	$ 2.05
Effect of dilutive stock based compensation	-	31,547	
Diluted earnings per share	$ 4,371,187	2,159,984	$ 2.02

Stock options for 38,200 shares and 39,000 shares of common stock were not considered in computing diluted earnings per common share for the years ended December 31, 2015 and 2014, respectively, because they were anti-dilutive.

BOARD OF DIRECTORS

George R. Gallucci
(Chairman)
Retired Banker &
Registered Investment Advisor

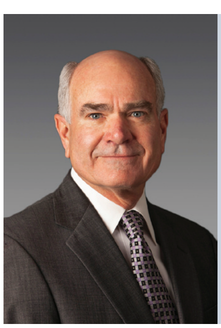
Harvey J. Nickelson
Retired Bank CEO &
Community Volunteer

William J. Hansen
(Vice-Chairman)
President & CEO
Hansen Insurance Co.

Tila Bañuelos
President & CEO
Mas Mac Inc.
McDonald's Restaurants

Thomas N. Griffin
Director & President
Grunsky, Ebey, Farrar & Howell

Kenneth R. Chappell
CPA, Partner-in-Charge
Hutchinson & Bloodgood, LLP



David V. Heald
President & CEO
Santa Cruz County Bank

BANK FOUNDERS

A group of local business people joined to create a local, community bank focused on serving the residents and businesses of Santa Cruz County when it became apparent that the last of the local independent banks was soon to be taken over by a large out-of-area bank holding company. This group that we recognize as Founders all contributed time, money, and talent, not only to the Bank's organizing effort, but continue to be involved and support our Bank as customers, referring family, friends and business contacts to us, and serving as ambassadors of the Bank in our community.

The Bank's Founders are listed below:

Richard Alderson
*Joseph Anzalone****
*Tila Bañuelos**
Victor Bogard
Anthony & Rebecca Campos
Charles Canfield
*Kenneth R. Chappell**
Kate & Fred Chen
Marshall Delk
*George R. Gallucci**
*Thomas N. Griffin**
*William J. Hansen**
*David V. Heald**
Mark Holcomb
*Steven G. John***
Mateo Lettunich
Robert Lockwood
William Moncovich
Stuart Mumm
George Ow, Jr.
Louis Rittenhouse
Frank Saveria
*Robert*** & Bjorg Yonts*

**denotes Bank Director **denotes former Bank Director ***denotes deceased*

SANTA CRUZ COUNTY BANK MANAGEMENT TEAM

David V. Heald, President and Chief Executive Officer

Frederick L. Caiocca, Executive Vice President and Regional Credit Manager

Victor F. Davis, Senior Vice President, Chief Financial Officer and Cashier

Angelo DeBernardo, Jr., Senior Vice President, Chief Lending Officer

George T. Harrison, Senior Vice President, Chief Credit Officer

Heather La Fontaine, Senior Vice President, Chief Administrative Officer

Jaime Manriquez, Senior Vice President, Chief Information Officer & Chief Information Security Officer

Mary Anne Carson, Senior Vice President, Director of Marketing and Community Relations

Susan Chandler, Senior Vice President, SBA Department Manager

Tracy Ruelas-Hashimoto, Senior Vice President, Controller

Janice Zappa, Senior Vice President, Corporate Secretary

IN MEMORIAM

We dedicate this annual report in memory of two of our Bank Founders, Joseph Anzalone and Robert Yonts. These original Founders made an early commitment to support the concept of establishing a new local bank for our community. They will never be forgotten.

BANKING LOCATIONS

APTOS 7775 Soquel Dr. 831.662.6000
CAPITOLA 819 Bay Ave. 831.464.5300
SANTA CRUZ 720 Front St. 831.457.5000
SCOTTS VALLEY 4604 Scotts Valley Dr. 831.461.5000
WATSONVILLE 595 Auto Center Dr. 831.761.7600

ADDITIONAL ATM & NIGHT DEPOSITORY LOCATIONS

DOMINICAN HOSPITAL 1555 Soquel Dr., Santa Cruz
DELUXE FOODS 783-25 Rio Del Mar Blvd., Aptos

SANTA CRUZ COUNTY BANK

www.sccountybank.com