FEDERAL DEPOSIT INSURANCE CORPORATION
Washington, D.C. 20429

FORM 10-Q

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended March 31, 2020

or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from _____________ to _____________

FDIC Certificate No. 32203

Summit State Bank

(Exact Name of Registrant as Specified in its Charter)

California	94-2878925
(State of Incorporation)	(I.R.S. Employer Identification No.)
500 Bicentennial Way, Santa Rosa, CA 95403	707-568-6000
(Address of Principal Executive Offices)	(Registrant's Telephone Number, Including Area Code)

N/A
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☐ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐	Accelerated filer ☐
Non-accelerated filer ☐	Smaller reporting company ☒
Emerging growth company ☐	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.☐

Indicate by check mark if the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No☒

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes ☐ No ☐

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock	SSBI	The NASDAQ Stock Market LLC

APPLICABLE ONLY TO CORPORATE ISSUERS

As of May 19, 2020, there were 6,069,600 shares of common stock outstanding.

SUMMIT STATE BANK

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SUMMIT STATE BANK AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
(In thousands except share data)

	March 31, 2020 (Unaudited)	December 31, 2019 (1)
ASSETS		
Cash and due from banks	$ 36,493	$ 38,299
Total cash and cash equivalents	36,493	38,299
Investment securities:		
Held-to-maturity, at amortized cost	-	7,998
Available-for-sale (at fair value; amortized cost of $58,690 in 2020 and $53,591 in 2019)	58,160	54,241
Total investment securities	58,160	62,239
Loans, less allowance for loan losses of $7,375 in 2020 and $6,769 in 2019	601,400	576,548
Bank premises and equipment, net	6,270	6,301
Investment in Federal Home Loan Bank stock, at cost	3,342	3,342
Goodwill	4,119	4,119
Accrued interest receivable and other assets	11,861	5,130
Total assets	$ 721,645	$ 695,978
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits:		
Demand - non interest-bearing	$ 136,875	$ 129,084
Demand - interest-bearing	66,412	69,383
Savings	27,459	28,359
Money market	123,341	128,377
Time deposits that meet or exceed the FDIC insurance limit	47,682	76,564
Other time deposits	172,237	142,070
Total deposits	574,006	573,837
Federal Home Loan Bank advances	69,300	45,600
Junior subordinated debt	5,865	5,862
Accrued interest payable and other liabilities	4,273	3,335
Total liabilities	653,444	628,634
Commitments and contingencies (Note 3)		
Shareholders' equity		
Preferred stock, no par value; 20,000,000 shares authorized; no shares issued and outstanding	-	-
Common stock, no par value; shares authorized - 30,000,000 shares; issued and outstanding 6,069,600 in 2020 and 6,069,600 in 2019	36,981	36,981
Retained earnings	31,593	29,906
Accumulated other comprehensive (loss) income, net	(373)	457
Total shareholders' equity	68,201	67,344
Total liabilities and shareholders' equity	$ 721,645	$ 695,978

(1) Information derived from audited financial statements.

The accompanying notes are an integral part of these unaudited consolidated financial statements.

SUMMIT STATE BANK AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(In thousands except earnings per share data)

	Three Months Ended	
	March 31, 2020 (unaudited)	**March 31, 2019 (unaudited)**
Interest income:		
Interest and fees on loans	$ 7,820	$ 6,452
Interest on deposits with banks	44	101
Interest on investment securities	369	590
Dividends on FHLB stock	59	54
Total interest income	8,292	7,197
Interest expense:		
Deposits	1,445	1,471
Federal Home Loan Bank advances	322	179
Total interest expense	1,767	1,650
Net interest income before provision for loan losses	6,525	5,547
Provision for loan losses	600	100
Net interest income after provision for loan losses	5,925	5,447
Non-interest income:		
Service charges on deposit accounts	214	190
Rental income	87	90
Net gain on loan sales	697	167
Net securities gain	871	-
Other income	60	46
Total non-interest income	1,929	493
Non-interest expense:		
Salaries and employee benefits	2,723	2,657
Occupancy and equipment	383	423
Other expenses	1,316	1,132
Total non-interest expense	4,422	4,212
Income before provision for income taxes	3,432	1,728
Provision for income taxes	1,017	303
Net income	$ 2,415	$ 1,425
Basic earnings per common share	$ 0.40	$ 0.23
Diluted earnings per common share	$ 0.40	$ 0.23
Basic weighted average shares of common stock outstanding	6,070	6,067
Diluted weighted average shares of common stock outstanding	6,074	6,073

The accompanying notes are an integral part of these unaudited consolidated financial statements.

SUMMIT STATE BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In thousands)

	Three Months Ended	
	March 31, 2020 (unaudited)	March 31, 2019 (unaudited)
Net income	$ 2,415	$ 1,425
Change in securities available-for-sale:		
Unrealized holding (losses) gains on available-for-sale securites arising during the period	(308)	1,622
Reclassification adjustment for gains realized in net income on available-for-sale securities	(871)	-
Net unrealized (losses) gains, before provision for income tax	(1,179)	1,622
Income tax benefit (provision)	349	(481)
Total other comprehensive (loss) income, net of tax	(830)	1,141
Comprehensive income	$ 1,585	$ 2,566

The accompanying notes are an integral part of these unaudited consolidated financial statements.

SUMMIT STATE BANK AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

For the Three Months Ended March 31, 2019, June 30, 2019, September 30, 2019, December 31, 2019 and March 31, 2020 (Unaudited)

(In thousands except per share data)

	Common Stock		Retained	Accumulated Other Comprehensive	Total Shareholders'
	Shares	Amount	Earnings	Income (Loss)	Equity
Balance, January 1, 2019	6,066	$ 36,967	$ 26,342	$ (1,789)	$ 61,520
Net income			1,425		1,425
Other comprehensive income, net				1,141	1,141
Exercise of stock options	2	7			7
Cash dividends - $0.12 per share			(728)		(728)
Balance, March 31, 2019	6,068	$ 36,974	$ 27,039	$ (648)	$ 63,365
Net income			1,172		1,172
Other comprehensive income, net				932	932
Cash dividends - $0.12 per share			(728)		(728)
Balance, June 30, 2019	6,068	$ 36,974	$ 27,483	$ 284	$ 64,741
Net income			2,045		2,045
Other comprehensive income, net				439	439
Exercise of stock options	2	7			7
Cash dividends - $0.12 per share			(728)		(728)
Balance, September 30, 2019	6,070	$ 36,981	$ 28,800	$ 723	$ 66,504
Net income			1,834		1,834
Other comprehensive loss, net				(266)	(266)
Cash dividends - $0.12 per share			(728)		(728)
Balance, December 31, 2019	6,070	$ 36,981	$ 29,906	$ 457	$ 67,344
Balance, January 1, 2020	6,070	36,981	29,906	457	$ 67,344
Net income			2,415		2,415
Other comprehensive loss, net				(830)	(830)
Cash dividends - $0.12 per share			(728)		(728)
Balance, March 31, 2020	6,070	$ 36,981	$ 31,593	$ (373)	$ 68,201

The accompanying notes are an integral part of these unaudited consolidated financial statements.

SUMMIT STATE BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)	Three Months Ended March 31, 2020 (unaudited)	Three Months Ended March 31, 2019 (unaudited)
Cash flows from operating activities:		
Net income	$ 2,415	$ 1,425
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation and amortization	208	199
Securities amortization and accretion, net	(3)	21
Accretion of deferred loan fees	(568)	(403)
Provision for loan losses	600	100
Net securities gains	(871)	-
Net gain on loan sales	(697)	(167)
Net change in accrued interest receivable and other assets	867	36
Net change in accrued interest payable and other liabilities	(569)	(173)
Share-based compensation expense	258	173
Net cash from operating activities	1,640	1,211
Cash flows from investing activities:		
Purchases of available-for-sale investment securities	(45,265)	(874)
Proceeds from calls of held-to-maturity investment securities	8,000	-
Proceeds from calls and maturities of available-for-sale investment securities	35,039	1,083
Loan origination and principal collections, net	(36,888)	(8,070)
Proceeds from sales of loans other than loans originated for resale	12,701	3,100
Purchases of bank premises and equipment, net	(177)	(760)
Net cash used in investing activities	(26,590)	(5,521)

(Continued)

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)	Three Months Ended March 31, 2020 (unaudited)	Three Months Ended March 31, 2019 (unaudited)
Cash flows from financing activities:		
Net change in demand, savings and money market deposits	(1,116)	3,526
Net change in certificates of deposit	1,285	50,540
Net change in short term Federal Home Loan Bank advances	(12,300)	(52,100)
Net change in long term Federal Home Loan Bank advances	36,000	-
Net change in Junior Subordinated Debt	3	-
Dividends paid on common stock	(728)	(728)
Proceeds from exercise of stock options	-	7
Net cash from financing activities	23,144	1,245
Net change in cash and cash equivalents	(1,806)	(3,065)
Cash and cash equivalents at beginning of year	38,299	21,693
Cash and cash equivalents at end of period	$ 36,493	$ 18,628
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest	$ 1,829	$ 1,615
Non-Cash Investing and Financing Activities:		
Net unrealized (losses) gains on available-for-sale securities	$ (1,179)	$ 1,622

The accompanying notes are an integral part of these unaudited consolidated financial statements.

SUMMIT STATE BANK AND SUBSIDIARY

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General

On January 15, 1999, Summit State Bank (the "Bank" or "the Bank") received authority to transact business as a California state-chartered commercial bank and is subject to regulation, supervision and examination by the State of California Department of Business Oversight and the Federal Deposit Insurance Corporation. The Bank was incorporated on December 20, 1982 under the name Summit Savings. The Bank provides a variety of banking services to individuals and businesses in its primary service area of Sonoma County, California. The Bank's branch locations include Santa Rosa, Petaluma, Rohnert Park and Healdsburg. The Bank offers depository and lending services primarily to meet the needs of its business, nonprofit organization and individual clientele. These services include a variety of transaction, money market, savings and time deposit account alternatives. The Bank's lending activities are directed primarily towards commercial real estate, construction and business loans. The Bank originally used its subsidiary Alto Service Corporation for its deed of trust services. On July 17, 2019 the Bank filed a certification of dissolution and the filing effectively dissolved ALTO.

The financial statements as of March 31, 2020 and for the three months ended March 31, 2020 and 2019 are unaudited. In the opinion of management, these unaudited financial statements contain all adjustments, consisting only of normal recurring accruals necessary to present fairly the financial statements of the Bank.

The accompanying unaudited interim financial statements have been prepared in accordance with U.S. Generally Accepted Accounting Principles for interim financial information and Article 8 of Regulation S-X of the Securities and Exchange Commission. Operating results for the three months ended March 31, 2020 are not necessarily indicative of the results that may be expected for the year ending December 31, 2020. These unaudited financial statements do not include all disclosures associated with the Bank's annual financial statements and notes thereto and accordingly, should be read in conjunction with the financial statements and notes thereto included in the Bank's Annual Report for the year ended December 31, 2019 on Form 10-K on file with the FDIC (Form 10-K may be found at www.summitstatebank.com).

The accompanying accounting and reporting policies of the Bank and subsidiary conform to U.S. Generally Accepted Accounting Principles and prevailing practices within the banking industry.

Principles of Consolidation

The consolidated financial statements include the accounts of the Bank and its wholly-owned subsidiary, Alto Service Corporation. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with U.S. Generally Accepted Accounting Principles requires management to make estimates and assumptions. 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 allowance for loan losses, goodwill impairment, valuation of other real estate owned, and fair values of investment securities are particularly subject to change.

Revenue Recognition

The Bank records revenue from contracts with customers in accordance with Accounting Standards Codification Topic 606, "Revenue from Contracts with Customers" ("Topic 606"). Under Topic 606, the Bank must identify the contract with a customer, identify the performance obligations in the contract, determine the transaction price, allocate the transaction price to the performance obligations in the contract, and recognize revenue when (or as) the Bank satisfies a performance obligation.

Most of our revenue-generating transactions are not subject to Topic 606, including revenue generated from financial instruments, such as our loans and investment securities. In addition, certain noninterest income streams such as fees associated with mortgage servicing rights, gains on sales of loans, financial guarantees, derivatives, and certain credit card fees are also not in scope of the new guidance. The Bank's noninterest revenue streams are largely based on transactional activity, or standard month-end revenue accruals such as asset management fees based on month-end market values. Consideration is often received immediately or shortly after the Bank satisfies its performance obligation and revenue is recognized. The Bank does not typically enter into long-term revenue contracts with customers, and therefore, does not experience significant contract balances. As of March 31, 2020, the Bank did not have any significant contract balances. The Bank has evaluated the nature of its revenue streams and determined that further disaggregation of revenue into more granular categories beyond what is presented on the statements of income was not necessary. The following are descriptions of revenues within the scope of ASC 606.

Deposit service charges - The Bank earns fees from its deposit customers for account maintenance, transaction-based and overdraft services. Account maintenance fees consist primarily of account fees and analyzed account fees charged on deposit accounts on a monthly basis. The performance obligation is satisfied, and the fees are recognized on a monthly basis as the service period is completed. Transaction-based fees on deposit accounts are charged to deposit customers for specific services provided to the customer, such as non-sufficient funds fees, overdraft fees, and wire fees. The performance obligation is completed as the transaction occurs and the fees are recognized at the time each specific service is provided to the customer.

Debit and ATM interchange fee income and expenses - Debit and ATM interchange income represent fees earned when a debit card issued by the Bank is used. The Bank earns interchange fees from debit cardholder transactions through the Visa payment network. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, concurrently with the transaction processing services provided to the cardholder. The performance obligation is satisfied, and the fees are earned when the cost of the transaction is charged to the cardholders' debit card. Certain expenses directly associated with the credit and debit card are recorded on a net basis with the interchange income.

Rental Income – Leases originated by the Bank are recorded as rental income and included in the other non-interest income category. Rental income is recognized in the month in which the revenue covers. Leasehold improvements and operational expenses associated with the rental proper are recorded separate from the income as an expense.

Gain/loss on other real estate owned, net - The Bank records a gain or loss from the sale of other real estate owned when control of the property transfers to the buyer, which generally occurs at the time of an executed deed of trust. When the Bank finances the sale of other real estate owned to the buyer, the Bank assesses whether the buyer is committed to perform their obligations under the contract and whether collectability of the transaction price is probable. Once these criteria are met, the other real estate owned asset is derecognized and the gain or loss on sale is recorded upon the transfer of control of the property to the buyer. In determining the gain or loss on sale, the Bank adjusts the transaction price and related gain or loss on sale if a significant financing component is present

Junior Subordinated Debt

On June 28, 2019 the Bank completed the private placement of $6,000,000 in fixed-to-floating rate subordinated notes (the "Notes") to support organic growth and for general corporate purposes. The Notes are for a 10-year term, due June 30, 2029, and have been structured to qualify as Tier 2 capital for regulatory purposes. The Notes will bear interest at a fixed rate of 6.0% per annum until June 30, 2024. For the remainder of the term, through June 30, 2029, the Notes will bear interest at a rate equal to 3-month Libor plus 362 basis points. The subordinated notes are redeemable by the Bank at its option, in whole or in part, on or after June 30, 2024, or in whole but not in part under certain other circumstances. The Notes are reported net of any debt issuance cost which totaled $135,000 at March 31, 2020.

Alto Service Corporation Dissolution

Alto Service Corporation ("Alto") was originally established to act as the Trustee for Deeds of Trust and is wholly owned by Summit. In June 2019 the Bank began the process to dissolve Alto in accordance with the Bank's Plan of Dissolution which included paying off all of its liabilities, which total $0, and distribute its net assets to the Bank. A Certificate of Dissolution was filed with the State of California and Alto was dissolved effective July 17, 2019.

Recently Adopted Accounting Standards

Accounting Standards Pending Adoption

In June of 2016, the FASB issued ASU No. 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The amendments are intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The ASU requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. Organizations will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. The ASU requires enhanced disclosures to help investors and other financial statement users to better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio. These disclosures include qualitative and quantitative requirements that provide additional information about the amounts recorded in the financial statements. In addition, the ASU amends the accounting guidance for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. In October 2019 FASB updated the effective date for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2022. Early application will be permitted on January 1 for fiscal years beginning after December 15, 2018. The Bank has a CECL model in place that has been running parallel to existing practices since January 1, 2019. The Bank may elect to adopt the new CECL model before the effective date but currently has not determined if or when early adoption will occur. The CECL model will continue to run parallel and be back tested until it is brought into live production; prior to going live the Bank will communicate the impact this new standard will have on the financial statements. Due to current economic uncertainties related to COVID-19 and uncertainty related to the date of adoption, an estimate on the impact of this new standard cannot reasonably be made.

In January of 2017, the FASB issued ASU No. 2017-04, Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment. The amendments are intended to simplify the subsequent measurement of goodwill, and the amendments eliminate Step 2 from the goodwill impairment test. The annual, or interim, goodwill impairment test is performed by comparing the fair value of a reporting unit with its carrying amount. An impairment charge should be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. In addition, income tax effects from any tax-deductible goodwill on the carrying amount of the reporting unit should be considered when measuring the goodwill impairment loss, if applicable. The amendments also eliminate the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The Bank adopted this standard effective January 1, 2020. There was no cumulative effect adjustment recorded upon adoption and the method for determining impairment has been disclosed.

In August 2018, the FASB issued ASU No. 2018-13, Fair Value Measurement (Topic 820): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement. The amendments in this update remove, modify or add disclosure requirements for fair value measurements to improve the effectiveness of disclosures. The Bank adopted this standard effective January 1, 2020. There was no cumulative effect adjustment recorded upon adoption.

In April 2019, the FASB issued ASU No. 2019-04, Codification Improvements to Topic 326, Financial Instruments - Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments. With respect to Topic 815, Derivatives and Hedging, ASU 2019-04 clarifies that the reclassification of a debt security from held-to-maturity ("HTM") to available-for-sale ("AFS") under the transition guidance in ASU 2017-12 would not (1) call into question the classification of other HTM securities, (2) be required to actually designate any reclassified security in a last-of-layer hedge, or (3) be restricted from selling any reclassified security. As part of the transition of ASU 2019-04, entities may reclassify securities that would qualify for designation as the hedged item in a last-of-layer hedging relationship from HTM to AFS; however, entities that already made such a reclassification upon their adoption of ASU 2017-12 are precluded from reclassifying additional securities. ASU 2019-04 has the same effective date as ASU 2016-13. Management does not anticipate any potential impact from this new standard. The Bank will continue evaluating the potential impact of this standard in connection with the adoption of ASU 2016-13.

In May 2019, the FASB issued ASU No. 2019-05, Financial Instruments - Credit Losses (Topic 326); Targeted Transition Relief. This ASU allows entities to irrevocably elect, upon adoption of ASU 2016-13, the fair value option on financial instruments that (1) were previously recorded at amortized cost and (2) are within the scope of ASC 326-20 if the instruments are eligible for the fair value option under ASC 825-10. The fair value option election does not apply to held-to-maturity debt securities. Entities are required to make this election on an instrument-by-instrument basis. ASU 2019-05 has the same effective date as ASU 2016-13 (i.e., the first quarter of 2023). Management does not anticipate any potential impact from the new standard on our financial statements.

In March 2020, the FASB issued ASU No. 2020-04, Reference Rate Reform (Topic 848). The amendments in this ASU are elective and provide optional guidance for a limited period of time to ease the potential burden in accounting for (or recognizing the effects of) reference rate reform. The amendments in this ASU provide optional expedients and exceptions for applying generally accepted accounting principles (GAAP) to contracts, hedging relationships, and other transactions that reference LIBOR or another reference rate expected to be discontinued because of reference rate reform. The amendments in this ASU may be elected as of March 12, 2020 through December 31, 2022. An entity may choose to elect the amendments in this update at an interim period subsequent to March 12, 2020 with the method of adoption varying based on transaction type. Currently the Bank only has one loan and one subordinated debt agreement that reference LIBOR. The impact this ASU will have on the Bank is anticipated to be minimal and the Bank has not elected to apply these amendments. The Bank will continue to assess the applicability of the ASU and monitor guidance for reference rate reform from the FASB and its impact on our financial condition and results of operations.

Earnings Per Common Share

Basic earnings per common share (EPS), which excludes dilution, is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted earnings per common 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 share in the earnings of the Bank. Dilutive EPS is computed by dividing income available to common shareholders by the weighted-average common shares outstanding plus the weighted-average number of dilutive shares for the period. The number of potential common shares included in the quarterly diluted EPS is computed using the average market price during the months included in the reporting period under the treasury stock method. Stock options for 3,000 shares of common stock for the three months ended March 31, 2020 were not considered in computing diluted earnings per share because they were anti-dilutive. Stock options for 4,000 shares of common stock for the three months ended March 31, 2019 were not considered in computing diluted earnings per share because they were anti-dilutive.

The factors used in the earnings per common share computation follow:

	Three Months Ended	
(in thousands except earnings per share)	**March 31, 2020**	**March 31, 2019**
Basic		
Net income	$ 2,415	$ 1,425
Weighted average common shares outstanding	6,070	6,067
Basic earnings per common share	$ 0.40	$ 0.23
Diluted		
Net income	$ 2,415	$ 1,425
Weighted average common shares outstanding for basic earnings per common share	6,070	6,067
Add: Dilutive effects of assumed exercises of stock options	4	6
Average shares and dilutive potential common shares	6,074	6,073
Diluted earnings per common share	$ 0.40	$ 0.23

2. SHAREHOLDERS’ EQUITY

Regulatory Capital

The Bank’s actual and required capital amounts and ratios consisted of the following:

(in thousands)	March 31, 2020 Amount	March 31, 2020 Ratio	December 31, 2019 Amount	December 31, 2019 Ratio
Common Equity Tier 1 Capital Ratio				
Summit State Bank	$ 63,518	10.3%	$ 62,071	10.2%
Minimum requirement with capital conservation buffer	$ 43,023	7.0%	$ 42,472	7.0%
Minimum requirement for "Well-Capitalized" institution	$ 39,950	6.5%	$ 39,438	6.5%
Minimum regulatory requirement	$ 27,657	4.5%	$ 27,303	4.5%
Tier 1 Capital Ratio				
Summit State Bank	$ 63,518	10.3%	$ 62,071	10.2%
Minimum requirement with capital conservation buffer	$ 52,242	8.5%	$ 51,573	8.5%
Minimum requirement for "Well-Capitalized" institution	$ 49,169	8.0%	$ 48,539	8.0%
Minimum regulatory requirement	$ 36,877	6.0%	$ 36,404	6.0%
Total Capital Ratio				
Summit State Bank	$ 76,958	12.5%	$ 74,986	12.4%
Minimum requirement with capital conservation buffer	$ 64,534	10.5%	$ 63,708	10.5%
Minimum requirement for "Well-Capitalized" institution	$ 61,461	10.0%	$ 60,674	10.0%
Minimum regulatory requirement	$ 49,169	8.0%	$ 48,539	8.0%
Tier 1 Leverage Ratio				
Summit State Bank	$ 63,518	9.3%	$ 62,071	9.3%
Minimum requirement for "Well-Capitalized" institution	$ 34,189	5.0%	$ 33,510	5.0%
Minimum regulatory requirement	$ 27,351	4.0%	$ 26,808	4.0%

Share-Based Compensation Plans

The shareholders approved the 2013 Equity Incentive Plan (“Plan”) on July 29, 2013. The Plan allows for various equity-based incentives such as stock appreciation rights, restricted stock awards, stock grants and qualified performance-based awards. The Plan reserved 187,500 shares of common stock for issuance to Bank employees and directors. The Plan requires that the option exercise price may not be less than the fair value of the stock at the date the option is granted. Option awards have vesting periods of 5 years unless otherwise approved by the Board of Directors. The option expiration dates are determined by the Board of Directors but may not be later than ten years from the date of grant. No options were granted during the three months ended March 31, 2020 and

March 31, 2019. As of March 31, 2020, 187,500 shares remain available for future grants under the Plan. There were 7,500 options outstanding as of March 31, 2020, which includes options granted under prior stock option plans.

The Bank has granted Stock Appreciation Rights ("SARs") in 2020, 2019 and 2018 to key employees and directors. There were 28,000 SAR grants for the three months ended March 31, 2020. The SARs provide long-term incentives to the employees and directors by providing a cash payment of the difference between the market price of the Bank's common stock at time of exercise and the price at the grant date. The SARs expire ten years from the date of grant, and each has an annual vesting of 20% for the first five years. The obligations associated with the SARs are accounted for as liabilities and are included in accrued interest payable and other liabilities on the balance sheets. The total compensation expense accrued related to the SARs totaled $23,000 and $17,000 for the three months ended March 31, 2020 and March 31, 2019. As of March 31, 2020, there were SAR agreements based on 240,000 common shares and as of March 31, 2019, there were SAR agreements based on 135,000 common shares.

3. COMMITMENTS AND CONTINGENCIES

The Bank is subject to legal proceedings and claims which arise in the ordinary course of business. In the opinion of management, the amount of ultimate liability with respect to such actions will not materially affect the financial condition or results of operations of the Bank.

The Bank's business activity is primarily with clients located within Northern California. Although the Bank has a diversified loan portfolio, a significant portion of its clients' ability to repay loans is dependent upon the real estate market and various economic factors within Sonoma County. Generally, loans are secured by various forms of collateral. The Bank's loan policy requires sufficient collateral to be obtained as necessary to meet the Bank's relative risk criteria for each borrower. The Bank's collateral for the lending portfolio consists primarily of real estate, accounts receivable, inventory and other financial instruments. At March 31, 2020, loans with real estate collateral approximated $550,802,000 or 90% of the loan portfolio compared to $526,265,000 or 90% at December 31, 2019.

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business in order to meet the financing needs of its clients and to reduce its own exposure to fluctuations in interest rates. These financial instruments consist of commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized on the balance sheets. The Bank's exposure to credit loss in the event of nonperformance by the other party for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and standby letters of credit as it does for loans included on the balance sheet.

Commitments to extend credit, which totaled $75,350,000 and $68,545,000 at March 31, 2020 and December 31, 2019, respectively, are agreements to lend to a client as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each client's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of the credit, is based on management's credit evaluation of the borrower. Collateral held relating to these commitments varies, but may include securities, equipment, accounts receivable, inventory and deeds of trust on residential real estate and owner-occupied or income-producing commercial properties.

Standby letters of credit, which totaled $1,723,000 and $1,846,000 at March 31, 2020 and December 31, 2019, respectively, are conditional commitments issued by the Bank to guarantee the performance of a client to a first party. The credit risk involved in issuing standby letters of credit is essentially the same as that involved in extending loans to clients. The fair value of the liability related to these standby letters of credit, which represents the fees received for issuing the guarantees, was not significant at March 31, 2020 and December 31, 2019. The Bank recognizes these fees as revenue over the term of the commitment or when the commitment is used.

4. FAIR VALUE

Accounting standards establish a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

> Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.
>
> Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
>
> Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The fair values of most securities available for sale are determined by matrix pricing, which is a mathematical technique widely used in the industry to value 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 (Level 2 inputs).

The fair value of impaired loans that are collateral dependent are generally based on 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 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.

Estimated fair values are disclosed for financial instruments for which it is practicable to estimate fair value. These estimates are made at a specific point in time based on relevant market data and information about the financial instruments. These estimates do not reflect any premium or discount that could result from offering the Bank's entire holdings of a particular financial instrument for sale at one time, nor do they attempt to estimate the value of anticipated future business related to the instruments. In addition, the tax ramifications related to the realization of unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of these estimates.

Because no active market exists for a significant portion of the Bank's financial instruments, fair value estimates are based on judgments regarding current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the fair values presented.

The following table presents a summary of the carrying value and fair value by level of financial instruments on the Bank's balance sheet at March 31, 2020 and December 31, 2019:

	March 31, 2020			December 31, 2019		
(in thousands)	Carrying Amount	Fair Value	Fair Value Hierarchy	Carrying Amount	Fair Value	Fair Value Hierarchy
Financial assets:						
Cash and due from banks	$ 36,493	$ 36,493	Level 1	$ 38,299	$ 38,299	Level 1
Investment securities - held-to-maturity	-	-	Level 2	7,998	7,981	Level 2
Investment securities - available-for-sale	58,160	58,160	Level 2	54,241	54,241	Level 2
Loans, net of allowance	601,400	610,782	Level 3	576,548	580,524	Level 3
Investment in Federal Home Loan Bank stock	3,342	3,342	Level 2	3,342	3,342	Level 2
Accrued interest receivable	2,082	2,082	Level 1	1,936	1,936	Level 1
Financial liabilities:						
Deposits	$574,006	$ 575,118	Level 2	$573,837	$573,502	Level 2
Federal Home Loan Bank advances	69,300	69,371	Level 2	45,600	45,730	Level 2
Junior subordinated debt	5,865	5,283	Level 3	5,862	5,574	Level 3
Accrued interest payable	230	230	Level 1	293	293	Level 1

Assets and Liabilities Measured on a Recurring Basis

Assets measured at fair value on a recurring basis are summarized below:

		Fair Value Measurements at March 31, 2020 (In thousands)		
	March 31, 2020	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Securities available-for-sale:				
Government agencies	$ 34,934	$ -	$ 34,934	$ -
Mortgage-backed securities - residential	8,740	-	8,740	-
Corporate debt	14,486	-	14,486	-
Total securities available-for-sale	$ 58,160	$ -	$ 58,160	$ -

		Fair Value Measurements at December 31, 2019 (In thousands)		
	December 31, 2019	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Securities available-for-sale:				
Government agencies	$ 39,887	$ -	$ 39,887	$ -
Mortgage-backed securities - residential	8,974	-	8,974	-
Corporate debt	5,380	-	5,380	-
Total securities available-for-sale	$ 54,241	$ -	$ 54,241	$ -

No liabilities were measured at fair value on a recurring basis at March 31, 2020 or December 31, 2019.

There were no transfers between Level 1 and Level 2 or Level 3 during the three months ended March 31, 2020 or 2019.

Assets and Liabilities Measured on a Non-Recurring Basis

There were no assets or liabilities measured at fair value on a non-recurring basis at March 31, 2020 and December 31, 2019.

5. INVESTMENT SECURITIES

The amortized costs and estimated fair value of investment securities are reflected in the tables below:

	March 31, 2020			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Held-to-maturity:				
Government agencies	$ -	$ -	$ -	$ -
Available-for-sale:				
Government agencies	$ 35,000	$ 39	$ (105)	$ 34,934
Mortgage-backed securities - residential	8,410	330	-	8,740
Corporate debt	15,280	16	(810)	14,486
Total available-for-sale	58,690	385	(915)	58,160
Total investment securities	$ 58,690	$ 385	$ (915)	$ 58,160

	December 31, 2019			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Held-to-maturity:				
Government agencies	$ 7,998	$ -	$ (17)	$ 7,981
Available-for-sale:				
Government agencies	$ 39,487	$ 574	$ (174)	$ 39,887
Mortgage-backed securities - residential	8,841	133	-	8,974
Corporate debt	5,263	132	(15)	5,380
Total available-for-sale	53,591	839	(189)	54,241
Total investment securities	$ 61,589	$ 839	$ (206)	$ 62,222

The activity related to recorded gross gains and losses of investment securities is reflected in the table below:

	Three Months Ended	
(in thousands)	**March 31, 2020**	**March 31, 2019**
Proceeds from sales	$ -	$ -
Proceeds from calls	39,621	-
Gross realized gains on sales and calls	871	-
Gross realized losses on sales and calls	-	-

There were no investment securities in a continuous unrealized loss position greater than 12 months at March 31, 2020 and two at December 31, 2019. At March 31, 2020 the Bank held thirty-six investment securities in an unrealized loss position for less than twelve months and at December 31, 2019 the Bank held eight investment securities in an unrealized loss for less than twelve months.

Management periodically evaluates each investment security for other-than-temporary impairment (OTTI), relying primarily on industry analyst reports and observation of market conditions and interest rate fluctuations. All of the impairment appearing in the investment securities portfolio valuations is considered to be temporary. The measured impairment in the securities values is primarily attributable to changes in short term interest rates, market shifts of the Treasury yield curve and other variable market and economic conditions. The measured impairment in securities values did not result from any significant or persistent deterioration in the underlying credit quality of any of the investments. The securities portfolio consists primarily of debt securities with non-contingent contractual cash flows. Full realization of the principal balance is expected upon final maturity. Management has the intent and ability to hold the securities until recovery of the carrying value, which could be at the final maturity. There was no OTTI recorded in 2020 or 2019.

Investment securities with unrealized losses are summarized and classified according to the duration of the loss period as follows:

	March 31, 2020					
	Less than 12 Months		12 Months or More		Total	
(in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Debt securities:						
Held-to-maturity:						
Government agencies	$ -	$ -	$ -	$ -	$ -	$ -
Available-for-sale:						
Government agencies	$ 12,395	$ (105)	$ -	$ -	$12,395	$ (105)
Mortgage-backed securities - residential	-	-	-	-	-	-
Corporate debt	13,247	(810)	-	-	13,247	(810)
Total available-for-sale	25,642	(915)	-	-	25,642	(915)
Total investment securities	$ 25,642	$ (915)	$ -	$ -	$25,642	$ (915)

	December 31, 2019					
	Less than 12 Months		12 Months or More		Total	
(in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Debt securities:						
Held-to-maturity:						
Government agencies	$ 4,992	$ (5)	$ 2,989	$ (12)	$ 7,981	$ (17)
Available-for-sale:						
Government agencies	$ 17,769	$ (174)	$ -	$ -	$17,769	$ (174)
Corporate debt	-	-	235	(15)	235	(15)
Total available-for-sale	17,769	(174)	235	(15)	18,004	(189)
Total investment securities	$ 22,761	$ (179)	$ 3,224	$ (27)	$25,985	$ (206)

The amortized cost and estimated fair value of investment securities by contractual maturity at March 31, 2020 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.

	Available-for-Sale	
(in thousands)	Amortized Cost	Fair Value
Within one year	$ 1,222	$ 1,223
After one year through five years	5,339	5,108
After five years through ten years	13,719	13,162
After ten years	30,000	29,925
	50,280	49,418
Investment securities not due at a single maturity date:		
Mortgage-backed securities - residential	8,410	8,742
	$ 58,690	$ 58,160

6. LOANS

Outstanding loans are summarized as follows:

(in thousands)	March 31, 2020	December 31, 2019
Commercial & agricultural	$ 128,859	$ 129,590
Real estate - commercial	345,081	312,758
Real estate - construction and land	43,741	44,689
Real estate - single family	51,080	54,357
Real estate - multifamily	39,914	41,870
Consumer & lease financing	100	53
	608,775	583,317
Allowance for loan losses	(7,375)	(6,769)
	$ 601,400	$ 576,548

Changes in the allocation of allowance for loan losses by loan class for the three months ended March 31, 2020 and 2019 are as follows:

(in thousands)	Three Months Ended March 31, 2020				
	Balance at December 31, 2019	Provision (reversal)	Charge-offs	Recoveries	Balance at March 31, 2020
Commercial & agricultural	$ 887	$ 4	$ -	$ 6	$ 897
Real estate - commercial	1,976	1,272	-	-	3,248
Real estate - construction and land	1,602	48	-	-	1,650
Real estate - single family	323	(20)	-	-	303
Real estate - multifamily	510	8	-	-	518
Consumer & lease financing	2	2	-	-	4
Unallocated	1,469	(714)	-	-	755
Total	$ 6,769	$ 600	$ -	$ 6	$ 7,375

(in thousands)	Three Months Ended March 31, 2019				
	Balance at December 31, 2018	Provision (reversal)	Charge-offs	Recoveries	Balance at March 31, 2019
Commercial & agricultural	$ 904	$ 31	$ -	$ 10	$ 945
Real estate - commercial	2,830	(25)	-	-	2,805
Real estate - construction and land	705	133	-	-	838
Real estate - single family	684	56	-	-	740
Real estate - multifamily	308	(26)	-	-	282
Consumer & lease financing	6	(5)	-	-	1
Unallocated	592	(64)	-	-	528
Total	$ 6,029	$ 100	$ -	$ 10	$ 6,139

The following table presents the balance in the allowance for loan losses and loan balances by class and based on impairment method as of March 31, 2020 and December 31, 2019:

	March 31, 2020					
	Allowance for Loan Losses			Loans		
(in thousands)	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total Ending Allowance Balance	Loans Individually Evaluated for Impairment	Loans Collectively Evaluated for Impairment	Total Ending Loans Balance
Commercial & agricultural	$ 328	$ 569	$ 897	$ 576	$ 128,283	$ 128,859
Real estate - commercial	-	3,248	3,248	1,259	343,822	345,081
Real estate - construction and land	-	1,650	1,650	-	43,741	43,741
Real estate - single family	-	303	303	958	50,122	51,080
Real estate - multifamily	-	518	518	-	39,914	39,914
Consumer & lease financing	-	4	4	-	100	100
Unallocated	-	755	755	-	-	-
Total	$ 328	$ 7,047	$ 7,375	$ 2,793	$ 605,982	$ 608,775

	December 31, 2019					
	Allowance for Loan Losses			Loans		
(in thousands)	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total Ending Allowance Balance	Loans Individually Evaluated for Impairment	Loans Collectively Evaluated for Impairment	Total Ending Loans Balance
Commercial & agricultural	$ 330	$ 557	$ 887	$ 910	$ 128,680	$ 129,590
Real estate - commercial	-	1,976	1,976	1,277	311,481	312,758
Real estate - construction and land	-	1,602	1,602	-	44,689	44,689
Real estate - single family	-	323	323	963	53,394	54,357
Real estate - multifamily	-	510	510	-	41,870	41,870
Consumer & lease financing	-	2	2	-	53	53
Unallocated	-	1,469	1,469	-	-	-
Total	$ 330	$ 6,439	$ 6,769	$ 3,150	$ 580,167	$ 583,317

The recorded investment in the aforementioned disclosure and the next several disclosures do not include accrued interest receivable and net deferred fees because such amounts are not considered material. Accrued interest receivable for the total loan portfolio was $1,863,000 and $1,645,000 and net deferred loan fees were $714,000 and $268,000 as of March 31, 2020 and December 31, 2019, respectively.

The following table presents total impaired loans evaluated for impairment by class of loans:

(in thousands)	Commercial & agricultural	Real estate - commercial	Real estate - construction and land	Real estate - single family	Real estate - multifamily	Consumer & lease financing	Total
March 31, 2020							
Recorded investment in impaired loans:							
With no related allowance recorded	$ 156	$ 1,419	$ -	$ 958	$ -	$ -	$ 2,533
With an allowance recorded	420	-	-	-	-	-	420
Total recorded investment in impaired loans	$ 576	$ 1,419	$ -	$ 958	$ -	$ -	$ 2,953
Unpaid principal balance of impaired loans:							
With no related allowance recorded	$ 219	$ 1,702	$ -	$ 1,017	$ -	$ -	$ 2,938
With an allowance recorded	421	-	-	-	-	-	421
Total unpaid principal balance of impaired loans	$ 640	$ 1,702	$ -	$ 1,017	$ -	$ -	$ 3,359
Allowance for loan losses allocation	$ 328	$ -	$ -	$ -	$ -	$ -	$ 328
Average recorded investment in impaired loans during the quarter ended March 31, 2020	578	1,433	-	1,019	-	-	3,030
Interest income recognized on impaired loans during the quarter ended March 31, 2020	7	16	-	16	-	-	39
December 31, 2019							
Recorded investment in impaired loans:							
With no related allowance recorded	$ 488	$ 1,441	$ -	$ 964	$ -	$ -	$ 2,893
With an allowance recorded	307	-	-	88	-	-	395
Total recorded investment in impaired loans	$ 795	$ 1,441	$ -	$ 1,052	$ -	$ -	$ 3,288
Unpaid principal balance of impaired loans:							
With no related allowance recorded	$ 612	$ 1,717	$ -	$ 1,023	$ -	$ -	$ 3,352
With an allowance recorded	307	-	-	88	-	-	395
Total unpaid principal balance of impaired loans	$ 919	$ 1,717	$ -	$ 1,111	$ -	$ -	$ 3,747
Allowance for loan losses allocation	$ 330	$ -	$ -	$ -	$ -	$ -	$ 330
March 31, 2019							
Allowance for loan losses allocation	$ 366	$ -	$ -	$ -	$ -	$ -	$ 366
Average recorded investment in impaired loans during the quarter ended March 31, 2019	1,000	1,505	-	1,082	108	-	3,695
Interest income recognized on impaired loans during the quarter ended March 31, 2019	13	1	-	13	-	-	27

The following table presents the recorded investment in nonaccrual loans and loans past due over 90 days still accruing by class of loans as of March 31, 2020 and December 31, 2019:

(in thousands)	March 31, 2020 Nonaccrual	March 31, 2020 Loans Past Due Over 90 Days Still Accruing	December 31, 2019 Nonaccrual	December 31, 2019 Loans Past Due Over 90 Days Still Accruing
Commercial & agricultural	$ 114	$ -	$ -	$ -
Real estate - commercial	302	-	315	-
Real estate - construction and land	-	-	-	-
Real estate - single family	-	-	-	-
Real estate - multifamily	-	-	-	-
Consumer & lease financing	-	-	-	-
Total	$ 416	$ -	$ 315	$ -

The following table presents the aging of the recorded investment in past due loans, inclusive of nonaccrual loans, as of March 31, 2020 by class of loans:

(in thousands)	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial & agricultural	$ -	$ -	$ 167	$ 167	$ 128,692	$ 128,859
Real estate - commercial	-	88	-	88	344,993	345,081
Real estate - construction and land	-	-	-	-	43,741	43,741
Real estate - single family	-	-	-	-	51,080	51,080
Real estate - multifamily	-	-	-	-	39,914	39,914
Consumer & lease financing	-	-	-	-	100	100
Total	$ -	$ 88	$ 167	$ 255	$ 608,520	$ 608,775

The following table presents the aging of the recorded investment in past due loans, inclusive of nonaccrual loans, as of December 31, 2019 by class of loans:

(in thousands)	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial & agricultural	$ 146	$ -	$ -	$ 146	$ 129,444	$ 129,590
Real estate - commercial	-	-	315	315	312,443	312,758
Real estate - construction and land	-	-	-	-	44,689	44,689
Real estate - single family	-	-	-	-	54,357	54,357
Real estate - multifamily	-	-	-	-	41,870	41,870
Consumer & lease financing	-	-	-	-	53	53
Total	$ 146	$ -	$ 315	$ 461	$ 582,856	$ 583,317

A loan is considered past due if a scheduled payment of interest or principal that is due is unpaid for 30 days or more.

Troubled Debt Restructurings

From time to time, the Bank may agree to modify the contractual terms of a borrower's loan. In cases where such modifications represent a concession to a borrower experiencing financial difficulty, the modification is considered a troubled debt restructuring ("TDR"). At March 31, 2020 and December 31, 2019, loans modified in a TDR totaled $2,373,000 and $2,729,000 which are included in the impaired loan disclosures above. The total TDRs includes $141,000 and $151,000 that are also included in nonperforming loans at March 31, 2020 and December 31, 2019. TDRs had specific loss allocations of $0 as of March 31, 2020, December 31, 2019 and March 31, 2019.

There were no loans modified as troubled debt restructurings during the three months ended March 31, 2020 and March 31, 2019.

There were no loans modified as troubled debt restructurings for which there was a payment default within twelve months following the modification during the three months ended March 31, 2020 and 2019. A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms.

In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Bank's internal underwriting policy.

In accordance with Section 4013 of the CARES Act and related interagency policy statements, financial institutions may elect to not apply GAAP requirements to loan modifications related to the COVID-19 pandemic that would otherwise be categorized as a troubled debt restructuring. This applies to modifications of loans that were not more than 30 days past due as of December 31, 2019 and that occur beginning on March 1, 2020, until the earlier of 60 days after the COVID-19 national emergency is terminated or as of December 31, 2020. In the first quarter of 2020 the Bank modified 18 loans due to the COVID-19 pandemic; 15 of these loans were current and 3 of these loans were less than 15 days past due as of March 31, 2020. This suspension is not applicable to the Bank since none of these loan modifications qualify as a TDR under regular circumstances under Section 4013.

Credit Quality Indicators

The Bank categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Bank analyzes loans individually by classifying the loans as to credit risk. This analysis is performed on a quarterly basis for loans in excess of $250,000. Smaller balances are graded at origination and updated based on payment status and other information obtained from borrowers. The Bank uses the following definitions for risk ratings:

PASS - Loans not meeting any of the three criteria below that are analyzed individually as part of the above described process are considered to be pass rated loans.

SPECIAL MENTION - Loans in this category are considered "criticized" from a regulatory point of view but are not considered "classified" until the risk classification becomes substandard or worse. Loans in this category represent above average risk and potential weakness which may, if not corrected, weaken the loan and threaten repayment at some future date.

SUBSTANDARD - Loans in this category have well defined weakness that jeopardize full repayment of the debt, although loss may not seem likely. Loss potential does not have to exist in individual loans in the Substandard classification but will be apparent in the aggregate. Typically, these loans have not met repayment plans as agreed. The primary source of repayment may have failed to materialize; repayment may be dependent on collateral liquidation or other secondary sources. Bankrupt borrowers and those with continuously past due payments are considered substandard.

DOUBTFUL - Loans in this category have all the characteristics of substandard loans with the added weakness that payment in full or liquidation in full is highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors, which may work to the strengthening of the loan, its classification as an estimated loss is deferred until the amount of the loss may be more accurately determined.

As of March 31, 2020, the Special Mention category was attributable to the downgrade of one C&I relationship. The risk category of loans by class of loans as of March 31, 2020 is as follows:

(in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Commercial & agricultural	$ 110,792	$ 11,646	$ 6,421	$ -	$ 128,859
Real estate - commercial	343,835	-	1,246	-	345,081
Real estate - construction and land	43,741	-	-	-	43,741
Real estate - single family	50,910	-	170	-	51,080
Real estate - multifamily	39,914	-	-	-	39,914
Consumer & lease financing	100	-	-	-	100
Total	$ 589,292	$ 11,646	$ 7,837	$ -	$ 608,775

The risk category of loans by class of loans as of December 31, 2019 is as follows:

(in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Commercial & agricultural	$ 122,864	$ -	$ 6,726	$ -	$ 129,590
Real estate - commercial	312,443	-	315	-	312,758
Real estate - construction and land	44,689	-	-	-	44,689
Real estate - single family	54,185	-	172	-	54,357
Real estate - multifamily	41,870	-	-	-	41,870
Consumer & lease financing	53	-	-	-	53
Total	$ 576,104	$ -	$ 7,213	$ -	$ 583,317

7. FHLB ADVANCES

The Bank adjusts its level of FHLB advances outstanding to manage balance sheet liquidity. Each advance is payable at its maturity date, with a prepayment penalty for fixed rate advances. The advances were collateralized by $359,126,000 and $352,723,000 of loans under a blanket lien arrangement at March 31, 2020 and December 31, 2019. Based on this collateral the Bank was eligible to borrow up to a total of $214,251,000 and $223,944,000 of which $144,951,000 and $148,644,000 was available for additional advances as of March 31, 2020 and December 31, 2019.

Advances outstanding from the Federal Home Loan Bank were $69,300,000 at March 31, 2020, with maturities from April 2020 through February 2025 and fixed rates from 1.28% to 1.90%. Advances outstanding were $45,600,000 at December 31, 2019, with maturities from January 2020 through December 2024 and fixed rates from 1.57% to 1.90%.

At March 31, 2020, FHLB fixed rate advances are scheduled to mature as follows:

(in thousands)	Weighted Average Interest Rate	March 31, 2020
Due on or before March 31, 2021	0.21%	$ 20,800
Due on or before March 31, 2023	1.57%	$ 25,500
Due on or before March 31, 2025	1.65%	$ 23,000
		$ 69,300

8. LEASES

A lease is defined as a contract, or part of a contract, that conveys the right to control the use of identified property, plan or equipment for a period of time in exchange for consideration. On January 1, 2019, the Bank adopted ASU No. 2016-02 *"Leases"* (Topic 842) and all subsequent ASUs that modified Topic 842. For the Bank, Topic 842 primarily affected the accounting treatment for operating lease agreements in which the Bank is the lessee.

Lessee Accounting

The types of leases where the Bank is a lessee are real estate properties for four branches located in Healdsburg, Rohnert Park, Petaluma and Santa Rosa, office spaces in Santa Rosa, a lending office in Roseville and photocopier equipment. These leases have variable terms maturing prior to 2025. A majority of the leases are classified as operating leases and were previously not recognized on the Bank's statements of condition. With the adoption of Topic 842, operating lease agreements are required to be recognized on the statements of condition as a right-of-use ("ROU") asset and a corresponding lease liability.

The calculated amount of the ROU assets and lease liabilities in the table below are calculated by discounting the minimum contractual balance due of all future payments through the end of the current term to present value. When the Bank determines exercising the renewal option for any lease agreement is reasonably certain, it will include the extended term in the calculation of the ROU asset and lease liability.

As it pertains to the discount rate, Topic 842 requires the use of the rate implicit in the lease whenever this rate is readily determinable. As this rate is rarely determinable, the Bank uses its incremental borrowing rate in calculating the discounted present value.

The following table represents the statements of condition classification of the Bank's ROU assets and lease liabilities. The Bank elected not to include short-term leases (i.e., leases with initial terms of twelve months or less) on the statements of condition.

(in thousands)		March 31, 2020
Operating Leases	**Classification**	
Lease right-of-use assets	Accrued Int Rec & Other Assets	$ 798
Lease liabilities	Accrued Int Payable & Other Liabilities	812
Financing Leases		
Lease right-of-use assets	Bank Premises & Equip	$ 32
Lease liabilities	Accrued Int Payable & Other Liabilities	32

The following table represents lease costs for the three months ended March 31, 2020:

(in thousands)	March 31, 2020
Lease Costs	
Operating lease cost	$ 106
Financing lease cost	
Interest on lease liabilities	-
Amortization of right-of-use assets	3
Sublease income	(87)
Net lease cost	$ 22

(in thousands)	March 31, 2020
Other Information	
Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows from operating leases	$ 104
Operating cash flows from finance leases	-
Financing cash flows from finance leases	3

	March 31, 2020
Weighted-average remaining lease term	
Operating leases	4.3 years
Financing leases	2.7 years
Weighted-average discount rate	
Operating leases	2.83%
Financing leases	2.87%

Rent expense for the three months ended March 31, 2019 was $112,000

Future minimum payments for finance leases and operating leases as of March 31, 2020 were as follows:

(in thousands)

Twelve Months Ended:	Operating Leases	Financing Leases
March 31, 2021	$ 275	$ 13
March 31, 2022	220	13
March 31, 2023	227	9
March 31, 2024	233	4
March 31, 2025	159	1
Thereafter	17	-
Total Future Minimum Lease Payments	1,131	40
Amounts Representing Interest	(71)	(1)
Present Value of Net Future Minimum Lease Payments	$ 1,060	$ 39

9. OTHER EXPENSES

Other expenses consisted of the following:

	Three Months Ended	
(in thouands)	March 31, 2020	March 31, 2019
Data processing	$ 451	$ 332
Professional fees	220	135
Director fees and expenses	119	129
Nasdaq listing and regulatory license expens	42	36
Advertising and promotion	168	201
Deposit and other insurance premiums	133	77
Telephone and postage	21	18
Other expenses	162	204
	$ 1,316	$ 1,132

10. SUBSEQUENT EVENT

Dividend

On April 27, 2020, the Board of Directors declared a $0.12 per common share cash dividend to shareholders of record at the close of business on May 15, 2020, to be paid on May 22, 2020.

Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion provides additional information about the financial condition of the Bank at March 31, 2020 and December 31, 2019, and results of operations for the three months ended March 31, 2020 and 2019. The following analysis should be read in conjunction with the financial statements of the Bank and the notes thereto appearing elsewhere in the report, which were prepared in accordance with U.S. Generally Accepted Accounting Principles. The interim financial information provided as of and for the three months ended March 31, 2020 and 2019 are unaudited. In the opinion of management of the Bank, the interim financial information presented reflects all adjustments (consisting solely of normal recurring accruals) considered necessary for a fair representation of the results of such periods.

All references to yields, cost of liabilities and net interest margin are annualized for the periods discussed.

Forward Looking Statements. This discussion includes forward-looking statements within the meaning of the "safe harbor" provisions of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that are based on the current beliefs of the Bank management as well as assumptions made by and information currently available to the Bank's management. When used in this discussion, the words "anticipate," "believe," "estimate," "expect," "should," "intend," "project," "may," "will," "would," variations of such words and words or phrases of similar meaning constitute forward-looking statements. Although the Bank believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct.

These forward-looking statements relate to, among other things, expectations regarding the business environment in which the Bank operates, projections of future performance, potential future performance, potential future credit experience, perceived opportunities in the market, and statements regarding the Bank's mission and vision. Factors which may cause actual results to vary from forward-looking statements include, but are not limited to, changes in interest rates, general economic and business conditions, changes in business strategy or development plans, changes in credit quality, the availability of capital to fund the expansion of our business, legislative and regulatory changes, government monetary and fiscal policies, real estate valuations, competition in the financial services industry, demographic changes, civil disturbances or terrorist threats or acts, or apprehension about the possible future occurrences of acts of this type, outbreak or escalation of hostilities in which the United States is involved, any declaration of war by the U.S. Congress or any other national or international calamity, crisis or emergency, and other risks referenced in this discussion.

This discussion contains certain forward-looking information about us. All statements other than statements of historical fact are forward-looking statements. Such statements involve inherent risks and uncertainties, many of which are difficult to predict and are generally beyond our control. We caution readers that a number of important factors could cause actual results to differ materially from those expressed in, implied or projected by, such forward-looking statements. Risks and uncertainties include, but are not limited to:

- lower revenues than expected;
- credit quality deterioration which could cause an increase in the provision for credit losses;
- competitive pressure among depository institutions increases significantly;
- the cost of additional capital is more than expected;
- a change in the interest rate environment reduces interest margins;
- asset/liability repricing risks and liquidity risks;

- legislative or regulatory requirements or changes adversely affecting our business;
- changes in the securities markets;
- general economic conditions, either nationally or in the market areas in which we do or anticipate doing business, are less favorable than expected;
- potential weakness of real estate collateral values;
- the economic and regulatory effects of the continuing war on terrorism and other events of war, including the wars in Iraq and Afghanistan;
- our ability to complete any future acquisitions, to successfully integrate acquired entities, or to achieve expected synergies and operating efficiencies within expected time-frames or at all;
- the integration of any future acquired businesses costs more, takes longer or is less successful than expected; and
- regulatory approvals for announced or future acquisitions cannot be obtained on the terms expected or on the anticipated schedule.

Also, other important factors that could cause actual results to differ materially from the Bank's expectations are disclosed under Item 1A. "RISK FACTORS," in our Annual Report on Form 10-K on file with the Federal Deposit Insurance Corporation ("FDIC") and below under this "MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS – *Critical Accounting Policies*" and elsewhere in this report.

If any of these risks or uncertainties materializes, or if any of the assumptions underlying such forward-looking statements proves to be incorrect, our results could differ materially from those expressed in, implied or projected by, such forward-looking statements. We assume no obligation to update such forward-looking statements.

We caution that these statements are further qualified by important factors, in addition to those under "Risk Factors" in our Annual Report on Form 10-K and elsewhere in this report, which could cause actual results to differ significantly from those in the forward-looking statements, including, among other things, economic conditions and other risks.

Forward-looking statements are not guarantees of performance. By their nature, they involve risks, uncertainties and assumptions. Our future results and shareholder values may differ significantly from those expressed in these forward-looking statements. You are cautioned not to put undue reliance on any forward-looking statement. Any such statement speaks only as of the date of this discussion, regardless of the time of delivery of this document. We do not undertake any obligation to update or release any revisions to any forward-looking statements, to report any new information, future event or other circumstances after the date of this filing or to reflect the occurrence of unanticipated events, except as required by law. However, your attention is directed to any further disclosures made on related subjects in any subsequent reports we may file with the FDIC, including on Forms 10-K, 10-Q and 8-K.

Government and Regulatory Oversight. The Bank is subject to regulatory oversight by the Department of Business Oversight (DBO) from the state of California and the Federal Deposit Insurance Corporation (FDIC). These regulatory bodies periodically perform financial examinations of the Bank. There is a potential that an examination may derive different estimates than those reached by management and could require material adjustments or restatements.

Critical Accounting Policies. The discussion and analysis of the Bank's results of operations and financial condition are based upon financial statements which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires the Bank's management to make estimates and judgments that affect the reported amounts of assets and liabilities, income and expense, and the related disclosures of contingent assets and liabilities at the date of these financial statements.

The Bank believes these estimates and assumptions to be reasonably accurate; however, actual results may differ from these estimates under different assumptions or circumstances. Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan losses, consideration of goodwill impairment and consideration of potential other than temporary impairment on investment securities.

Allowance for Loan Losses. The allowance for loan losses is determined first and foremost by promptly identifying potential credit weaknesses that could jeopardize repayment. The Bank's process for evaluating the adequacy of the allowance for loan losses includes determining estimated loss percentages for each credit based on the Bank's historical loss experience and other factors in the Bank's credit grading system and accompanying risk analysis for determining an adequate level of the allowance. The risks are assessed by rating each account based upon paying habits, loan to collateral value ratio, financial condition and level of classifications. The allowance for loan losses was $7,375,000 at March 31, 2020 compared to $6,769,000 at December 31, 2019.

The Bank maintains the allowance for loan losses to provide for probable incurred losses in the loan portfolio. Additions to the allowance for loan losses are established through a provision charged to expense. All loans which are judged to be uncollectible are charged against the allowance while any recoveries are credited to the allowance. The Bank's policy is to charge off any known losses at the time of determination. Any unsecured loan more than 90 days delinquent in payment of principal or interest and not in the process of collection is charged off in total. Secured loans are evaluated on a case by case basis to determine the ultimate loss potential to the Bank subsequent to the liquidation of collateral. In those cases where management believes the Bank is inadequately protected, a charge-off will generally be made to reduce the loan balance to a level equal to the liquidation value of the collateral unless management believes the collateral deficiency may be overcome by borrower cash flows.

The Bank's loan policy provides procedures designed to evaluate and assess the credit risk factors associated with the loan portfolio, to enable the Bank to assess such credit risk factors prior to granting new loans and to evaluate the sufficiency of the allowance for loan losses. The Bank conducts an assessment of the allowance on a monthly basis and undertakes a more critical evaluation quarterly. At the time of the quarterly review, the Board of Directors will examine and formally approve the adequacy of the allowance. The quarterly evaluation includes an assessment of the following factors: any external loan review and any recent regulatory examination, estimated potential loss exposure on each pool of loans, concentrations of credit, value of collateral, the level of delinquent and nonaccrual loans, trends in loan volume, effects of any changes in lending policies and procedures, changes in lending personnel, current economic conditions at the local, state and national level and historical losses and recoveries. The refinement in methodology was a $1,800,000 increase in allocated reserves based on loss history and a $2,500,000 reduction in qualitative factor reserves. This refinement caused a one-time increase in the unallocated allowance at December 31, 2019 and the unallocated has subsequently reduced back down to historical levels beginning March 31, 2020.

Goodwill. Management assesses the carrying value of the Bank's goodwill at least annually in order to determine if this intangible asset is impaired. In reviewing the carrying value of the Bank's goodwill, management assesses the recoverability of such assets by evaluating the fair value of the related business unit. If the carrying amount of goodwill exceeds its fair value, an impairment loss is recognized for the amount of the excess and the carrying value of goodwill is reduced accordingly. Any impairment would be required to be recorded during the period identified.

Accounting standards require an annual evaluation of goodwill for impairment using various estimates and assumptions. The Bank typically performs its evaluation of goodwill for impairment at year end, as of December 31. The last evaluation performed by the Bank was as of December 31,

2020. Due to recent economic impacts caused by the COVID-19 pandemic, the Bank performed a goodwill assessment test as of March 31, 2020 to determine if conditions warrant a detailed impairment analysis to make a final determination. The fair value of the Bank's common stock at the close of business on March 31, 2020 was $7.99 per common share compared to a book value of $11.24 per common share. Although the Bank's stock price was below its book value, when considering other qualitative factors including increased stock price in Q2 2020, increase in net income when compared to prior quarters and uninterrupted operations throughout the pandemic, the price decline is considered a temporary suppression and the Bank concludes that goodwill is not impaired.

Investment Securities. Management assesses at each reporting date whether there is an "other-than-temporary" impairment to the Bank's investment securities. Such impairment, if related to credit losses, must be recognized in current earnings rather than in other comprehensive income or loss, net of tax. All individual securities that are in an unrealized loss position at each reporting date are examined for other-than-temporary impairment (OTTI). Specific investment level factors examined to assess impairment include the severity and duration of the unrealized loss, the nature, financial condition and results of operations of the issuers of the securities and whether there has been any cause for default on the securities or any adverse change in the rating of the securities by the various rating agencies, as well as whether the decline in value is credit or liquidity related. Additionally, the Bank's financial resources and overall intent and ability to hold the securities until their fair values recover is determined. There was no OTTI recorded in 2020 or 2019. Investment securities are discussed in more detail under "Investment Portfolio."

Application of New Accounting Guidance. In February of 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. This Update was issued to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The core principle of Topic 842 is that a lessee should recognize the assets and liabilities that arise from leases. All leases create an asset and a liability for the lessee in accordance with FASB Concepts Statement No. 6, Elements of Financial Statements, and, therefore, recognition of those lease assets and lease liabilities represents an improvement over previous GAAP, which did not require lease assets and lease liabilities to be recognized for most leases. For public companies, the amendments in this update are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Lease commitments will be reflected on the balance sheet as lease assets and lease liabilities. The Bank adopted this standard in January 2019.

In June of 2016, the FASB issued ASU No. 2016-13*, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. The amendments are intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The ASU requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. Organizations will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. The ASU requires enhanced disclosures to help investors and other financial statement users to better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio. These disclosures include qualitative and quantitative requirements that provide additional information about the amounts recorded in the financial statements. In addition, the ASU amends the accounting guidance for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. In October 2019 FASB updated the effective date for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2022. Early application will be permitted on January 1 for fiscal years beginning after December 15, 2018. In 2018 the Bank began running the Advanced Risk Consulting Expected Loss Model (ARC ELM) parallel to the current "incurred loss" model. The ARC ELM meets the "current expected credit loss" ("CECL") model standard by projecting expected net losses for loan pools with similar default risks over the lives of the loans under a defined set of short-term and long-term economic variables. The model further uses actual historical nonaccrual rates, gross charge-off rates and recovery rates that are modeled against key economic variables. The Bank began conducting formal tests of the ARC ELM model results against the existing incurred loss model in the first quarter of 2019. The Bank may elect to adopt the new CECL model before the effective date but currently has not determined if or when early adoption will occur. The CECL model will continue to run parallel until it is brought into live production; prior to going live the Bank will communicate the impact this new standard will have on the financial statements including the cumulative effect on retained earnings or other components of equity.

In March 2017, the FASB issued ASU No. 2017-08, *Receivables – Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities.* Under current GAAP, entities normally amortize the premium as an adjustment of yield over the contractual life of the instrument. This guidance shortens the amortization period for certain callable debt securities held at a premium to the earliest call date. This update is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The adoption of this ASU did not have a material impact on the Bank's financial statements.

In January of 2017, the FASB issued ASU No. 2017-04, *Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment.* The amendments are intended to simplify the subsequent measurement of goodwill, and the amendments eliminate Step 2 from the goodwill impairment test. The annual, or interim, goodwill impairment test is performed by comparing the fair value of a reporting unit with its carrying amount. An impairment charge should be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. In addition, income tax effects from any tax-deductible goodwill on the carrying amount of the reporting unit should be considered when measuring the goodwill impairment loss, if applicable. The amendments also eliminate the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The amendments should be applied on a prospective basis. The nature of and reason for the change in accounting principle should be disclosed upon transition. The amendment is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early application will be permitted for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. Management does not anticipate any significant impact from the new standard on our financial statements.

In April 2019, the FASB issued ASU No. 2019-04, *Codification Improvements to Topic 326, Financial Instruments - Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments.* With respect to Topic 815, Derivatives and Hedging, ASU 2019-04 clarifies that the reclassification of a debt security from held-to-maturity ("HTM") to available-for-sale ("AFS") under the transition guidance in ASU 2017-12 would not (1) call into question the classification of other HTM securities, (2) be required to actually designate any reclassified security in a last-of-layer hedge, or (3) be restricted from selling any reclassified security. As part of the transition of ASU 2019-04, entities may reclassify securities that would qualify for designation as the hedged item in a last-of-layer hedging relationship from HTM to AFS; however, entities that already made such a reclassification upon their adoption of ASU 2017-12 are precluded from reclassifying additional securities. Management is in the process of evaluating the impact of this standard in connection with its adoption of ASU 2016-13.

In May 2019, the FASB issued ASU No. 2019-05, *Financial Instruments - Credit Losses (Topic 326); Targeted Transition Relief.* This ASU allows entities to irrevocably elect, upon adoption of ASU 2016-13, the fair value option on financial instruments that (1) were previously recorded at amortized cost and (2) are within the scope of ASC 326-20 if the instruments are eligible for the fair value option under ASC 825-10. The fair value option election does not apply to held-to-maturity debt securities. Entities are required to make this election on an instrument-by-instrument basis. ASU 2019-05 has the same effective date as ASU 2016-13. Management does not anticipate any potential impact from the new standard on our financial statements.

Financial Summary
(Dollars in thousands except per share data)

	As of and for the Three Months Ended	
	March 31, 2020 (Unaudited)	March 31, 2019 (Unaudited)
Statement of Income Data:		
Net interest income	$ 6,525	$ 5,547
Provision for loan losses	600	100
Non-interest income	1,929	493
Non-interest expense	4,422	4,212
Provision for income taxes	1,017	303
Net income	$ 2,415	$ 1,425
Selected per Common Share Data:		
Basic earnings per common share	$ 0.40	$ 0.23
Diluted earnings per common share	$ 0.40	$ 0.23
Dividend per share	$ 0.12	$ 0.12
Book value per common share (2)	$ 11.24	$ 10.44
Selected Balance Sheet Data:		
Assets	$ 721,645	$ 626,290
Loans, net	601,400	509,989
Deposits	574,006	555,255
Average assets	688,842	627,931
Average earning assets	673,731	616,014
Average shareholders' equity	68,569	62,388
Nonperforming loans	416	736
Total nonperforming assets	416	736
Troubled debt restructures (accruing)	2,231	2,472
Selected Ratios:		
Return on average assets (1)	1.41%	0.92%
Return on average common shareholders' equity (	14.13%	9.26%
Efficiency ratio (3)	58.31%	69.74%
Net interest margin (1)	3.88%	3.65%
Common equity tier 1 capital ratio	10.30%	10.70%
Tier 1 capital ratio	10.30%	10.70%
Total capital ratio	12.50%	11.80%
Tier 1 leverage ratio	9.30%	9.60%
Common dividend payout ratio (4)	30.14%	51.09%
Average shareholders' equity to average assets	9.95%	9.94%
Nonperforming loans to total loans	0.07%	0.14%
Nonperforming assets to total assets	0.06%	0.12%
Allowance for loan losses to total loans	1.21%	1.19%
Allowance for loan losses to nonperforming loans	1774.05%	834.24%

(1) Annualized.

(2) Total shareholders' equity divided by total common shares outstanding.

(3) Non-interest expenses to net interest and non-interest income, net of securities gains.

(4) Common dividends divided by net income available for common shareholders.

Results of Operations

Three months ended March 31, 2020 and March 31, 2019

The Bank's primary source of income is net interest income, which is the difference between interest income and fees derived from earning assets and interest paid on liabilities which fund those assets. Net interest income, expressed as a percentage of total average interest earning assets, is referred to as the net interest margin. The Bank's net interest income is affected by changes in the volume and mix of interest earning assets and interest-bearing liabilities. It is also affected by changes in yields earned on interest earning assets and rates paid on interest bearing deposits and other borrowed funds. The Bank also generates non-interest income, including transactional fees, service charges, office lease income and gains and losses on loans and investment securities. Non-interest expenses consist primarily of employee compensation and benefits, occupancy and equipment expenses and other operating expenses. The Bank's results of operations are also affected by its provision for loan losses. Results of operations may also be significantly affected by other factors including general economic and competitive conditions, mergers and acquisitions of other financial institutions within the Bank's market area, changes in market interest rates, government policies, and actions of regulatory agencies.

Net Income

A summary of the net income and annualized ratios are as follows:

	Three Months Ended		
(Dollars in thousands)	March 31, 2020	March 31, 2019	Change
Net income	$ 2,415	$ 1,425	$ 990
Earnings per diluted share	$ 0.40	$ 0.23	$ 0.17
Annualized return on average assets	1.41%	0.92%	0.49%
Annualized return on average common shareholders' equity	14.13%	9.26%	4.87%

Net Interest Income and Net Interest Margin

Net interest income increased $978,000 or 18% to $6,525,000 for the first quarter of 2020 compared to $5,547,000 for the same quarter of 2019. The annualized net interest margin was 3.88% for the first quarter of 2020, compared to 3.65% for the same period of 2019.

Average earning assets increased 9% to $673,731,000 for the first quarter of 2020, as compared to $616,014,000 for the same quarter of 2019. The annualized yield on average earning assets was 4.94% and the annualized cost of average interest-bearing liabilities was 1.46% for the first quarter of 2020, as compared to the annualized yield on average earning assets of 4.74% and annualized cost of interest-bearing liabilities of 1.50% for the same quarter of 2019.

The increase in net interest income for the quarter was attributable to higher volume of average earning assets and higher average yields on those assets increased more than the increase in interest-bearing liabilities and the cost of interest-bearing liabilities for the first quarter.

The following table presents condensed average balance sheet information for the Bank, together with interest rates earned and paid on the various sources and uses of its funds for each of the periods presented. Average balances are based on daily average balances. Nonaccrual loans are included in loans with any interest collected reflected on a cash basis.

	Three Months Ended March 31, 2020			Three Months Ended March 31, 2019		
(Dollars in thousands)	Average Balance	Interest Income/ Expense	Average Rate (4)	Average Balance	Interest Income/ Expense	Average Rate (4)
Assets						
Interest earning assets:						
Interest-bearing deposits with banks	$ 15,905	$ 44	1.11%	$ 21,184	$ 101	1.93%
Taxable investment securities	55,725	369	2.66%	78,071	590	3.06%
Dividends on FHLB Stock	3,342	59	7.08%	3,085	54	7.10%
Loans, net of unearned income (1)	598,759	7,820	5.24%	513,674	6,452	5.09%
Total earning assets/interest income	673,731	8,292	4.94%	616,014	7,197	4.74%
Non-earning assets	21,983			18,006		
Allowance for loan losses	(6,872)			(6,089)		
Total assets	$ 688,842			$ 627,931		
Liabilities and Shareholders' Equity						
Interest-bearing liabilities:						
Deposits:						
Interest-bearing demand deposits	$ 68,799	$ 30	0.17%	$ 65,038	$ 20	0.12%
Savings and money market	153,588	337	0.88%	132,272	250	0.77%
Time deposits	198,391	1,078	2.18%	219,424	1,201	2.22%
FHLB advances	58,336	228	1.57%	28,491	179	2.55%
Subordinated Debt	5,863	94	6.43%	-	-	0.00%
Total interest-bearing liabilities/interest exp	484,977	1,767	1.46%	445,225	1,650	1.50%
Non interest-bearing deposits	132,377			117,394		
Other liabilities	2,919			2,924		
Total liabilities	620,273			565,543		
Shareholders' equity	68,569			62,388		
Total liabilities and shareholders' equity	$ 688,842			$ 627,931		
Net interest income and margin (2)		$ 6,525	3.88%		$ 5,547	3.65%
Net interest spread (3)			3.48%			3.24%

(1) The net amortization of deferred costs on loans included in interest income was $101,000 and $19,000 for the three months ended March 31, 2020 and 2019.
(2) Net interest margin is computed by dividing net interest income by average total earning assets.
(3) Net interest spread is the difference between the average rate earned on average total earning assets and the average rate paid on average total interest-bearing liabilities.
(4) Annualized.

The following tables show the change in interest income and interest expense and the amount of change attributable to variances in volume and rates. The unallocated change in rate or volume variance has been allocated between the rate and volume variances in proportion to the absolute dollar amount of the change of each.

	Volume and Yield/Rate Variances 2020 Compared to 2019 for the Three Months Ended March 31		
	Change Due to		
(Dollars in thousands)	Net	Volume	Yield/Rate
Interest income:			
Interest-bearing deposits with banks	$ (57)	$ (29)	$ (28)
Taxable investment securities	(221)	(183)	(38)
Dividends on FHLB stock	5	5	-
Loans, net	1,368	1,103	265
Total interest income	1,095	896	199
Interest expense:			
Interest-bearing demand deposits	$ 10	$ 1	$ 9
Savings and money market	87	44	43
Time deposits	(123)	(116)	(7)
FHLB advances	49	135	(86)
Subordinated Debt	94	94	-
Total interest expense	117	158	(41)
Increase in net interest income	$ 978	$ 738	$ 240

Provision for Loan Losses

The Bank maintains an allowance for loan losses for probable incurred losses that are expected as an incidental part of the banking business. Write-offs of loans are charged against the allowance for loan losses, which is adjusted periodically to reflect changes in the volume of outstanding loans and estimated losses due to changes in the financial condition of borrowers or the value of property securing nonperforming loans, or changes in general economic conditions and other qualitative factors. Additions to the allowance for loan losses are made through a charge against income referred to as the “provision for loan losses” or recoveries of previous write-offs.

The Bank’s loan policy provides procedures designed to evaluate and assess the credit risk factors associated with the loan portfolio, to enable management to assess such credit risk factors prior to granting new loans and to evaluate the sufficiency of the allowance for loan losses. Management conducts an assessment of the allowance for loan losses on a monthly basis and undertakes a more critical evaluation quarterly. At the time of the quarterly review, the Board of Directors evaluates and formally approves the adequacy of the allowance. The quarterly evaluation includes an assessment of the following factors: any external loan review and regulatory examination, estimated probable loss exposure on each pool of loans, concentrations of credit, value of collateral, the level of delinquent and nonaccrual loans, trends in loan volume, effects of any changes in the lending policies and procedures, changes in lending personnel, current economic conditions and a migration analysis of historical losses and recoveries dating back to 2009 and going through 2106. Prior to this the Bank was calculating historical losses and recoveries for 2009 to current. The Bank also refined how it is measuring the change in current economic conditions to more accurately reflect economic trends and the impact this will have at the Bank. The refinement in methodology was a $1,800,000 increase in allocated reserves based on loss history and a $2,500,000 reduction in qualitative factor reserves as of December 31, 2020. Additionally, adjustments have been made to the qualitative factors to address uncertainty related to the COVID-19 pandemic resulting in an increase in the loan loss provision in Q1 2020.

There was a provision for loan losses for the three months ended March 31, 2020 of $600,000 compared to $100,000 for the three months March 31, 2019. The nonperforming loans to total loans ratio declined to 0.07% at March 31, 2020 compared to 0.14% at March 31, 2019. The nonperforming loans were primarily secured by real estate with minimal loss prospects. There were net recoveries of $6,000 during the three months ended March 31, 2020, compared to net recoveries of $10,000 for the three months ended March 31, 2019. See Balance Sheet Activity – Nonperforming Assets and Allowance for Loan Losses for additional discussion.

Future provisions for loan losses are dependent on asset quality trends, loan portfolio growth and the general condition of the economy. As a significant portion of the Bank's loan portfolio is collateralized by real estate, the valuation of the underlying collateral can have a significant impact on the adequacy of the allowance for loan losses and specific allocations for impaired loans, which may require future loan loss provisions.

Non-interest Income

The following are the sources of non-interest income for the periods indicated:

	Three Months Ended		
(in thousands)	March 31, 2020	March 31, 2019	Change
Service charges on deposit accounts	$ 214	$ 190	$ 24
Rental income	87	90	(3)
Net gain on loan sales	697	167	530
Net securities gains	871	-	871
Other income	60	46	14
Total non-interest income	$ 1,929	$ 493	$ 1,436

The increase in net gains on loan sales for the three months ended March 31, 2020 were due to increased loan sale activity on SBA guaranteed loans. The increase in securities gains during the first quarter 2020 compared to 2019 were due to called securities.

Non-interest Expense

The following are the sources of non-interest expense for the periods indicated:

	Three Months Ended		
(in thousands)	March 31, 2020	March 31, 2019	Change
Salaries and employee benefits	$ 2,723	$ 2,657	$ 66
Occupancy and equipment	383	423	(40)
Other expenses	1,316	1,132	184
Total non-interest expense	$ 4,422	$ 4,212	$ 210

Non-interest operating expenses increased $210,000 between the first quarters of 2020 and 2019. The increase during the three month periods was due to an increase in the 401(k) match and increased incentive pay. Occupancy expense decreased due to termination of Santa Rosa administrative office lease. The difference in other expenses was due to an increase in Data Processing expense and FDIC insurance expense.

Provision for Income Taxes

The Bank accrues income tax expense based on the anticipated annual tax rates during the financial period covered. The provision for income taxes for Federal and State corporate income tax and effective rates for the three months ended March 31, 2020 was $1,017,000 (29.6%) compared to $303,000 (17.5%) for the same period in 2019. The decline in the effective tax rate in 2019 was due to a one-time tax benefit recorded from the installation of solar panels.

Balance Sheet Activity

At March 31, 2020 and December 31, 2019

Investment Portfolio

Securities classified as available-for-sale for accounting purposes are recorded at their fair value on the balance sheets. Available-for-sale (AFS) investment securities carried at fair value totaled $58,160,000 at March 31, 2020 and comprised 8.1% of total assets. At March 31, 2020, the Bank had no investment securities classified as held-to-maturity. At December 31, 2019, investment securities comprised 7.8% of total assets with AFS investments at a fair value of $54,241,000 and amortized cost of $53,591,000. Held-to-maturity investments at December 31, 2019 were carried at amortized cost of $7,998,000 and had a fair value of $7,981,000. Changes in the fair value of AFS securities (e.g., unrealized holding gains or losses) are reported as "other comprehensive income (loss)," net of tax, and carried as accumulated other comprehensive income or loss, net of tax, within shareholders' equity until realized, unless any declines in value below amortized cost are the result of other than temporary impairment. The held-to-maturity investments are government agency callable securities with step-up interest rates.

There were $45,000,000 in bonds purchased during the three months ended March 31, 2020, $48,615,000 in bonds called or matured and no bonds sold. For the three months ended March 31, 2019, there were no bonds purchased, $1,083,000 in bonds were called or matured and no bonds sold. There were net gains of $871,000 on the called bonds for the three months ended March 31, 2020. There were no net gains on the called bonds for the three months ended March 31, 2019.

The Bank utilizes the investment portfolio to manage liquidity and attract funding that requires collateralization. At March 31, 2020, investment securities with a fair value of $5,030,000 were pledged to secure time deposits from the State of California and other public deposits and represented 9% of the investment portfolio. At December 31, 2019, investment securities with a fair value of $6,000,000, or 9% of the investment portfolio, were pledged. At March 31, 2020 investment securities with a fair value of $35,184,000 were callable within one year.

The Bank does not own securities of any single issuer (other than U.S. Government agencies) whose aggregate book value was in excess of 10% of the Bank's total shareholders' equity at the time of purchase.

Loan Portfolio

The following table shows the composition of the loan portfolio by amount, percentage of total loans for each major loan category and the dollar volume and percentage change between the dates indicated.

(in thousands)	March 31, 2020	%	December 31, 2019	%	Net Change	Percent Change
Commercial & agricultural (1)	$ 128,859	21.2%	$ 129,590	22.2%	$ (731)	(0.6)%
Real estate - commercial	345,081	56.7%	312,758	53.6%	32,323	10.3%
Real estate - construction and land	43,741	7.2%	44,689	7.7%	(948)	(2.1)%
Real estate - single family	51,080	8.4%	54,357	9.3%	(3,277)	(6.0)%
Real estate - multifamily	39,914	6.6%	41,870	7.2%	(1,956)	(4.7)%
Consumer & lease financing	100	0.0%	53	0.0%	47	88.7%
	608,775	100%	583,317	100%	25,458	4.4%
LESS:						
Allowance for Loan Losses	(7,375)		(6,769)		(606)	9.0%
Total Loans, Net	$ 601,400		$ 576,548		$ 24,852	4.3%

(1) Includes loans secured by farmland.

Gross loans increased $25,458,000 (4.4%) to $608,775,000 at March 31, 2020 from December 31, 2019. The increase was predominantly in the real estate secured - commercial loan category.

At March 31, 2020, the Bank had approximately $75,350,000 in undisbursed loan commitments, of which approximately $33,471,000 were commercial and agricultural and $41,854,000 related to real estate loan types. At December 31, 2019, the Bank had approximately $68,545,000 in undisbursed loan commitments, of which approximately $35,201,000 were commercial and agricultural and $33,319,000 related to real estate loan types.

Nonperforming Assets

Nonperforming assets consist of nonperforming loans and other real estate owned. Nonperforming loans are those for which the borrower fails to perform under the terms of the obligation and consist of nonaccrual loans and accruing loans past due 90 days or more.

The following are the nonperforming assets for the respective periods:

(in thousands)	March 31, 2020	December 31, 2019
Nonaccrual loans	$ 416	$ 315
Accruing loans past due 90 days or more	-	-
Total nonperforming loans	416	315
Other real estate owned	-	-
Total nonperforming assets	$ 416	$ 315
Nonperforming loans to total loans	0.07%	0.05%
Nonperforming assets to total assets	0.06%	0.05%
Allowance for loan losses to nonperforming loans	1774.05%	2150.07%

The $416,000 in nonaccrual loans consist of three loans and are primarily secured by real estate collateral. The nonperforming loans represent 0.06% of total assets at March 31, 2020.

Loans that are classified as TDRs were $2,373,000 at March 31, 2020, of which $2,231,000 were considered performing loans and $141,000 are nonperforming loans and are included in the table above.

Loans that are classified as TDRs were $2,729,000 at December 31, 2019, of which $2,578,000 were considered performing loans and $150,000 are nonperforming loans and are included in the table above.

There was no other real estate owned (OREO) at March 31, 2020 or December 31, 2019.

Allowance for Loan Losses

The Bank maintains the allowance for loan losses to provide for inherent losses in the loan portfolio. Additions to the allowance for loan losses are established through a provision for loan losses charged to expense. All loans which are judged to be uncollectible are charged against the allowance while any recoveries are credited to the allowance. The Bank's policy is to charge off any known losses at the time of determination. Any unsecured loan more than 90 days delinquent in payment of principal or interest and not in the process of collection is charged off in total. Secured loans are evaluated on a case by case basis to determine the ultimate loss potential to us subsequent to the liquidation of collateral. In those cases where we believe we are inadequately protected, a charge off will be made to reduce the loan balance to a level equal to the liquidation value of the collateral.

The Bank's loan policy provides procedures designed to evaluate and assess the credit risk factors associated with the loan portfolio, to enable management to assess such credit risk factors prior to granting new loans and to evaluate the sufficiency of the allowance for loan losses. Management conducts an assessment of the allowance for loan losses on a monthly basis and undertakes a more critical evaluation quarterly. At the time of the quarterly review, the Board of Directors evaluates and formally approves the adequacy of the allowance. The quarterly evaluation includes an assessment of the following factors: any external loan review and regulatory examination, estimated probable incurred loss exposure on each pool of loans, concentrations of credit, value of collateral, the level of delinquent and nonaccrual loans, trends in loan volume, effects of any changes in lending policies and procedures, changes in lending personnel, current economic conditions at the local, state and national level and a migration analysis of historical losses and recoveries for the prior twelve quarters.

In addition to the allowance for loan losses, the Bank maintains a reserve for losses for undisbursed loan commitments which is reported in other liabilities on the balance sheets. This reserve was $600,000 as of March 31, 2020 and $700,000 as of December 31, 2019.

The following table summarizes the activity in the Allowance for Loan Losses during the periods indicated.

SUMMARY OF ACTIVITY IN ALLOWANCE FOR LOAN LOSSES

(Dollars in thousands)	Three Months Ended March 31, 2020	Year Ended December 31, 2019
Balance at beginning of period	$ 6,769	$ 6,029
Charge-offs:		
Commercial & agricultural	-	-
Real estate - commercial	-	-
Real estate - construction and land	-	-
Real estate - single family	-	-
Real estate - multifamily	-	-
Consumer & lease financing	-	-
Total loans charged-off	-	-
Recoveries:		
Commercial & agricultural	6	40
Real estate - commercial	-	-
Real estate - construction and land	-	-
Real estate - single family	-	-
Real estate - multifamily	-	-
Consumer & lease financing	-	-
Total recoveries	6	40
Net loans recovered	6	40
Provision for loan losses	600	700
Allowance for loan losses - end of period	$ 7,375	$ 6,769
Loans:		
Average loans outstanding during period, net of unearned income	$ 598,759	$ 542,630
Total loans at end of period, net of unearned income	$ 608,775	$ 583,317
Ratios:		
Net loans recovered to average net loans (1)	0.00%	0.01%
Net loans recovered to total loans (1)	0.00%	0.01%
Allowance for loan losses to average net loans	1.23%	1.25%
Allowance for loan losses to total loans	1.21%	1.16%
Net loans recovered to beginning allowance for loan losses (1)	0.36%	0.66%
Net loans recovered to provision for loan losses	1.00%	5.71%

(1) Annualized

Allocation of Allowance for Loan Losses

(in thousands)	March 31, 2020 Allowance Allocation	March 31, 2020 Amount of Category Loans to Total Loans	December 31, 2019 Allowance Allocation	December 31, 2019 Amount of Category Loans to Total Loans
Commercial & agricultural	$ 897	21.2%	$ 887	22.2%
Real estate - commercial	3,248	56.7%	1,976	53.6%
Real estate - construction and land	1,650	7.2%	1,602	7.7%
Real estate - single family	303	8.4%	323	9.3%
Real estate - multifamily	518	6.6%	510	7.2%
Consumer & lease financing	4	0.0%	2	0.0%
Unallocated	755		1,469	
Total	$ 7,375	100%	$ 6,769	100%

The allowance allocation to real estate loan categories is highly dependent on the estimated real estate collateral values that secure specific troubled loans. The specific loans being evaluated at one period versus another can result in variations in the allocations. The increase in allowance allocated to Commercial & agricultural, Real estate - construction and land and Real estate - multifamily loans was attributable to the increase in the amount of loans in each category. The decline in allowance allocated to Real estate - commercial and Real estate - single family loans was due to the decline in loans with specific allocations.

Part of the allocation of the allowance for loan losses is based on other qualitative factors and is attributable to management's assessment of various qualitative factors. Qualitative factors included the size of individual credits, concentrations and general economic conditions. Management also considers these qualitative factors in their evaluation of the adequacy of the allowance for loan losses. An unallocated allowance can arise from fluctuations in the amount of classified and nonperforming loans ("changes in credit grades") between periods. The Internal Asset Review Committee reviews the amount and reasons for unallocated allowances and whether it has arisen due to periodic fluctuations in the credit grades or has arisen due to changes in qualitative factors or changes in lending strategies. If the unallocated allowance has arisen from other than periodic fluctuations in credit grades, then the Internal Asset Review Committee may determine that a portion of the allowance for loan losses should be reversed. Factors used in determining whether the unallocated allowance should be maintained includes the trend in impaired and classified loans, the projected increase in new loans and additional allowance that may be attributed to recoveries of previously charged-off loans.

The unallocated allowance represents temporary changes in allocations resulting from changes in loan volumes, types and quality, as well as other factors. Management assesses the unallocated amount to determine if the amount is due to other than temporary changes in these factors. The unallocated allowance relates to the trend in impaired and classified loans and additional allowance that may be attributed to recoveries of previously charged-off loans.

Deposits

At March 31, 2020, the Bank had a deposit mix of 38% in time deposits, 26% in money market and savings accounts, and 36% in demand accounts. At December 31, 2019, the Bank had a deposit mix of 38% in time deposits, 27% in money market and savings accounts, and 35% in demand accounts.

At March 31, 2020, the State of California had no time deposits with the Bank compared to $27,000,000 at December 31, 2019. These deposits are received through a program run by the Treasurer of the State of California to place public deposits with community banks. The interest rates are tied to the U.S. Treasury three or nine month rate at the origination of the time deposit.

At March 31, 2020, the Bank had $34,885,000 in wholesale brokered deposits compared to $22,500,000 at December 31, 2019.

The Bank also obtains time deposits through an internet listing service. These deposits are primarily from other financial institutions. There were $27,312,000 and $3,921,000 of internet obtained deposits at March 31, 2020 and December 31, 2019, respectively.

Liquidity and Capital Resources

Maintenance of adequate liquidity requires that sufficient resources be available at all times to meet cash flow requirements of the Bank. Liquidity in a banking institution is required primarily to provide for deposit withdrawals and the credit needs of customers and to take advantage of investment opportunities as they arise. A bank may achieve desired liquidity from both assets and liabilities. Cash and deposits held in other banks, Federal funds sold, other short-term investments, maturing loans and investments, payments of principal and interest on loans and investments, and potential loan and investment securities sales are sources of asset liquidity. Deposit growth and access to credit lines established with correspondent banks, primarily with the FHLB, Federal Reserve and access to brokered certificates of deposit are sources of liability liquidity. The Bank reviews its liquidity position on a regular basis based upon its current position and expected trends of loans and deposits. Management believes that the Bank maintains adequate sources of liquidity to meet its liquidity needs.

The Bank is able to borrow from the Federal Reserve Discount Window by pledging investment securities or loans. The amount that is available is dependent on the value of the assets pledged, as of March 31, 2020 the value of the pledges were approximately $5,000,000.

The Bank's liquid assets, defined as cash and cash equivalents, deposits with banks, Federal funds sold and the market value of unpledged available-for-sale investment securities, totaled $89,623,000 and constituted 12% of total assets at March 31, 2020 compared to $94,647,000 or 14% of total assets at December 31, 2019.

At March 31, 2020 the Bank had $214,251,000 in borrowing lines of credit from the FHLB and correspondent banks with $69,300 in FHLB outstanding advances. At December 31, 2019, these lines of credit available were $223,944,000 with $45,600,000 in FHLB advances outstanding.

Cash was primarily provided in the first three months of 2020 by $43 million in call and maturities of investment securities, $36 million in FHLB long term advances and $13 million in proceeds from sales of loans. Cash was used in the first three months of 2020 to purchase $45 million in new investment securities, fund $37 million in new changes to loans and payoff $12 million in FHLB short term advances.

Cash was primarily provided in the first three months of 2019 by $50.5 million in certificates of deposits, $3.5 million increase in demand, savings and money market deposits, $3.1 million in proceeds from sales of loans and $1.1 million in calls and maturities of investment securities. Cash was used in the first three months of 2019 to pay off $52.1 million in FHLB advances and fund $8.1 million net change in loans.

The Bank will be participating in the Paycheck Protection Program ("PPP") and is anticipated to produce about $90,000,000 in PPP loans in addition to the Bank's existing loan growth goals. The PPP loans will be funded through the Bank's growth in deposits and the Federal Reserve's PPP Liquidity Facility (PPPLF) program which uses term financing backed by the Bank's PPP loans.

Additional information on the Bank's cash flows can be reviewed in the *Statement of Cash Flows* in Part I, Item 1 of this report.

The following table presents the capital ratios for Summit State Bank and the correspondent regulatory minimum requirements:

	March 31, 2020		December 31, 2019	
(in thousands)	Amount	Ratio	Amount	Ratio
Common Equity Tier 1 Capital Ratio				
Summit State Bank	$ 63,518	10.3%	$ 62,071	10.2%
Minimum requirement with capital conservation buffer	$ 43,023	7.0%	$ 42,472	7.0%
Minimum requirement for "Well-Capitalized" institution	$ 39,950	6.5%	$ 39,438	6.5%
Minimum regulatory requirement	$ 27,657	4.5%	$ 27,303	4.5%
Tier 1 Capital Ratio				
Summit State Bank	$ 63,518	10.3%	$ 62,071	10.2%
Minimum requirement with capital conservation buffer	$ 52,242	8.5%	$ 51,573	8.5%
Minimum requirement for "Well-Capitalized" institution	$ 49,169	8.0%	$ 48,539	8.0%
Minimum regulatory requirement	$ 36,877	6.0%	$ 36,404	6.0%
Total Capital Ratio				
Summit State Bank	$ 76,958	12.5%	$ 74,986	12.4%
Minimum requirement with capital conservation buffer	$ 64,534	10.5%	$ 63,708	10.5%
Minimum requirement for "Well-Capitalized" institution	$ 61,461	10.0%	$ 60,674	10.0%
Minimum regulatory requirement	$ 49,169	8.0%	$ 48,539	8.0%
Tier 1 Leverage Ratio				
Summit State Bank	$ 63,518	9.3%	$ 62,071	9.3%
Minimum requirement for "Well-Capitalized" institution	$ 34,189	5.0%	$ 33,510	5.0%
Minimum regulatory requirement	$ 27,351	4.0%	$ 26,808	4.0%

The Bank's capital is supplemented through the retention of net income less dividends paid. The Bank's common dividend declared on April 27, 2020 is $0.12 per share or $728,000.

Impact of Inflation

The primary impact of inflation on the Bank is its effect on interest rates. The Bank's primary source of income is net interest income, which is affected by changes in interest rates. The Bank attempts to limit the impact of inflation on its net interest margin through management of rate-sensitive assets and liabilities and analyses of interest rate sensitivity. The effect of inflation on premises and equipment as well as on non-interest expenses has not been significant for the periods presented.

Item 3 Quantitative and Qualitative Disclosures about Market Risk

Proper management of the rate sensitivity and maturities of assets and liabilities is required to provide an optimum and stable net interest margin. Interest rate sensitivity spread management is an important tool for achieving this objective and for developing ways in which to improve profitability. Management has assessed its market risk at March 31, 2020 and believes that there has been no material change since December 31, 2019.

The Bank constantly monitors earning asset and deposit levels, developments and trends in interest rates, liquidity, capital adequacy and marketplace opportunities. Management responds to all of these to protect and possibly enhance net interest income while managing risks within acceptable levels as set forth in the Bank's policies. In addition, alternative business plans and transactions are contemplated for their potential impact. This process is known as asset/liability management and is carried out by changing the maturities and relative proportions of the various types of loans, investments, deposits and borrowings in the ways described above. The Board monitors and establishes target positions for interest rate and market value risks through the Asset Liability Committee of the Board.

The tool most commonly used to manage and analyze the interest rate sensitivity of a bank is known as a computer simulation model. To quantify the extent of risks in both the Bank's current position and in transactions it might make in the future, the Bank uses a model to simulate the impact of different interest rate scenarios on net interest income. The hypothetical impact of an interest rate shock for incremental interest rate changes up to 4.00% is modeled quarterly, representing the primary means the Bank uses for interest rate risk management decisions. The Bank is liability sensitive; that is, more liabilities reprice within one year than assets. The expectation for a liability sensitive bank is that the net interest margin will decline in a rising interest rate environment.

When preparing its modeling, the Bank makes significant assumptions about the lag in the rate of change in various asset and liability categories. The Bank bases its assumptions on past experience and comparisons with other banks and tests the validity of its assumptions by reviewing actual results with projected expectations.

The computer simulation model assumes a static balance sheet, that is, cash flows from various assets and liabilities are reinvested in similar assets and liabilities. It does not model various dynamic changes in the pricing or term of new assets and liabilities that may occur during the year after the interest rate shock. The computer simulation model projects at March 31, 2020 the following changes over a one-year period in net interest income:

Interest Rate Risk Simulation Model

(in thousands)

Interest Rate Shock	-3%	-2%	-1%	1%	2%	3%
Net interest income change	$ 2,956	$ 1,863	$ 770	$ (441)	$ (413)	$ (397)
Net interest percent change	11.3%	7.1%	3.0%	-1.7%	-1.6%	-1.5%

The Bank's investment portfolio has an average maturity of 13.4 years and would be susceptible to a material decline in market value if interest rates were to materially rise. Management monitors this exposure in relation to the Bank's capital ratios and the interaction of the projected changes in other interest sensitive assets and liabilities to reach a desired balance between current earnings and market risk.

Item 4 Controls and Procedures

Under the supervision and with the participation of the Bank's management, including its Chief Executive Officer and Chief Financial Officer, the Bank conducted an evaluation of the effectiveness of the design and operation of its disclosure controls and procedures as defined by Rule 13a-15(e) under the Securities Exchange Act of 1934.

Based on the evaluation, the Chief Executive Officer and Chief Financial Officer concluded that as of the end of the period covered by this report the disclosure controls and procedures were adequate and effective, and that the material information required to be included in this report, was properly recorded, processed, summarized and reported, and was made known to the Chief Executive Officer and Chief Financial Officer by others within the Bank in a timely manner, particularly during the period when this quarterly report on Form 10-Q was being prepared.

There was no change in the Bank's internal control over financial reporting that occurred during the most recent fiscal quarter that materially affected, or is reasonably likely to materially affect, internal control over financial reporting.

PART II OTHER INFORMATION

Item 1 Legal Proceedings

The nature of our business causes us to be involved in legal proceedings from time to time. As of the date of this report, the Bank is not a party to any litigation where management anticipates that the outcome will have a material adverse effect on the financial position or results of operations.

Item 1A Risk Factors

In addition to the other information set forth in this Form 10-Q, you should carefully consider the risk factors that appeared under Item 1A, "Risk Factors" in the Bank's 2019 Annual Report. There are no material changes from the risk factors included within the Bank's 2019 Annual Report, other than the risks described below.

The ongoing COVID-19 coronavirus pandemic and measures intended to prevent its spread could have a material adverse effect on our business, results of operations and financial condition, and such effects will depend on future developments, which are highly uncertain and are difficult to predict.

Global health concerns relating to the COVID-19 outbreak and related government actions taken to reduce the spread of the virus have created significant economic uncertainty and reduced economic activity, including within our market areas. Governmental authorities have implemented numerous measures to try to contain the virus, such as travel bans and restrictions, quarantines, "stay at home" orders and business limitations and shutdowns. These measures have cause significant unemployment and have negatively impacted consumer and business spending. The United States government has taken steps to attempt to mitigate some of the more severe anticipated economic effects of the virus, including the passage of the CARES Act, but there can be no assurance that such steps will be effective or achieve their desired results in a timely fashion.

The outbreak has adversely impacted and is likely to further adversely impact our operations and the operations of our borrowers, customers and business partners. In particular, we may experience losses due to a number of operational factors impacting us or our borrowers, customers or business partners, including but not limited to:

- credit losses resulting from financial stress being experienced by our borrowers as a result of the outbreak and related governmental actions;
- declines in the value of collateral securing loans we have made;
- third party disruptions, including outages at network providers and other suppliers;
- increased cyber and payment fraud risk, as cybercriminals attempt to profit from the disruption, given increased online and remote activity;
- decreased loan growth;
- decreased interest and non-interest income;
- declines in the value of securities we own, as a result of increasing inflation, credit ratings decline, deterioration in issuers' financial condition or a decline in the liquidity for debt securities, for example;
- operational failures due to changes in our normal business practices necessitated by the outbreak and related governmental actions; and
- Unavailability of key personnel or a significant number of our employees due to the effects and restrictions of a COVID-19 outbreak within our market area.

These factors may remain prevalent for a significant period of time and may continue to adversely affect our business, results of operations and financial condition even after the COVID-19 outbreak has subsided.

The spread of COVID-19 has caused us to modify our business practices (including restricting employee travel, and developing work from home and social distancing plans for our employees), and we may take further actions as may be required by government authorities or as we determine are in the best interests of our employees, customers and business partners. There is no certainty that such measures will be sufficient to mitigate the risks posed by the virus or will otherwise be satisfactory to government authorities.

The extent to which the coronavirus outbreak impacts our business, results of operations and financial condition will depend on future developments, which are highly uncertain and are difficult to predict, including, but not limited to, the duration and spread of the outbreak, its severity, the actions to contain the virus or treat its impact, and how quickly and to what extent normal economic and operating conditions can resume. Even after the COVID-19 outbreak has subsided, we may continue to experience materially adverse impacts to our business as a result of the virus's economic impact, including reduced loan growth, interest and noninterest income; adverse impacts on our liquidity; and any recession that has occurred or may occur in the future.

There are no comparable recent events that provide guidance as to the effect the spread of COVID-19 as a global pandemic may have, and, as a result, we do not yet know the full extent of the impacts on our business, our operations or the economy as a whole. However, the effects could have a material impact on our results of operations and heighten many of our known risks described in the "Risk Factors" section of our Annual Report on Form 10-K for the year ended December 31, 2019.

Item 2 Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3 Defaults Upon Senior Securities

None.

Item 4 Mine Safety Disclosures

Not applicable.

Item 5 Other Information

None.

Item 6 Exhibits

The exhibits filed as part of this report are listed on the Exhibit Index filed as part of this report.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Summit State Bank

(registrant)

May 19, 2020	*/s/ Brian J. Reed*
Date	Brian J. Reed President and Chief Executive Officer (Principal Executive Officer)

May 19, 2020	*/s/ Camille D. Kazarian*
Date	Camille D. Kazarian Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)

EXHIBIT INDEX

Exhibit Number	Description
31.01	Certification of Principal Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) as adopted pursuant to §302 of the Sarbanes-Oxley Act of 2002
31.02	Certification of Principal Financial and Accounting Officer pursuant to Rule 13a-14(a)/15d-14(a) as adopted pursuant to §302 of the Sarbanes-Oxley Act of 2002
32.01	Certification of Principal Executive Officer and Principal Financial and Accounting Officer pursuant to 18 U.S.C. §1350 as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002

Exhibit 31.01

Certification of Principal Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) as adopted pursuant to §302 of the Sarbanes-Oxley Act of 2002

I, Brian J. Reed, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Summit State Bank (the registrant) for the quarter ended March 31, 2020;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant is made known to us by others within those entities, particularly during the period in which this report is being prepared;
(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

March 14, 2020	*/s/ Brian J. Reed*
Date	Brian J. Reed President and Chief Executive Officer (Principal Executive Officer) Summit State Bank

Exhibit 31.02

Certification of Principal Financial and Accounting Officer pursuant to Rule 13a-14(a)/15d-14(a) as adopted pursuant to §302 of the Sarbanes-Oxley Act of 2002

I, Camille D. Kazarian, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Summit State Bank (the registrant) for the quarter ended March 31, 2020;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

May 19, 2020	*/s/ Camille D. Kazarian*
Date	Camille D. Kazarian Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer) Summit State Bank

EXHIBIT 32.01

Certification of Principal Executive Officer and Principal Financial and Accounting Officer pursuant to 18 U.S.C. §1350 as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002

In connection with the quarterly report on Form 10-Q of Summit State Bank (the Registrant) for the quarter ended March 31, 2020, as filed with the Federal Deposit Insurance Corporation, the undersigned hereby certify pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

1) such Form 10-Q fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2) the information contained in such Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

May 19, 2020	*/s/ Brian J. Reed*
Date	Brian J. Reed President and Chief Executive Officer (Principal Executive Officer)
May 19, 2020	*/s/ Camille D. Kazarian*
Date	Camille D. Kazarian Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)

This certification accompanies each report pursuant to §906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Registrant for purposes of §18 of the Securities Exchange Act of 1934, as amended.