



RIVER VALLEY
COMMUNITY BANCORP

Yuba City, California

CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2020 and 2019

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INDEPENDENT AUDITOR'S REPORT

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

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of River Valley Community Bancorp, which comprise the consolidated balance sheets as of December 31, 2020 and 2019, and the related consolidated statements of comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of River Valley Community Bancorp as of December 31, 2020 and 2019, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Crowe LLP
Crowe LLP

Sacramento, California
March 16, 2021

River Valley Community Bancorp
Consolidated Balance Sheets
December 31, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Assets		
Cash and noninterest bearing due from banks	\$ 5,166,671	\$ 4,991,107
Interest bearing deposits in banks	47,800,372	43,364,723
Total cash and cash equivalents	<u>52,967,043</u>	<u>48,355,830</u>
Time deposits in banks	1,240,000	2,481,000
Investment securities available-for-sale	168,938,779	174,755,266
Loans:		
Real estate:		
Construction and development	12,573,700	17,242,760
Agriculture	13,279,898	11,668,876
1-4 family residential	18,573,069	17,250,292
Multifamily	18,926,985	14,526,434
Commercial	121,510,979	111,173,068
Agriculture production	2,679,716	5,554,434
Commercial and industrial	71,521,931	25,750,117
Consumer	100,659	189,083
Total loans, gross	<u>259,166,937</u>	<u>203,355,064</u>
Deferred loan fees, net	(1,426,553)	(297,853)
Allowance for loan losses	(3,469,736)	(2,545,704)
Total loans, net	<u>254,270,648</u>	<u>200,511,507</u>
Premises and equipment, net	7,181,641	5,071,399
Cash surrender value of life insurance	6,070,935	5,929,888
Accrued interest receivable and other assets	5,817,474	5,204,792
Total assets	<u>\$ 496,486,520</u>	<u>\$ 442,309,682</u>
Liabilities and Shareholders' Equity		
Liabilities:		
Demand deposits - noninterest bearing	\$ 199,745,571	\$ 127,771,668
Demand deposits - interest bearing	68,631,212	38,335,933
Money market and savings deposits	149,450,145	112,261,493
Time deposits - under \$250,000	14,500,103	15,580,741
Time deposits - \$250,000 or more	12,835,038	43,178,873
Total deposits	<u>445,162,069</u>	<u>337,128,708</u>
Federal Home Loan Bank borrowings	-	65,000,000
Accrued interest payable and other liabilities	4,542,894	2,383,582
Total liabilities	<u>449,704,963</u>	<u>404,512,290</u>
Shareholders' equity:		
Preferred stock – no par value; 5,000,000 shares authorized; no shares outstanding	-	-
Common stock – no par value; 50,000,000 shares authorized; 2,387,345 and 2,369,583 shares issued and outstanding in 2020 and 2019, respectively	16,223,734	16,013,906
Retained earnings	23,674,508	19,545,411
Accumulated other comprehensive income	6,883,315	2,238,075
Total shareholders' equity	<u>46,781,557</u>	<u>37,797,392</u>
Total liabilities and shareholders' equity	<u>\$ 496,486,520</u>	<u>\$ 442,309,682</u>

See accompanying notes to consolidated financial statements.

River Valley Community Bancorp
Consolidated Statements of Comprehensive Income
Years Ended December 31, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Interest income:		
Interest and fees on loans	\$ 11,445,662	\$ 9,768,476
Interest on taxable investment securities	3,282,935	4,117,559
Interest on investment securities exempt from Federal taxes	829,718	744,900
Interest on deposits in banks and other	383,702	929,754
Total interest income	<u>15,942,017</u>	<u>15,560,689</u>
Interest expense:		
Interest on demand deposits	53,834	41,179
Interest on money market and savings deposits	456,140	571,370
Interest on time deposits	515,731	769,207
Interest on Federal Home Loan Bank borrowings	749,121	1,822,028
Total interest expense	<u>1,774,826</u>	<u>3,203,784</u>
Net interest income	14,167,191	12,356,905
Provision for loan losses	1,000,000	385,000
Net interest income after provision for loan losses	<u>13,167,191</u>	<u>11,971,905</u>
Noninterest income:		
Service charges and fees	404,857	394,510
Earnings on cash surrender value of life insurance	141,047	137,218
Gain on sale of investment securities, net	2,463,598	693,006
Other	250,494	72,105
Total noninterest income	<u>3,259,996</u>	<u>1,296,839</u>
Noninterest expense:		
Salaries and employee benefits	5,035,829	4,501,847
Data processing and information technology	917,383	871,449
Occupancy and equipment	830,783	666,304
Directors' expense	293,241	284,579
Insurance and assessments	280,524	157,097
Professional fees	238,313	189,778
Debt extinguishment	2,329,628	-
Other	888,487	915,807
Total noninterest expense	<u>10,814,188</u>	<u>7,586,861</u>
Income before income tax expense	5,612,999	5,681,883
Income tax expense	1,483,902	1,522,809
Net income	<u>\$ 4,129,097</u>	<u>\$ 4,159,074</u>
Earnings per share - basic	<u>\$ 1.74</u>	<u>\$ 1.75</u>
Earnings per share - diluted	<u>\$ 1.69</u>	<u>\$ 1.68</u>
Comprehensive income:		
Net income	\$ 4,129,097	\$ 4,159,074
Other comprehensive income:		
Investment securities available-for-sale:		
Unrealized gains arising during the year	9,058,203	6,335,381
Reclassification adjustments for net gains in earnings	(2,463,598)	(693,006)
Income tax expense	<u>(1,949,365)</u>	<u>(1,667,886)</u>
Total other comprehensive income	<u>4,645,240</u>	<u>3,974,489</u>
Total comprehensive income	<u>\$ 8,774,337</u>	<u>\$ 8,133,563</u>

See accompanying notes to consolidated financial statements.

River Valley Community Bancorp
Consolidated Statements of Changes in Shareholders' Equity
Years Ended December 31, 2020 and 2019

	Common Stock		Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	Shares	Amount			
Balance, January 1, 2019	2,384,189	\$ 16,285,739	\$ 15,386,337	\$ (1,736,414)	\$ 29,935,662
Net income	-	-	4,159,074	-	4,159,074
Other comprehensive income	-	-	-	3,974,489	3,974,489
Stock compensation expense	-	217,126	-	-	217,126
Stock options exercised	12,713	136,408	-	-	136,408
Restricted stock units vested	3,617	-	-	-	-
Stock repurchases	(30,936)	(625,367)	-	-	(625,367)
Balance, December 31, 2019	<u>2,369,583</u>	<u>16,013,906</u>	<u>19,545,411</u>	<u>2,238,075</u>	<u>37,797,392</u>
Net income	-	-	4,129,097	-	4,129,097
Other comprehensive income	-	-	-	4,645,240	4,645,240
Stock compensation expense	-	177,830	-	-	177,830
Stock options exercised	32,062	318,196	-	-	318,196
Restricted stock units vested	700	-	-	-	-
Stock repurchases	(15,000)	(286,198)	-	-	(286,198)
Balance, December 31, 2020	<u>2,387,345</u>	<u>\$ 16,223,734</u>	<u>\$ 23,674,508</u>	<u>\$ 6,883,315</u>	<u>\$ 46,781,557</u>

See accompanying notes to consolidated financial statements.

River Valley Community Bancorp
Consolidated Statements of Cash Flows
Years Ended December 31, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Cash flows from operating activities:		
Net income	\$ 4,129,097	\$ 4,159,074
Adjustments to reconcile net income to net cash from operating activities:		
Provision for loan losses	1,000,000	385,000
Depreciation, amortization, and accretion, net	1,008,926	1,156,505
Earnings on cash surrender value of life insurance	(141,047)	(137,218)
Gain on sale of investment securities, net	(2,463,598)	(693,006)
Loss on disposal of premises and equipment	9,855	14,938
Change in deferred loan fees, net	1,128,700	109,134
Deferred income tax expense (benefit)	(344,085)	19,602
Stock compensation expense	177,830	217,126
Change in accrued interest receivable and other assets	(2,217,962)	102,142
Change in accrued interest payable and other liabilities	2,159,312	3,307
Net cash from operating activities	<u>4,447,028</u>	<u>5,336,604</u>
Cash flows from investing activities:		
Maturities of time deposits in banks	1,241,000	1,984,000
Investment securities available-for-sale:		
Purchases	(16,696,290)	(110,759,321)
Maturities and calls	2,499,882	7,800,000
Principal payments	7,271,113	8,944,846
Sales	21,129,059	83,195,957
Change in loans, net	(55,887,841)	(34,417,261)
Purchases of premises and equipment	(2,458,097)	(208,444)
Net cash from investing activities	<u>(42,901,174)</u>	<u>(43,460,223)</u>
Cash flows from financing activities:		
Change in non-time deposits, net	139,457,834	9,575,739
Change in time deposits, net	(31,424,473)	41,779,383
Change in Federal Home Loan Bank borrowings, net	(65,000,000)	5,000,000
Stock repurchases	(286,198)	(625,367)
Stock options exercised	318,196	136,408
Net cash from financing activities	<u>43,065,359</u>	<u>55,866,163</u>
Change in cash and cash equivalents	4,611,213	17,742,544
Cash and cash equivalents, beginning of year	48,355,830	30,613,286
Cash and cash equivalents, end of year	<u>\$ 52,967,043</u>	<u>\$ 48,355,830</u>
Supplemental cash flow disclosures:		
Supplemental disclosure of non-cash activities:		
Right of use asset acquired in exchange for an operating lease liability	\$ -	\$ 1,103,070
Supplemental disclosure of cash flow activities:		
Interest paid	\$ 2,021,934	\$ 2,979,764
Income taxes paid	1,670,000	930,000

See accompanying notes to consolidated financial statements.

Note 1. Summary of Significant Accounting Policies

General – On February 9, 2017, River Valley Community Bancorp (the “Bancorp”) was formed as a California corporation and subsequently became the sole shareholder of River Valley Community Bank (the “Bank”). The Bancorp and the Bank are collectively referred to as the “Company”, and they share a common board of directors and certain executive officers. The Bank was approved as a state-chartered, non-member bank on December 27, 2005 and is subject to regulation by the California Department of Business Oversight (the “DBO”) and the Federal Deposit Insurance Corporation (the “FDIC”). The Bank’s deposits are insured by the FDIC up to applicable legal limits. The Company is headquartered in Yuba City, California with branches in Yuba City, Grass Valley, Auburn, and Marysville, California and provides products and services primarily to small to middle-market businesses and professionals located in Sutter, Yuba, Nevada, Placer, and surrounding counties.

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

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

The global pandemic resulting from the outbreak of the coronavirus (COVID-19) has substantially and negatively impacted the United States economy, created significant volatility and disruption in financial markets, and materially increased unemployment levels. In addition, the pandemic has resulted in temporary closures of businesses and the institution of social distancing and sheltering in place requirements in most states and communities. The Company has and could continue to experience adverse effects from the COVID-19 pandemic. Information which was available to the Company at the date of the financial statements may change in the near term due to the COVID-19 pandemic, and the effect of the change could be material to the financial statements. The extent to which the COVID-19 pandemic will impact the Company’s estimates and assumptions is highly uncertain.

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

Time deposits in banks – Time deposits in banks have original maturities exceeding ninety days, have remaining maturities through June 2023, and are carried at cost. Time deposits in banks are fully insured.

Investment securities – Investment securities are classified as available-for-sale and are reported at fair value, with unrealized gains and losses excluded from earnings and reported, net of taxes, as accumulated other comprehensive income. Gains or losses on the sale of investment securities are computed on the specific identification method at the trade date. Interest earned on investment securities is reported in interest income, net of applicable adjustments for accretion of discounts and amortization of premiums.

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

Note 1. Summary of Significant Accounting Policies (continued)

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

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

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

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

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

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

Note 1. Summary of Significant Accounting Policies (continued)

Allowance for loan losses (continued)

The Company 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 Company and 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 Company's credit position at some future date. Special Mention loans are not adversely classified and do not expose the Company to sufficient risk to warrant adverse classification.

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

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

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

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

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

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

Note 1. Summary of Significant Accounting Policies (continued)

Allowance for loan losses (continued)

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

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

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

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

Premises and equipment – Land is carried at cost. Premises and equipment are carried at cost, less accumulated depreciation. Depreciation is determined using the straight-line method over the estimated useful lives of the related assets. The useful lives of premises are estimated to be 15 to 39 years. The useful lives of furniture, fixtures, and equipment are estimated to be 3 to 10 years. When assets are sold or otherwise disposed of, the cost and related accumulated depreciation or amortization are removed from the accounts, and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is charged to expense as incurred. The Company evaluates premises and equipment for financial impairment, as events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable.

Leases – The Company enters into leases in the normal course of business. The Company includes lease extension and termination options in the lease term if, after considering relevant economic factors, it is reasonably certain the Company will exercise the option. The Company has elected to account for any non-lease components in its real estate leases as part of the associated lease component. The Company has also elected not to recognize leases with original lease terms of 12 months or less (short-term leases) on the consolidated balance sheet. Leases are classified as operating or finance leases at the lease commencement date. Lease expense for operating leases and short-term leases is recognized on a straight-line basis over the lease term. Right of use assets represent the Company's right to use an underlying asset for the lease term and are included in accrued interest receivable and other assets on the consolidated balance sheet. Lease liabilities represent the Company's obligation to make lease payments arising from the lease and are included in accrued interest payable and other liabilities on the consolidated balance sheet. Right of use assets and lease liabilities are recognized at the lease commencement date based on the estimated present value of lease payments over the lease term, discounted using the Company's incremental borrowing rate.

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

Note 1. Summary of Significant Accounting Policies (continued)

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

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

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

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

Earnings per share – Basic earnings per share (EPS), which excludes dilution, is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock, such as stock options, result in the issuance of common stock, which shares in the earnings of the Company. The treasury stock method is applied to determine the dilutive effect of stock options in computing diluted earnings per share. Earnings per share are retroactively restated for stock dividends and stock splits through the date of issuance of the financial statements.

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

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

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

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

Note 1. Summary of Significant Accounting Policies (continued)

Fair value measurements – Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

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

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

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

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

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

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

Investment securities – Fair values for investment securities are calculated based on market prices of similar securities, using matrix pricing, resulting in a Level 2 classification. Matrix pricing is a mathematical technique commonly used to price debt securities that are not actively traded and values debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities.

Loans – The fair value disclosed for loans is determined using the exit price notion. The Company uses a net present value of cash flows methodology that seeks to incorporate interest rate, credit, liquidity, and prepayment risks in the fair value estimation. Inputs to the calculation include market rates for similarly offered products, market interest rate projections, estimated credit losses, and prepayment assumptions, resulting in a Level 3 classification.

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

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

FHLB borrowings – The carrying amounts of FHLB borrowings, generally maturing within 90 days, approximate fair values, resulting in a Level 2 classification.

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

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

Note 1. Summary of Significant Accounting Policies (continued)

Subsequent events – Management reviewed all events occurring from December 31, 2020 through March 16, 2021, the date the financial statements were available to be issued.

Adoption of New Accounting Standard – On January 1, 2019, the Company adopted Accounting Standards Update (ASU) 2016-02 *Leases* and all subsequent amendments to the ASU (collectively referred to as “ASC 842”), which requires the Company to recognize leases on the balance sheet. The standard was adopted under a modified retrospective approach as of the date of adoption, and the Company elected several of the available practical expedients, including (1) carryover of historical lease determination and lease classification conclusions, (2) carryover of historical initial direct cost balances for existing leases, and (3) accounting for lease and non-lease components in contracts in which the Company is a lessee as a single lease component. Adoption of the leasing standard resulted in the recognition of an operating right of use asset totaling \$1,103,070 and an operating lease liability totaling \$1,107,487 as of January 1, 2019. There was no material impact to the timing of expense or income recognition in the Company’s consolidated statements of comprehensive income. Prior periods were not restated.

Note 2. Investment Securities Available-for-Sale

The amortized cost and estimated fair value of investment securities available-for-sale as of December 31, 2020 and 2019 are as follows:

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Estimated Fair Value</u>
December 31, 2020:				
Obligations of states and political subdivisions	\$ 37,483,317	\$ 3,656,623	\$ -	\$ 41,139,940
U.S. Government sponsored agencies collateralized by mortgage obligations	51,387,429	5,233,264	-	56,620,693
U.S. Government sponsored agencies mortgage-backed securities	11,146,580	828,586	-	11,975,166
Corporate debt securities	30,855,464	351,418	(207,752)	30,999,130
Student loan backed securities	28,294,106	30,628	(120,884)	28,203,850
Total	<u>\$ 159,166,896</u>	<u>\$ 10,100,519</u>	<u>\$ (328,636)</u>	<u>\$ 168,938,779</u>
December 31, 2019:				
Obligations of states and political subdivisions	\$ 24,201,899	\$ 956,485	\$ (131,004)	\$ 25,027,380
U.S. Government sponsored agencies collateralized by mortgage obligations	64,031,718	1,783,510	(282,077)	65,533,151
U.S. Government sponsored agencies mortgage-backed securities	12,509,733	276,701	(65,796)	12,720,638
Corporate debt securities	42,409,962	1,194,676	(158,515)	43,446,123
Student loan backed securities	28,424,676	-	(396,702)	28,027,974
Total	<u>\$ 171,577,988</u>	<u>\$ 4,211,372</u>	<u>\$ (1,034,094)</u>	<u>\$ 174,755,266</u>

River Valley Community Bancorp
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December 31, 2020 and 2019

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

The following table summarizes securities with unrealized losses as of December 31, 2020 and 2019, aggregated by major security type and length of time in a continuous unrealized loss position:

	Less Than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
December 31, 2020:						
Obligations of states and political subdivisions	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
U.S. Government sponsored agencies collateralized by mortgage obligations	-	-	-	-	-	-
U.S. Government sponsored agencies mortgage-backed securities	-	-	-	-	-	-
Corporate debt securities	-	-	2,162,825	(207,752)	2,162,825	(207,752)
Student loan backed securities	-	-	17,022,881	(120,884)	17,022,881	(120,884)
Total	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 19,185,706</u>	<u>\$ (328,636)</u>	<u>\$ 19,185,706</u>	<u>\$ (328,636)</u>
December 31, 2019:						
Obligations of states and political subdivisions	7,200,121	(131,004)	-	-	7,200,121	(131,004)
U.S. Government sponsored agencies collateralized by mortgage obligations	18,996,346	(282,077)	-	-	18,996,346	(282,077)
U.S. Government sponsored agencies mortgage-backed securities	2,056,660	(44,822)	2,483,887	(20,974)	4,540,547	(65,796)
Corporate debt securities	-	-	3,205,849	(158,515)	3,205,849	(158,515)
Student loan backed securities	28,027,974	(396,702)	-	-	28,027,974	(396,702)
Total	<u>\$ 56,281,101</u>	<u>\$ (854,605)</u>	<u>\$ 5,689,736</u>	<u>\$ (179,489)</u>	<u>\$ 61,970,837</u>	<u>\$ (1,034,094)</u>

As of December 31, 2020, the Company's security portfolio consisted of 15 securities that were in an unrealized loss position, all of which had been in a loss position for greater than 12 months. Unrealized losses for all securities have not been recognized into income because the issuers' bonds are of high credit quality (investment grade or higher), management does not intend to sell and it is likely that management will not be required to sell the securities prior to their anticipated recovery, and the decline in fair value is largely due to changes in interest rates and other market conditions. The fair value is expected to recover as the bonds approach maturity.

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

The amortized cost and estimated fair value of available-for-sale investment securities as of December 31, 2020 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because the issuers of the securities may have the right to call or prepay obligations with or without call or prepayment penalties.

	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>
Within one year	\$ 3,002,554	\$ 3,006,540
After one year through five years	20,391,696	20,634,392
After five years through ten years	12,981,862	13,362,280
After ten years	<u>31,962,669</u>	<u>35,135,858</u>
	68,338,781	72,139,070
Investment securities not due at a single maturity date:		
U.S. Government sponsored agencies collateralized by mortgage obligations and mortgage-backed securities	62,534,009	68,595,859
Student loan backed securities	<u>28,294,106</u>	<u>28,203,850</u>
Total	<u>\$ 159,166,896</u>	<u>\$ 168,938,779</u>

Note 3. Loans and the Allowance for Loan Losses

The Company participated in the SBA Paycheck Protection Program (PPP), which consisted of federally guaranteed loans intended to provide liquidity to small businesses to pay employees, rent, mortgage interest, and utilities. The loans may be forgiven upon certain conditions being met, including the business providing payroll documentation evidencing compliance with the program. The Company began accepting PPP applications in April 2020 and originated approximately \$56,422,000 of PPP loans and collected approximately \$2,163,000 of related processing fees from the SBA during the year ended December 31, 2020. Processing fees were deferred and are being recognized as income over the original contractual life of the loan. Upon forgiveness, any remaining deferred processing fee is immediately recognized as income. During the year ended December 31, 2020, approximately \$11,143,000 of PPP loans were forgiven or paid in full and approximately \$1,021,000 of processing fees were recognized as interest and fees on loans in the consolidated statement of comprehensive income. As of December 31, 2020, the Company had approximately \$45,279,000 of PPP loans outstanding with related deferred processing fees of approximately \$1,142,000. PPP loans are included in the commercial and industrial loan class.

River Valley Community Bancorp
Notes to Consolidated Financial Statements
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Note 3. Loans and the Allowance for Loan Losses (continued)

The recorded investment in loans excludes accrued interest receivable and deferred loan fees, net due to their immaterial balances. The following tables present the activity in the allowance for loan losses by class for the years ended December 31, 2020 and 2019 and the recorded investments in loans and ending balance in the allowance for loan losses by class as of December 31, 2020 and 2019:

	Real Estate					Agriculture Production	Commercial & Indust.	Consumer	Total
	Construct. & Develop	Agriculture	1-4 Family Resident	Multifamily	Commercial				
December 31, 2020:									
<i>Allowance for Loan Losses:</i>									
Balance, beginning of year	\$ 352,467	\$ 110,208	\$ 103,258	\$ 86,379	\$ 1,192,430	\$ 46,665	\$ 653,305	\$ 992	\$ 2,545,704
Provision for loan losses	(23,882)	16,403	27,372	46,261	727,832	(21,544)	227,545	13	1,000,000
Loans charged off	-	-	-	-	-	-	(75,968)	-	(75,968)
Loans recovered	-	-	-	-	-	-	-	-	-
Total	<u>\$ 328,585</u>	<u>\$ 126,611</u>	<u>\$ 130,630</u>	<u>\$ 132,640</u>	<u>\$ 1,920,262</u>	<u>\$ 25,121</u>	<u>\$ 804,882</u>	<u>\$ 1,005</u>	<u>\$ 3,469,736</u>
December 31, 2019:									
<i>Allowance for Loan Losses:</i>									
Balance, beginning of year	\$ 110,637	\$ 57,996	\$ 108,015	\$ 102,188	\$ 1,054,715	\$ 55,783	\$ 648,287	\$ 1,379	\$ 2,139,000
Provision for loan losses	241,830	52,212	(4,757)	(15,809)	137,715	(9,118)	(17,660)	587	385,000
Loans charged off	-	-	-	-	-	-	-	(974)	(974)
Loans recovered	-	-	-	-	-	-	22,678	-	22,678
Total	<u>\$ 352,467</u>	<u>\$ 110,208</u>	<u>\$ 103,258</u>	<u>\$ 86,379</u>	<u>\$ 1,192,430</u>	<u>\$ 46,665</u>	<u>\$ 653,305</u>	<u>\$ 992</u>	<u>\$ 2,545,704</u>
December 31, 2020:									
<i>Loans:</i>									
Individually evaluated for impairment	\$ 235,124	\$ -	\$ -	\$ -	\$ 1,968,257	\$ -	\$ -	\$ -	\$ 2,203,381
Collectively evaluated for impairment	12,338,576	13,279,898	18,573,069	18,926,985	119,542,722	2,679,716	71,521,931	100,659	256,963,556
Total	<u>\$12,573,700</u>	<u>\$13,279,898</u>	<u>\$18,573,069</u>	<u>\$18,926,985</u>	<u>\$ 121,510,979</u>	<u>\$ 2,679,716</u>	<u>\$71,521,931</u>	<u>\$ 100,659</u>	<u>\$ 259,166,937</u>
<i>Allowance for Loan Losses:</i>									
Related to loans individually evaluated for impairment	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Related to loans collectively evaluated for impairment	328,585	126,611	130,630	132,640	1,920,262	25,121	804,882	1,005	3,469,736
Total	<u>\$ 328,585</u>	<u>\$ 126,611</u>	<u>\$ 130,630</u>	<u>\$ 132,640</u>	<u>\$ 1,920,262</u>	<u>\$ 25,121</u>	<u>\$ 804,882</u>	<u>\$ 1,005</u>	<u>\$ 3,469,736</u>

River Valley Community Bancorp
Notes to Consolidated Financial Statements
December 31, 2020 and 2019

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

	Real Estate					Agriculture Production	Commercial & Indust.	Consumer	Total
	Construct. & Develop	Agriculture	1-4 Family Resident	Multifamily	Commercial				
December 31, 2019:									
<i>Loans:</i>									
Individually evaluated for impairment	\$ -	\$ -	\$ -	\$ -	\$ 2,026,572	\$ -	\$ -	\$ -	\$ 2,026,572
Collectively evaluated for impairment	17,242,760	11,668,876	17,250,292	14,526,434	109,146,496	5,554,434	25,750,117	189,083	201,328,492
Total	<u>\$17,242,760</u>	<u>\$11,668,876</u>	<u>\$17,250,292</u>	<u>\$14,526,434</u>	<u>\$ 111,173,068</u>	<u>\$ 5,554,434</u>	<u>\$25,750,117</u>	<u>\$ 189,083</u>	<u>\$ 203,355,064</u>
<i>Allowance for Loan Losses:</i>									
Related to loans individually evaluated for impairment	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Related to loans collectively evaluated for impairment	352,467	110,208	103,258	86,379	1,192,430	46,665	653,305	992	2,545,704
Total	<u>\$ 352,467</u>	<u>\$ 110,208</u>	<u>\$ 103,258</u>	<u>\$ 86,379</u>	<u>\$ 1,192,430</u>	<u>\$ 46,665</u>	<u>\$ 653,305</u>	<u>\$ 992</u>	<u>\$ 2,545,704</u>

The following table presents the loan portfolio by class allocated by management's internal risk ratings as of December 31, 2020 and 2019:

	Real Estate					Agriculture Production	Commercial & Indust.	Consumer	Total
	Construct. & Develop	Agriculture	1-4 Family Resident	Multifamily	Commercial				
December 31, 2020:									
Pass	\$12,338,576	\$12,990,085	\$18,573,069	\$18,926,985	\$ 113,929,890	\$ 2,679,716	\$70,444,436	\$ 100,659	\$ 249,983,416
Special mention	-	-	-	-	-	-	240,996	-	240,996
Substandard	235,124	289,813	-	-	7,581,089	-	836,499	-	8,942,525
Total	<u>\$12,573,700</u>	<u>\$13,279,898</u>	<u>\$18,573,069</u>	<u>\$18,926,985</u>	<u>\$ 121,510,979</u>	<u>\$ 2,679,716</u>	<u>\$71,521,931</u>	<u>\$ 100,659</u>	<u>\$ 259,166,937</u>
December 31, 2019:									
Pass	\$17,242,760	\$11,260,275	\$17,250,292	\$14,526,434	\$ 102,528,093	\$ 5,554,434	\$24,644,307	\$ 189,083	\$ 193,195,678
Special mention	-	-	-	-	925,445	-	1,105,810	-	2,031,255
Substandard	-	408,601	-	-	7,719,530	-	-	-	8,128,131
Total	<u>\$17,242,760</u>	<u>\$11,668,876</u>	<u>\$17,250,292</u>	<u>\$14,526,434</u>	<u>\$ 111,173,068</u>	<u>\$ 5,554,434</u>	<u>\$25,750,117</u>	<u>\$ 189,083</u>	<u>\$ 203,355,064</u>

River Valley Community Bancorp
Notes to Consolidated Financial Statements
December 31, 2020 and 2019

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

The following table presents the loan portfolio by class allocated by the number of days past due and interest accrual status as of December 31, 2020 and 2019:

	Real Estate					Agriculture Production	Commercial & Indust.	Consumer	Total
	Construct. & Develop	Agriculture	1-4 Family Resident	Multifamily	Commercial				
December 31, 2020:									
Accruing interest:									
Current	\$ 12,338,576	\$ 13,279,898	\$ 18,573,069	\$ 18,926,985	\$ 121,510,979	\$ 2,679,716	\$ 71,521,931	\$ 100,659	\$ 258,931,813
30 to 59 days past due	-	-	-	-	-	-	-	-	-
60 to 89 days past due	-	-	-	-	-	-	-	-	-
90 days or more past due	-	-	-	-	-	-	-	-	-
Not accruing interest	235,124	-	-	-	-	-	-	-	235,124
Total	<u>\$ 12,573,700</u>	<u>\$ 13,279,898</u>	<u>\$ 18,573,069</u>	<u>\$ 18,926,985</u>	<u>\$ 121,510,979</u>	<u>\$ 2,679,716</u>	<u>\$ 71,521,931</u>	<u>\$ 100,659</u>	<u>\$ 259,166,937</u>
December 31, 2019:									
Accruing interest:									
Current	\$ 17,242,760	\$ 11,668,876	\$ 17,250,292	\$ 14,526,434	\$ 111,173,068	\$ 5,329,434	\$ 24,023,545	\$ 189,083	\$ 201,403,492
30 to 59 days past due	-	-	-	-	-	-	1,726,572	-	1,726,572
60 to 89 days past due	-	-	-	-	-	225,000	-	-	225,000
90 days or more past due	-	-	-	-	-	-	-	-	-
Not accruing interest	-	-	-	-	-	-	-	-	-
Total	<u>\$ 17,242,760</u>	<u>\$ 11,668,876</u>	<u>\$ 17,250,292</u>	<u>\$ 14,526,434</u>	<u>\$ 111,173,068</u>	<u>\$ 5,554,434</u>	<u>\$ 25,750,117</u>	<u>\$ 189,083</u>	<u>\$ 203,355,064</u>

River Valley Community Bancorp
Notes to Consolidated Financial Statements
December 31, 2020 and 2019

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

The following table presents balances related to impaired loans by class as of and for the years ended December 31, 2020 and 2019:

	Real Estate					Agriculture Production	Commercial & Indust.	Consumer	Total
	Construct. & Develop	Agriculture	1-4 Family Resident	Multifamily	Commercial				
December 31, 2020:									
Unpaid principal balance	235,124	\$ -	\$ -	\$ -	\$ 1,968,257	\$ -	\$ -	\$ -	\$ 2,203,381
Recorded investment:									
Without allowance	235,124	-	-	-	1,968,257	-	-	-	2,203,381
With allowance	-	-	-	-	-	-	-	-	-
Related allowance	-	-	-	-	-	-	-	-	-
Average recorded invest	141,074	-	-	-	2,001,579	-	9,868	-	2,152,521
Interest income recognized	13,583	-	-	-	113,417	-	-	-	127,000
December 31, 2019:									
Unpaid principal balance	\$ -	\$ -	\$ -	\$ -	\$ 2,026,572	\$ -	\$ -	\$ -	\$ 2,026,572
Recorded investment:									
Without allowance	-	-	-	-	2,026,572	-	-	-	2,026,572
With allowance	-	-	-	-	-	-	-	-	-
Related allowance	-	-	-	-	-	-	-	-	-
Average recorded invest	-	-	-	-	810,924	-	-	-	810,924
Interest income recognized	-	-	-	-	119,423	-	-	-	119,423

No specific reserves were allocated to customers whose loan terms have been modified in TDRs as of December 31, 2020 and 2019. The Company has not committed to lend additional amounts as of December 31, 2020 and 2019 to customers with outstanding loans that are classified as TDRs. During the year ended December 31, 2020, there were no modifications that were determined to be TDRs. During the year ended December 31, 2019, the Company modified the terms of one real estate – commercial loan with a recorded investment of \$300,000 at the time of restructuring, which was determined to be a TDR due to a reduction of the interest rate and extension of the maturity for a borrower suffering from financial difficulty. This TDR has been classified as an impaired loan with no specific reserve as of December 31, 2020 and 2019. During the years ended December 31, 2020 and 2019, there were no defaults on loans previously classified as TDRs. To determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Company's underwriting policy. During the year ended December 31, 2020, loans totaling approximately \$28,554,000 were amended to allow for the deferment of principal payments, and in some cases interest, for periods up to six months. These restructurings were not treated as TDRs in accordance with Section 4013 of the CARES Act. As of December 31, 2020, all such deferral periods had ended, and the loans are current with respect to regularly scheduled principal and interest payments.

Salaries and employee benefits totaling \$178,554 and \$219,208 have been deferred as direct loan origination costs for the years ended December 31, 2020 and 2019, respectively.

River Valley Community Bancorp
Notes to Consolidated Financial Statements
December 31, 2020 and 2019

Note 4. Premises and Equipment

Premises and equipment consisted of the following as of December 31, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Land	\$ 1,723,198	\$ 1,411,489
Buildings and improvements	5,453,918	3,766,691
Furniture, fixtures, and equipment	1,345,555	1,142,956
Leasehold improvements	42,722	42,722
In process	<u>85,830</u>	<u>5,610</u>
	8,651,223	6,369,468
Accumulated depreciation	<u>(1,469,582)</u>	<u>(1,298,069)</u>
Total	<u>\$ 7,181,641</u>	<u>\$ 5,071,399</u>

Depreciation included in occupancy and equipment expense totaled \$338,000 and \$281,452 for the years ended December 31, 2020 and 2019, respectively.

Note 5. Leases

As of December 31, 2020, the Company has no finance leases and one operating lease for a branch office. This operating lease has a remaining term through May 2023 with two optional 5-year renewal periods thereafter. As of December 31, 2020 and 2019, the right of use asset included in accrued interest receivable and other assets totaled \$976,659 and \$1,040,611, respectively, and the lease liability included in accrued interest payable and other liabilities totaled \$1,013,394 and \$1,062,377, respectively, determined using a discount rate of 3.17%. During the years ended December 31, 2020 and 2019, the Company recognized operating, short-term, and other variable lease costs totaling \$120,346 and \$138,923, respectively. Future undiscounted lease payments are as follows for the years ending December 31:

2021	\$ 84,198
2022	86,724
2023	89,326
2024	92,006
2025	94,766
Thereafter	<u>790,584</u>
Total undiscounted lease payments	1,237,604
Less imputed interest	<u>224,210</u>
Net lease liability	<u>\$ 1,013,394</u>

Note 6. Time Deposits

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

2021	\$ 25,851,023
2022	971,280
2023	472,085
2025	<u>40,753</u>
Total	<u>\$ 27,335,141</u>

Note 7. Borrowing Facilities

The Company has unsecured Federal funds lines of credit with correspondent banks under which it can borrow up to \$23,200,000 as of December 31, 2020. There were no borrowings outstanding under these arrangements as of December 31, 2020 and 2019, respectively.

In addition, the Company has an arrangement with the FHLB under which it may borrow up to 35% of total assets, which must be fully secured by qualifying assets. As of December 31, 2020 and 2019, the estimated fair value of investment securities pledged was approximately \$58,382,000 and \$76,083,000, respectively, and the recorded investment in loans pledged was approximately \$181,212,000 and \$155,659,000, respectively. As of December 31, 2020, no borrowings were outstanding. As of December 31, 2019, outstanding fixed rate borrowings were as follows:

<u>Amount</u>	<u>Maturity</u>	<u>Interest Rate</u>
\$ 30,000,000	06/10/21	2.00%
20,000,000	04/29/21	2.43%
15,000,000	04/29/20	2.50%
<u>\$ 65,000,000</u>		

During the year ended December 31, 2020, outstanding borrowings from the FHLB were restructured and later repaid in their entirety. As a result of these transactions, the Company incurred early termination penalties totaling \$2,329,628, which are included in noninterest expense on the consolidated statements of comprehensive income.

Additionally, the Company utilized the FHLB borrowing arrangement to obtain letters of credit totaling \$11,000,000 and \$35,000,000 as of December 31, 2020 and 2019, respectively, which are used to secure certain public fund deposit accounts. The combination of outstanding borrowings and outstanding letters of credit reduce the amount available to be borrowed. As of December 31, 2020 and 2019, the available borrowing capacity under this arrangement was approximately \$75,883,000 and \$56,494,000, respectively.

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December 31, 2020 and 2019

Note 8. Income Taxes

Income taxes for the years ended December 31, 2020 and 2019 consist of the following:

	<u>2020</u>	<u>2019</u>
Current	\$ 1,827,987	\$ 1,503,207
Deferred	(344,085)	19,602
Income tax expense	<u>\$ 1,483,902</u>	<u>\$ 1,522,809</u>

Deferred tax assets and liabilities as of December 31, 2020 and 2019 consist of the following:

	<u>2020</u>	<u>2019</u>
Deferred tax assets:		
Allowance for loan losses	\$ 988,749	\$ 703,556
Lease liability	299,596	314,077
Accrued expenses	232,864	189,467
Future benefit of state tax deduction	154,329	140,671
Other	111,095	90,957
Total	<u>1,786,633</u>	<u>1,438,728</u>
Deferred tax liabilities:		
Unrealized gain on investment securities available-for-sale	(2,888,568)	(939,203)
Lease right of use asset	(288,736)	(307,642)
Premises and equipment	(242,334)	(232,200)
Deferred loan origination costs, net	(100,469)	(110,045)
Other	(44,565)	(22,397)
Total	<u>(3,564,672)</u>	<u>(1,611,487)</u>
Deferred tax liability, net	<u>\$ (1,778,039)</u>	<u>\$ (172,759)</u>

The provision for income taxes differs from amounts computed by applying the statutory federal income tax rate to operating income before income taxes. The significant items comprising these differences consist of the following for the years ended December 31, 2020 and 2019:

	<u>2020</u>		<u>2019</u>	
	<u>Amount</u>	<u>Rate</u>	<u>Amount</u>	<u>Rate</u>
Federal income tax at statutory rates	\$ 1,178,730	21.0%	\$ 1,193,195	21.0%
State franchise tax, net of Federal benefit	478,795	8.5%	486,420	8.6%
Tax exempt investment securities, net	(174,241)	-3.1%	(156,361)	-2.8%
Other	618	0.0%	(445)	0.0%
Total	<u>\$ 1,483,902</u>	<u>26.4%</u>	<u>\$ 1,522,809</u>	<u>26.8%</u>

Federal and California state franchise tax returns submitted for the year ended December 31, 2017 and 2016, respectively, and after that time are currently open for examination. The Company currently has no tax returns under examination.

Note 9. Commitments and Contingencies

Financial instruments with off-balance sheet risk – The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments consist of the following as of December 31, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Commitments to extend credit	\$ 44,228,701	\$ 53,759,218
Standby letters of credit	10,000	20,000

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

Commitments to extend credit are agreements to lend to a customer if there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, and deeds of trust on residential real estate and income-producing commercial properties.

Real estate loan commitments represent approximately 42% of total commitments and are generally secured by property with a loan-to-value ratio not to exceed 75%. Agricultural production loan commitments represent approximately 13% of total commitments and are generally secured by crop assignments, accounts receivable, and farm equipment and have variable interest rates. Commercial and industrial loan commitments represent approximately 45% of total commitments and are generally unsecured or secured by collateral other than real estate and have variable interest rates.

Concentrations of credit risk – The Company grants real estate loans to customers in Sutter, Yuba, Nevada, Placer, and surrounding counties. In management's judgment, a concentration of loans exists in real estate secured loans with approximately 71% of the Company's loans being real estate related. Although management believes the loans within this concentration have no more than the normal risk of collectability, a substantial decline in the performance of the economy in general or a decline in real estate values in the Company's primary market area could have an adverse impact on the collectability of these loans. Cash flows from commercial real estate properties and personal income represents the primary source of repayment for most of these loans.

Deposit concentration – The Company has a limited number of deposit relationships greater than 3% of total deposits that in the aggregate represents approximately 9% of the Company's deposits as of December 31, 2020. The loss of these deposit relationships could have a material impact on the Company's operations and liquidity. However, management mitigates this risk by maintaining sufficient on and off-balance sheet liquidity to manage fluctuations in account balances.

Correspondent banking arrangements – The Company maintains funds on deposit with other federally insured financial institutions under correspondent banking agreements. As of December 31, 2020, uninsured deposits at correspondent banks totaled approximately \$10,599,000. Management performs an assessment of the financial strength of its correspondent banks annually or more frequently as deemed necessary.

Note 10. Stock Compensation

The Company has one stock compensation plan, the River Valley Community Bank 2016 Equity Incentive Plan (the "Plan"), which was approved by the Company's shareholders. A total of 279,200 shares of common stock are reserved for grants of awards to employees, directors, and consultants under incentive and non-statutory stock option agreements and restricted stock agreements. The Plan was adopted by the Bancorp as part of the Merger, and new equity awards and common shares are issued by the Bancorp.

The amount, frequency, and terms of share-based awards may vary based on competitive practices, the Company's operating results, and government regulations. Generally, stock awards vest over a five-year term, and stock options expire ten years after the date of grant. New shares are issued upon stock option exercise or restricted stock vesting. The Plan requires that the option price may not be less than the fair market value of the stock at the date the option is granted and that the stock must be paid in full at the time the option is exercised.

Restricted stock awards are grants of shares of common stock that are subject to forfeiture until specific conditions or goals are met. Conditions may be based on continuing employment or achieving specified performance goals. During the period of restriction, participants holding restricted stock do not have voting or dividend rights. The restrictions lapse in accordance with a schedule or with other conditions determined by the Board of Directors. No restricted stock was issued during the years ended December 31, 2020 and 2019.

A summary of stock option activity for the year ended December 31, 2020 is presented below:

	<u>Shares</u>	<u>Weighted Avg. Exercise Price</u>	<u>Weighted Avg. Remaining Contract Term (Years)</u>
Outstanding, beginning of year	239,950	\$ 14.48	
New grants	13,300	19.74	
Exercises	(32,062)	9.93	
Forfeitures	(16,038)	17.59	
Expired	-	-	
Outstanding, end of year	<u>205,150</u>	<u>\$ 14.76</u>	5.63
Exercisable, end of year	<u>133,390</u>	<u>\$ 13.19</u>	4.53

Information related to stock options granted during the years ended December 31, 2020 and 2019 and total compensation cost recognized for all stock awards during the same periods is as follows:

	<u>2020</u>	<u>2019</u>
Weighted average grant date fair value per share	\$ 5.84	\$ 7.00
Significant fair value assumptions:		
Expected term	6.5 years	6.5 years
Expected annual volatility	27.8%	30.7%
Expected annual dividend yield	0.0%	0.0%
Risk-free interest rate	0.8%	1.9%
Total compensation cost included in noninterest expense	177,830	\$ 217,126

Stock options exercised during the years ended December 31, 2020 and 2019 had an intrinsic value of \$234,949 and \$112,668, respectively, and resulted in the Company receiving cash of \$318,196 and \$136,408, respectively, upon exercise. As of December 31, 2020, the unrecognized compensation cost related to non-vested stock awards totaled \$396,274, which is expected to be amortized on a straight-line basis over a weighted average period of 2.1 years and will be adjusted for subsequent changes in forfeitures.

Note 11. Shareholders' Equity

Earnings per share – A reconciliation of the components of the basic and diluted earnings per share computations for the years ended December 31, 2020 and 2019 is as follows:

	Net Income Available to Common Shareholders	Weighted Average Shares Outstanding	Earnings per Common Share
December 31, 2020:			
Basic	\$ 4,129,097	2,372,884	\$ 1.74
Dilution effect	-	65,131	(0.05)
Diluted	<u>\$ 4,129,097</u>	<u>2,438,015</u>	<u>\$ 1.69</u>
December 31, 2019:			
Basic	\$ 4,159,074	2,381,659	\$ 1.75
Dilution effect	-	89,726	(0.07)
Diluted	<u>\$ 4,159,074</u>	<u>2,471,385</u>	<u>\$ 1.68</u>

Shares of common stock issuable under stock options that have an exercise price greater than average market prices are not included in the computation of diluted earnings per share due to their antidilutive effect. For the years ended December 31, 2020 and 2019, antidilutive stock options totaled 7,300 and 16,000, respectively.

Dividends – Upon declaration by the Board of Directors, all shareholders of record will be entitled to receive dividends. The California Financial Code restricts the total dividend payment of any state banking association in any calendar year to the lesser of (1) the bank's retained earnings or (2) the bank's net income for its last three fiscal years, less distributions made to shareholders during the same three-year period. As of December 31, 2020, retained earnings of \$11,465,469 were free of such restrictions.

Note 11. Shareholders' Equity (continued)

Regulatory capital – The Bank is subject to regulatory capital requirements administered by the FDIC. Capital adequacy guidelines and 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 regulatory action. 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. Under Basel III rules, the Bank must hold a capital conservation buffer above the adequately capitalized risk-based capital ratios of 2.500%. The net unrealized gain or loss on investment securities available-for-sale is not included in computing regulatory capital. Management believes that as of December 31, 2020, the Bank meets all capital adequacy requirements to which it is subject.

Prompt corrective action regulations provide five classifications: 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. As of December 31, 2020, the most recent regulatory notification categorized the Bank as well capitalized. No conditions or events have occurred since that notification that management believes has changed the Bank's category.

Actual and required capital amounts and ratios for the Bank as of December 31, 2020 and 2019 are as follows:

	2020		2019	
	Amount	Ratio	Amount	Ratio
Tier 1 capital to average assets:				
The Bank	\$ 39,527,000	8.1%	\$ 35,136,000	8.2%
Minimum to be "Well-Capitalized"	24,664,250	5.0%	21,424,300	5.0%
Minimum regulatory requirement	19,731,400	4.0%	17,139,440	4.0%
Tier 1 common to risk weighted assets:				
The Bank	\$ 39,527,000	13.3%	\$ 35,136,000	11.5%
Minimum to be "Well-Capitalized"	19,358,365	6.5%	19,666,790	6.5%
Minimum regulatory requirement	13,401,945	4.5%	13,615,470	4.5%
Tier 1 capital to risk weighted assets:				
The Bank	\$ 39,527,000	13.3%	\$ 35,136,000	11.5%
Minimum to be "Well-Capitalized"	23,825,680	8.0%	24,205,280	8.0%
Minimum regulatory requirement	17,869,260	6.0%	18,153,960	6.0%
Total capital to risk weighted assets:				
The Bank	\$ 43,187,000	14.5%	\$ 37,842,000	12.5%
Minimum to be "Well-Capitalized"	29,782,100	10.0%	30,256,600	10.0%
Minimum regulatory requirement	23,825,680	8.0%	24,205,280	8.0%

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Note 12. Derivatives

As of December 31, 2020 and 2019, the Company has derivatives that do not qualify for hedge accounting, and therefore changes in fair value are reported in earnings. The derivatives consist of interest rate floors and caps placed on variable rate loans to make them perform similar to fixed rate loans. For each of these loans, the Company entered into a corresponding interest rate swap agreement with a third party, with notional amounts and other terms consistent with the related loan. The amount exchanged under the interest rate swap agreements is determined by reference to the notional amount and other terms. Summary information about the Company's derivatives as of December 31, 2020 and 2019 is as follows:

	<u>2020</u>	<u>2019</u>
Total loans with floors and caps	\$ 2,575,751	\$ 3,676,570
Total notional amounts of interest rate swaps	2,575,751	3,676,570
Total fair value of floors and caps, net	317,809	192,674
Total fair value of interest rate swaps, net	(317,809)	(192,674)
Weighted average maturity	10.2 years	10.2 years

The fair value of interest rate floors and caps, net is reflected in accrued interest payable and other liabilities with changes in fair value recorded in noninterest income. The fair value of interest rate swaps, net is reflected in accrued interest receivable and other assets with changes in fair value recorded in noninterest income. Changes in the fair value of interest rate floors and caps are offset by contrasting changes in the fair value of interest rate swaps, resulting in little to no impact on noninterest income. As of December 31, 2020 and 2019, the estimated fair value of investment securities pledged to secure the interest rate swap agreements was approximately \$452,000 and \$558,000, respectively.

Note 13. Related Party Transactions

During the normal course of business, the Company enters into transactions with related parties, including directors and executive officers. The following is a summary of the aggregate activity involving related party borrowers for the years ended December 31, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Related party loans, beginning of year	\$ 10,882,380	\$ 8,295,972
Advances	6,716,335	6,113,531
Payments	(6,759,767)	(3,527,123)
Related party loans, end of year	<u>\$ 10,838,948</u>	<u>\$ 10,882,380</u>
Undisbursed commitments to related parties, end of year	<u>\$ 4,135,843</u>	<u>\$ 5,927,302</u>

Related party deposits totaled approximately \$23,717,000 and \$20,514,000 as of December 31, 2020 and 2019, respectively. During the year ended December 31, 2020, the Company paid approximately \$634,000 to an entity controlled by a director in relation to building improvements at a new branch opened in August 2020.

Note 14. Employee Benefit Plan

The Company has a 401(k) profit sharing plan. All employees 18 years of age or older with 30 days of service are eligible to participate in the plan. Eligible employees may elect to make tax deferred contributions up to the maximum amount allowed by law. Safe harbor contributions of \$113,322 and \$109,427 were made during the years ended December 31, 2020 and 2019, respectively.

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Note 15. Fair Value Measurements

Assets and liabilities measured at fair value on a recurring basis as of December 31, 2020 and 2019 and the level input used to determine the estimated fair value are summarized below:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
December 31, 2020:				
Investment securities available-for-sale:				
Obligations of states and political subdivisions	\$ -	\$ 41,139,940	\$ -	\$ 41,139,940
U.S. Government sponsored agencies collateralized by mortgage obligations	-	56,620,693	-	56,620,693
U.S. Government sponsored agencies mortgage-backed securities	-	11,975,166	-	11,975,166
Corporate debt securities	-	30,999,130	-	30,999,130
Student loan backed securities	-	28,203,850	-	28,203,850
Total investment securities	<u>\$ -</u>	<u>\$ 168,938,779</u>	<u>\$ -</u>	<u>\$ 168,938,779</u>
Derivative assets, net	<u>\$ -</u>	<u>\$ 317,809</u>	<u>\$ -</u>	<u>\$ 317,809</u>
Derivative liabilities, net	<u>\$ -</u>	<u>\$ (317,809)</u>	<u>\$ -</u>	<u>\$ (317,809)</u>
December 31, 2019:				
Investment securities available-for-sale:				
Obligations of states and political subdivisions	-	25,027,380	-	25,027,380
U.S. Government sponsored agencies collateralized by mortgage obligations	-	65,533,151	-	65,533,151
U.S. Government sponsored agencies mortgage-backed securities	-	12,720,638	-	12,720,638
Corporate debt securities	-	43,446,123	-	43,446,123
Student loan backed securities	-	28,027,974	-	28,027,974
Total investment securities	<u>\$ -</u>	<u>\$ 174,755,266</u>	<u>\$ -</u>	<u>\$ 174,755,266</u>
Derivative assets, net	<u>\$ -</u>	<u>\$ 192,674</u>	<u>\$ -</u>	<u>\$ 192,674</u>
Derivative liabilities, net	<u>\$ -</u>	<u>\$ (192,674)</u>	<u>\$ -</u>	<u>\$ (192,674)</u>

The following transfers between levels occurred during the years ended December 31, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Transfers from Level 1 to Level 2:		
Corporate debt securities	\$ -	\$ 6,690,243

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Note 15. Fair Value Measurements (continued)

The carrying amounts and estimated fair values of financial instruments not carried at fair value as of December 31, 2020 and 2019 are as follows:

	Carrying Amount	Estimate Fair Value			Total
		Level 1	Level 2	Level 3	
December 31, 2020:					
Financial assets:					
Cash and due from banks	\$ 5,166,671	\$ 5,166,671	\$ -	\$ -	\$ 5,166,671
Interest bearing deposits in banks	47,800,372	47,800,372	-	-	47,800,372
Time deposit in banks	1,240,000	-	1,354,314	-	1,354,314
Loans, net	254,270,648	-	-	253,883,444	253,883,444
Accrued interest receivable	1,620,293	-	1,620,293	-	1,620,293
Financial liabilities:					
Deposits	445,162,069	417,826,928	27,388,566	-	445,215,494
Accrued interest payable	39,927	-	39,927	-	39,927
December 31, 2019:					
Financial assets:					
Cash and due from banks	\$ 4,991,107	\$ 4,991,107	\$ -	\$ -	\$ 4,991,107
Interest bearing deposits in banks	43,364,723	43,364,723	-	-	43,364,723
Time deposit in banks	2,481,000	-	2,547,617	-	2,547,617
Loans, net	200,511,507	-	-	199,562,042	199,562,042
Accrued interest receivable	1,473,799	-	1,473,799	-	1,473,799
Financial liabilities:					
Deposits	337,128,708	278,369,094	58,857,448	-	337,226,542
FHLB borrowings	65,000,000	-	65,350,707	-	65,350,707
Accrued interest payable	287,035	-	287,035	-	287,035