Southern California Bancorp

Bank of Southern California

2021 ANNUAL REPORT

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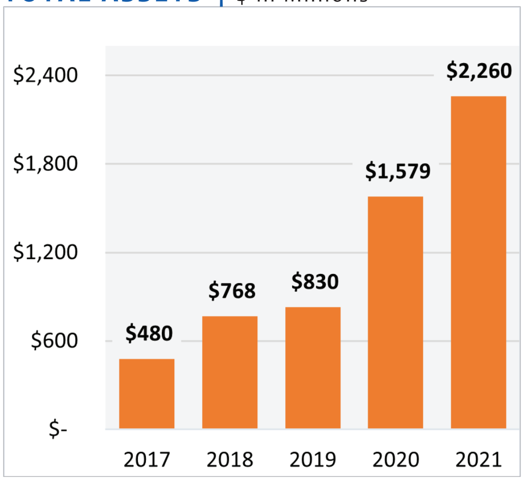
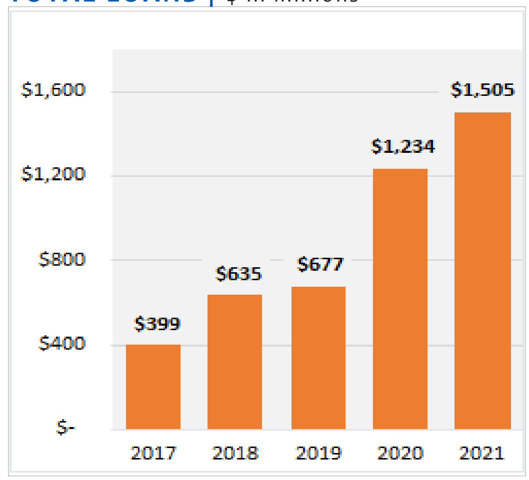
FINANCIAL PERFORMANCE

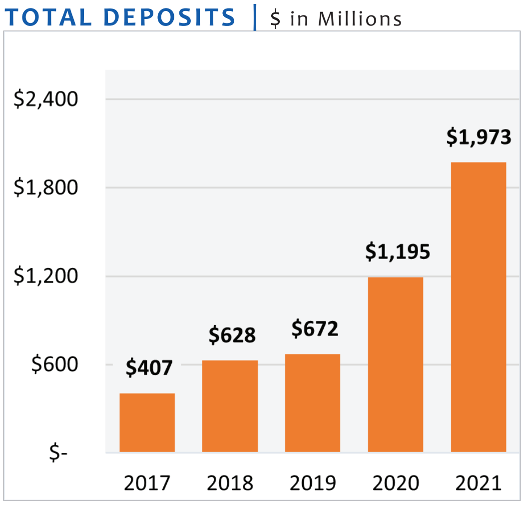
TOTAL ASSETS | $ in Millions



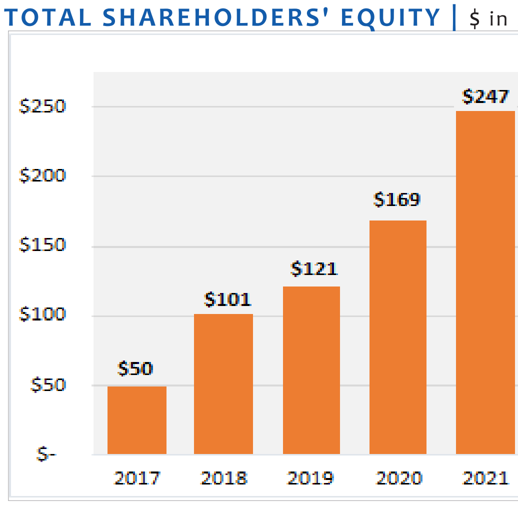
TOTAL LOANS | $ in Millions



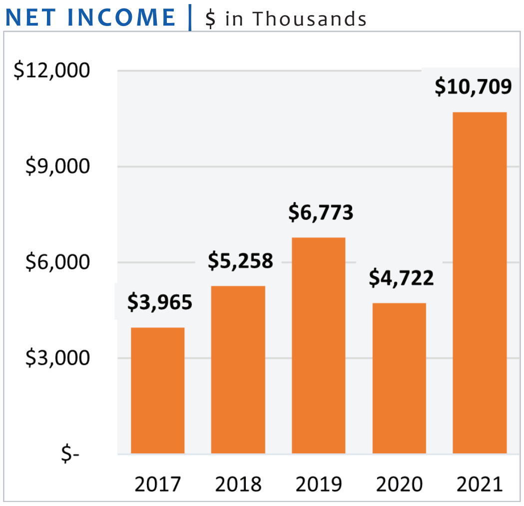
TOTAL DEPOSITS | $ in Millions



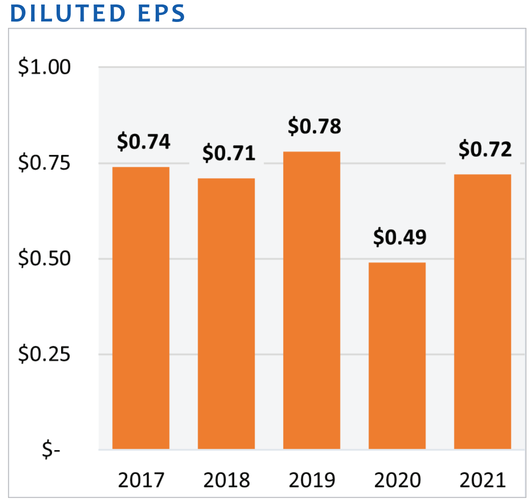
TOTAL SHAREHOLDERS' EQUITY | $ in Millions



NET INCOME | $ in Thousands



DILUTED EPS



EXECUTIVE PROFILE

BOARD OF DIRECTORS

Irwin L. Golds
Chairman of the Board
CEO and Co-founder of
Capitis Real Estate

John Farkash
Chairman Emeritus and President,
Farkash Construction, Inc.

Lester Machado, MD, DDS, FRCS (Ed)
Oral and Maxillofacial Surgeon

Jan Lynn Owen
Senior Advisor, Manatt Financial Services

Kaveh Varjavand
President, AARCS, LLC.

David J. Volk
Principal, Castle Creek Advisors

Anita Wolman
Banking and Corporate Governance Consultant

Frank D. Di Tomaso
Former Chairman and CEO of
Bank of Santa Clarita

EXECUTIVE MANAGEMENT

Thomas G. Dolan
Executive Vice President,
Chief Executive Officer

Richard Hernandez
President,
Chief Banking Officer

Jean Carandang
Executive Vice President,
Chief Financial Officer

Khoi Dang
Executive Vice President,
Chief Administrative Officer, Chief Legal
Counsel and Corporate Secretary

Anthony J. DiVita
Executive Vice President,
Chief Strategy Officer

Jeffery T. Hurtik
Executive Vice President,
Chief Information Officer

Pamela C. Isaacson
Executive Vice President,
Chief Operations Officer

Martin Liska
Executive Vice President,
Chief Risk Officer

Nicole Swain
Executive Vice President,
President of Private Banking

Anne A. Williams
Executive Vice President,
Chief Credit Officer

COMMON STOCK

Stock Exchange Listing
The common stock trades on the
OTC Marketplace (OTC Pink) under
the symbol BCAL.

Transfer Agent
Computershare Investor Services

Locations

Carlsbad
3142 Tiger Run Ct., Ste. 107
Carlsbad, CA 92010

Cerritos (Administration)
18000 Studebaker Road, Ste. 100
Cerritos, CA 90703

Del Mar
12265 El Camino Real, Ste. 100
San Diego, CA 92130

Downtown Los Angeles (Administration)
355 S. Grand Ave., Ste. 1710
Los Angeles, CA 90071

Downtown San Diego
1620 Fifth Ave., Ste. 120
San Diego, CA 92101

Encino
16255 Ventura Blvd., Ste. 1100
Encino, CA 91436

Glendale
801 N. Brand Blvd., Ste. 185
Glendale, CA 91203

Irvine
400 Spectrum Center Dr., Ste. 100
Irvine, CA 92618

La Quinta
47-000 Washington St.
La Quinta, CA 92253

Ramona
1315 Main St.
Ramona, CA 92065

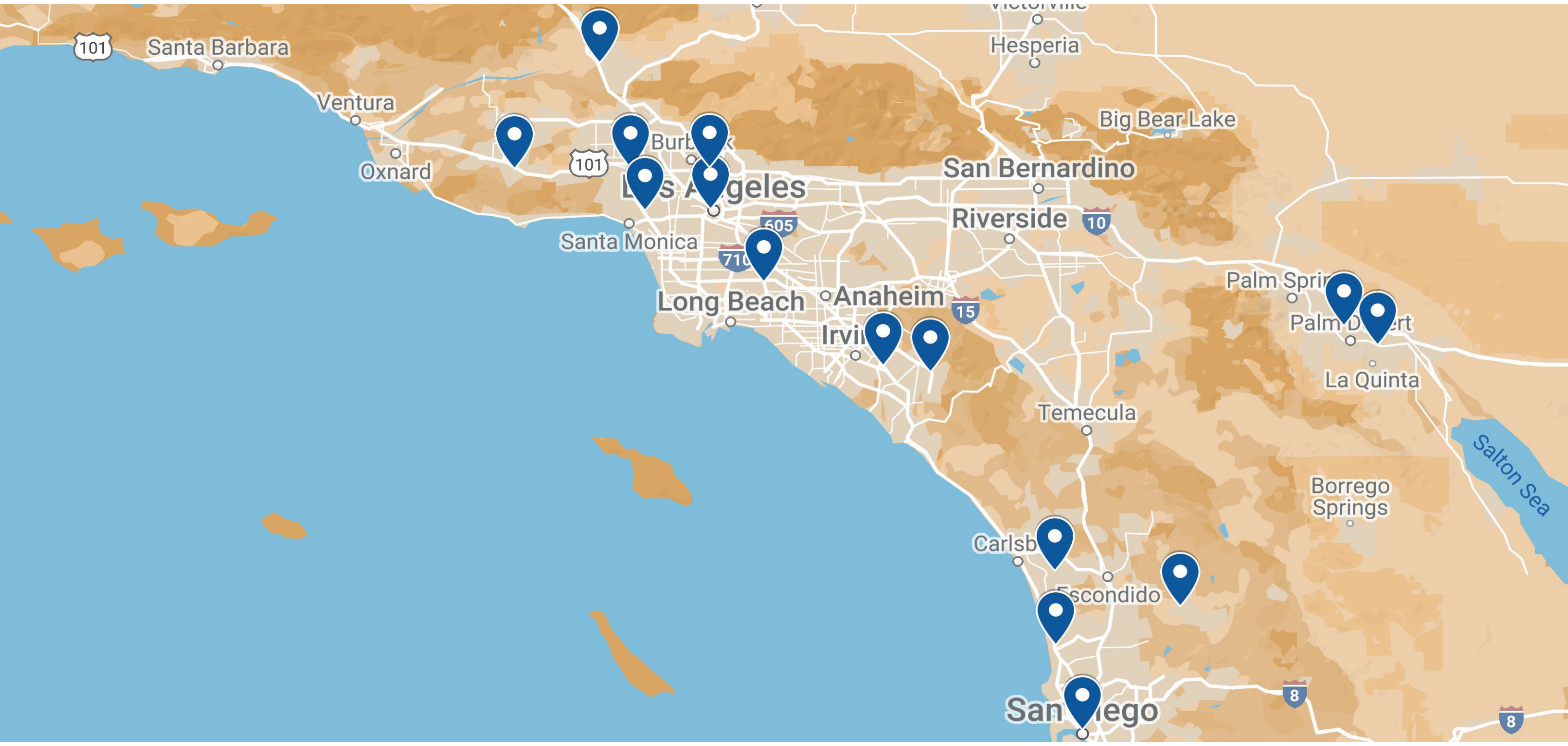
Rancho Mirage
40101 Monterey Ave., Ste. H
Rancho Mirage, CA 92270

Rancho Santa Margarita
22342 Avenida Empresa, Ste. 101A
Rancho Santa Margarita, CA 92688

Santa Clarita
23780 Magic Mountain Pkwy.
Santa Clarita, CA 91355

West Los Angeles
1640 S. Sepulveda Blvd., Ste. 130
Los Angeles, CA 90025

Westlake Village
875 S. Westlake Blvd., Ste. 101
Westlake Village, CA 91361



CPAs & BUSINESS ADVISORS

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
Southern California Bancorp and Subsidiary
San Diego, California

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of Southern California Bancorp and Subsidiary (the "Company") as of December 31, 2021 and 2020, the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2021 and 2020, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB and in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risk of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current-period audit of the financial statements that were communicated or required to be communicated to the audit committee and that (1) relate to accounts or disclosures that are material to the financial statements and (2) involved especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

Allowance for Loan Losses

As discussed in Note 4 to the Company's consolidated financial statements, the Company has a gross loan portfolio of $1.5 billion and related allowance for loan losses of $11.7 million as of December 31, 2021. The Company's allowance for loan losses is a material and complex estimate requiring significant management judgment in the evaluation of the credit quality and the estimation of inherent losses within the loan portfolio. The allowance for loan losses includes a general reserve which is determined based on the results of a quantitative and a qualitative analysis of all loans not measured for impairment at the reporting date.

The Company's general reserves cover non-impaired loans and are based on historical loss rates for each portfolio. In calculating the allowance for loan losses, the Company considers relevant credit quality indicators for each loan segment, stratifies loans by risk rating, and estimates losses for each loan type based upon their nature and risk profile. This process requires significant management judgment in the review of the loan portfolio and assignment of risk ratings based upon the characteristics of loans. In addition, estimation of losses inherent within the portfolio requires significant management judgment, particularly where the Company has not incurred sufficient historical losses and has utilized industry data in forming its estimate.

Auditing these complex judgments and assumptions involves especially challenging auditor judgment due to the nature and extent of audit evidence and effort required to address these matters, including the extent of specialized skill or knowledge needed.

The primary procedures we performed to address this critical audit matter included:

- Gaining an understanding of the design and implementation of controls relating to management's timely identification of problem loans, appropriate application of loan rating policy, consistency of application of accounting policies and appropriateness of assumptions used in the allowance for loan losses calculation.

- Evaluating the reasonableness of assumptions and sources of data used by management in forming historical loss factors by performing a retrospective review of loan loss experience and analyzing the historical data used in developing the assumptions.

- Evaluating the appropriateness of inputs and factors that the Company used in forming the qualitative loss factors and assessing whether such inputs and factors were relevant, reliable, and reasonable for the purpose used. We also evaluated the period-to-period consistency with which qualitative loss factors are determined and applied.

- Testing the mathematical accuracy and computation of the allowance for loan losses.

Accounting for Acquisitions

As described in Note 2 to the Company's consolidated financial statements, the Company had a significant acquisition during the year ended December 31, 2021: the acquisition of Bank of Santa Clarita for a purchase price of $65.3 million. As a result of this acquisition, management was required to determine estimated fair values of the assets and liabilities at the acquisition date.

The Company's determination of fair values of certain identifiable tangible and intangible assets is complex and included the following areas of management's judgments: (i) application of accounting guidance related to business combinations, (ii) significant unobservable inputs and assumptions utilized by management in determining the fair values of certain identifiable tangible and intangible assets, and (iii) changes in certain assumptions that could have a significant impact on the fair values of the identifiable tangible and intangible assets acquired.

Auditing these elements involved especially challenging auditor judgment due to the nature and extent of audit effort required to address these matters, including the extent of specialized skill or knowledge needed.

The primary procedures we performed to address this critical audit matter included:

- Gaining an understanding of the design and implementation of controls related to management's identification of assets and liabilities acquired in the acquisition transaction and management's consideration of the methodologies and related significant inputs and assumptions used in the determination of estimated fair values of assets and liabilities acquired.

- Assessing management's application of accounting guidance related to business combinations.

- Assessing the reasonableness of significant underlying assumptions by evaluating whether the information used by the Company: (i) was reasonably available at the time of the analysis; (ii) was the best information available under the circumstances; and (iii) gave consideration to observable market prices.

- Assessing the methodology utilized by management, including complex assumptions used, and testing the underlying source information, in the determination of fair values as of the acquisition date with the assistance of our internal valuation specialists.

Eide Bailly LLP

We have served as the Company's auditor since 2019. Vavrinek, Trine, Day & Co., LLP, who joined Eide Bailly LLP in 2019, had served as the Company's auditor since 2007.

Laguna Hills, California
April 25, 2022

SOUTHERN CALIFORNIA BANCORP AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
December 31, 2021 and 2020
(dollars in thousands, except share data)

	December 31,	
	2021	**2020**
ASSETS		
Cash and due from banks	$ 22,435	$ 11,951
Federal funds and interest-bearing balances	557,571	238,866
Total cash and cash equivalents	580,006	250,817
Debt securities available for sale	55,567	24,702
Loans held for investment	1,504,748	1,233,881
Allowance for loan losses	(11,657)	(10,255)
Loans held for investment, net	1,493,091	1,223,626
Restricted stock, at cost	12,493	8,585
Premises and equipment	19,639	6,517
Right of use asset	8,069	8,534
Goodwill	36,784	19,723
Core deposit intangible	2,022	1,876
Bank owned life insurance	37,849	17,991
Deferred taxes, net	5,069	6,296
Accrued interest and other assets	9,277	10,381
Total assets	$ 2,259,866	$ 1,579,048
LIABILITIES		
Noninterest-bearing demand	$ 986,935	$ 533,923
Interest-bearing NOW accounts	193,525	83,567
Money market and savings accounts	690,348	458,530
Time deposits under $250,000	66,615	67,158
Time deposits $250,000 and over	35,675	51,561
Total deposits	1,973,098	1,194,739
Borrowings	20,409	199,648
Operating lease liability	9,002	9,397
Accrued interest and other liabilities	10,829	6,379
Total liabilities	2,013,338	1,410,163
Commitments and contingencies (Notes 5 and 12)		
SHAREHOLDERS' EQUITY		
Preferred stock - 50,000,000 shares authorized, no par value; no shares issued and outstanding at December 31, 2021 and 2020	—	—
Common stock - 50,000,000 shares authorized, no par value; issued and outstanding 17,707,737 and 13,267,380 at December 31, 2021 and 2020	214,163	146,896
Retained earnings	32,403	21,694
Accumulated other comprehensive (loss) income - net of taxes	(38)	295
Total shareholders' equity	246,528	168,885
Total liabilities and shareholders' equity	$ 2,259,866	$ 1,579,048

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

SOUTHERN CALIFORNIA BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
For the Years Ended December 31, 2021 and 2020
(dollars in thousands, except per share data)

	Year Ended December 31,	
	2021	**2020**
INTEREST AND DIVIDEND INCOME		
Interest and fees on loans	$ 66,213	$ 50,477
Interest on debt securities	455	422
Interest on deposits at other financial institutions	470	479
Interest and dividends on other interest-earning assets	635	437
Total interest and dividend income	67,773	51,815
INTEREST EXPENSE		
Interest on NOW, money market and savings accounts	1,320	1,646
Interest on time deposits	734	2,234
Interest on borrowings	1,308	1,990
Total interest expense	3,362	5,870
Net interest income	64,411	45,945
Provision for loan losses	1,200	4,552
Net interest income after provision for loan losses	63,211	41,393
NONINTEREST INCOME		
Service charges and fees on deposit accounts	826	563
Interchange and ATM income	775	476
Gain on sale of loans	920	—
Income from bank owned life insurance	786	361
Servicing and related income on loans, net	116	138
Gain on sale of debt securities	46	574
Loss on sale and disposal of fixed assets	(4)	(93)
Gain on branch sale	726	—
Other charges and fees	323	277
Total noninterest income	4,514	2,296
NONINTEREST EXPENSE		
Salaries and employee benefits	34,883	21,691
Occupancy and equipment	5,522	3,785
Data processing and communications	4,111	2,870
Legal, audit and professional	1,678	868
Marketing, advertising and public relations	678	566
Regulatory assessments	990	498
FHLB prepayment penalty	—	2,370
Director and shareholder expenses	636	545
Merger and related expenses	2,450	2,248
Core deposit intangible amortization	364	386
Other expenses	2,227	1,094
Total noninterest expense	53,539	36,921
Income before income taxes	14,186	6,768
Income tax expense	3,477	2,046
Net income	$ 10,709	$ 4,722
Earnings per share:		
Basic	$ 0.74	$ 0.50
Diluted	$ 0.72	$ 0.49

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

SOUTHERN CALIFORNIA BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
For the Years Ended December 31, 2021 and 2020
(dollars in thousands)

	Year Ended December 31,	
	2021	**2020**
Net income	$ 10,709	$ 4,722
Other comprehensive loss, net of tax:		
Unrealized (losses) gains on securities available for sale:		
Change in net unrealized (loss) gain	(423)	563
Reclassification of gain recognized in net income	(46)	(574)
	(469)	(11)
Income tax (benefit) expense:		
Change in net unrealized (loss) gain	(123)	163
Reclassification of gain recognized in net income	(13)	(166)
	(136)	(3)
Total other comprehensive loss	(333)	(8)
Total comprehensive income	$ 10,376	$ 4,714

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

SOUTHERN CALIFORNIA BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
For the Years Ended December 31, 2021 and 2020
(dollars in thousands, except share data)

	Common Stock		Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	Shares	Amount			
Balance at December 31, 2019	9,405,190	$ 103,249	$ 16,972	$ 303	$ 120,524
Stock-based compensation	—	2,653	—	—	2,653
Issuance of common stock, net	3,615,345	40,625	—	—	40,625
Stock options exercised	58,500	369	—	—	369
Restricted share awards vested	188,345	—	—	—	—
Net income	—	—	4,722	—	4,722
Other comprehensive loss	—	—	—	(8)	(8)
Balance at December 31, 2020	13,267,380	146,896	21,694	295	168,885
Stock-based compensation	—	5,501	—	—	5,501
Issuance of common stock in business combination	4,102,254	65,267	—	—	65,267
Stock options exercised	303,100	172	—	—	172
Restricted share awards vested, net of tax withholding	257,795	(2,893)	—	—	(2,893)
Repurchase of shares to cover stock option proceeds and tax liabilities	(222,792)	(780)	—	—	(780)
Net income	—	—	10,709	—	10,709
Other comprehensive loss	—	—	—	(333)	(333)
Balance at December 31, 2021	17,707,737	$ 214,163	$ 32,403	$ (38)	$ 246,528

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

SOUTHERN CALIFORNIA BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2021 and 2020
(dollars in thousands)

	Year Ended December 31,	
	2021	**2020**
OPERATING ACTIVITIES		
Net income	$ 10,709	$ 4,722
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,358	1,067
Core deposit intangible amortization	364	386
Gain on sale of loans	(920)	—
Gain on branch sale	(726)	—
Provision for loan losses	1,200	4,552
Deferred income tax expense (benefit)	137	(2,091)
Impairment charges of right-of-use assets	287	—
Stock-based compensation	5,501	2,653
Increase in cash surrender value of bank owned life insurance	(591)	(361)
Income from bank owned life insurance	(195)	—
Gain on sale of debt securities	(46)	(574)
(Accretion) amortization of net discounts and deferred loan fees	(7,370)	862
Provision for losses - unfunded commitments	600	—
Net increase in other items	9,344	1,143
Net cash provided by operating activities	19,652	12,359
INVESTING ACTIVITIES		
Net cash acquired in business combination	115,420	36,965
Net cash transferred for branch sale	(81,467)	—
Purchase of bank owned life insurance	(10,773)	—
Proceeds from bank owned life insurance death benefits	586	—
Proceeds from sale of debt securities available for sale	2,840	10,009
Proceeds from maturities and paydowns of debt securities available for sale	5,601	4,791
Purchases of debt securities available for sale	(26,044)	(13,668)
Net purchase of stock investments	(2,323)	(705)
Net repayment (funding) of loans	5,343	(337,316)
Proceeds from loans sale	1,092	—
Purchases of premises and equipment	(1,753)	(1,767)
Net cash provided by (used in) investing activities	8,522	(301,691)
FINANCING ACTIVITIES		
Net increase in deposits	518,450	281,816
Proceeds of Federal Home Loan Bank advances	—	55,000
Repayment of Federal Home Loan Bank advances	(44,551)	(85,000)
Proceeds of other borrowings	—	250,743
Repayment of other borrowings	(169,383)	(94,252)
Proceeds from exercise of stock options	172	369
Repurchase of common shares	(3,673)	—
Proceeds from common stock issued, net of expenses	—	40,625
Net cash provided by financing activities	301,015	449,301
Net change in cash and cash equivalents	329,189	159,969
Cash and cash equivalents at beginning of year	250,817	90,848
Cash and cash equivalents at end of year	$ 580,006	$ 250,817

SOUTHERN CALIFORNIA BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2021 and 2020

(dollars in thousands)

	2021	2020
Supplemental Disclosures of Cash Flow Information:		
Interest paid	$ 3,587	$ 5,705
Taxes paid	1,033	5,508
Reduction of ROU assets from branch sale	1,242	—
Reduction of lease liabilities from branch sale	1,801	—
Lease liability arising from obtaining right-of-use assets	3,463	2,224
Net assets acquired in business combination (Note 2):		
Fair value of stock and equity award consideration	65,267	—
Cash consideration	—	25,913
Fair value of net assets acquired	48,206	22,409

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

NOTE 1 – BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Southern California Bancorp is a California corporation incorporated on October 2, 2019 and is registered with the Board of Governors of the Federal Reserve System as a bank holding company for Bank of Southern California, N.A. under the Bank Holding Company Act of 1956, as amended. Bank of Southern California, N.A. is a wholly owned subsidiary of Southern California Bancorp ("SCB") and began business operations in December 2001 under the name Ramona National Bank. The name was changed to First Business Bank, N.A. in 2006 and to Bank of Southern California, N.A. in 2010. The Bank operates under a federal charter and its primary regulator is the Office of the Comptroller of the Currency ("OCC"). References herein to "Southern California Bancorp," "SCB", "Bancorp" or the "holding company," refer to Southern California Bancorp on a stand-alone basis. The words "we," "us," "our," or the "Company" refer to Southern California Bancorp, and Bank of Southern California, N.A. collectively and on a consolidated basis. References to the "Bank" refer to Bank of Southern California, N.A.

The Bank operates full-service banking offices in San Diego County, Los Angeles County, Orange County, and the Coachella Valley in Riverside County. Many of the banking offices have been acquired through a number of acquisitions.

Effective at the close of business on September 24, 2021, the Orange, Redlands and Santa Fe Springs branches were sold to a third party financial institution who acquired certain branch assets and assumed certain branch liabilities including deposits. No loans were sold as part of the transaction. The assets and liabilities of these three branches primarily consisted of $146 thousand of cash and cash equivalents and $82.4 million of deposits. The transaction resulted in a net cash payment to the third party financial institution of $81.5 million, and a gain on sale of $726 thousand recorded as a component of noninterest income in the consolidated statements of income.

The Company completed the acquisition of Bank of Santa Clarita ("BSCA") on October 1, 2021. The acquisition has been accounted for using the acquisition method of accounting and, accordingly, the operating results of BSCA have been included in the consolidated financial statements from October 2, 2021 through December 31, 2021. Refer to Note 2 – Business Combinations for more information about the BSCA acquisition.

Shares of SCB common stock are traded on the OTC Markets Group Inc. Pink Open Market ("OTC Pink") under the symbol "BCAL".

Basis of Presentation

The accompanying consolidated financial statements include the accounts of the Company, and its wholly owned subsidiary, Bank of Southern California, N.A., and have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). Certain prior period amounts have been reclassified to conform to current period presentation.

Principles of Consolidation

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

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change are the determination of the allowance for loan losses, the fair value of assets and liabilities acquired in business combinations and related purchase price allocation, the valuation of acquired loans, the valuation of goodwill and separately identifiable intangible assets associated with mergers and acquisitions, loan sales and servicing of financial assets and deferred tax assets and liabilities.

Operating Segments

We operate one reportable segment — commercial banking. The factors considered in making this determination include all of the banking products and services offered by the Company are available in each branch of the Company, all branches are located within the same economic environment, management does not allocate resources based on the performance of different lending or transaction activities and how information is reviewed by the chief executive officer and other key decision makers. As a result, we determined that all services we offer relate to commercial banking.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, cash balances due from banks, and federal funds sold. Interest-bearing deposits with financial institutions represent primarily cash held at the Federal Reserve Bank of San Francisco. The Board of Governors of the Federal Reserve System ("Federal Reserve") has cash reserve requirements for depository institutions based on the amount of deposits held. At December 31, 2021, the Bank had no required cash balance held by the Federal Reserve. The Company maintains amounts due from banks that exceed federally insured limits. The Company has not experienced any losses in such accounts.

Debt Securities

Debt securities are classified as held-to-maturity when the Company has the positive intent and ability to hold the securities to maturity. Debt securities classified as held-to-maturity securities are carried at amortized cost. Debt securities not classified as trading securities nor as held-to-maturity securities are classified as available-for-sale securities and recorded at fair value. Unrealized gains or losses on available-for-sale securities are excluded from net income and reported as an amount net of taxes as a separate component of other comprehensive income included in shareholders' equity. Premiums or discounts on held-to-maturity and available-for-sale securities are amortized or accreted into income using the interest method. Realized gains or losses on sales of held-to-maturity or available-for-sale securities are recorded using the specific identification method.

Management evaluates securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: OTTI related to credit loss, which must be recognized in the income statement and OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. The related write-downs are included in earnings as realized losses.

Restricted Stock Investments

The Bank is a member of the Federal Home Loan Bank ("FHLB") system. Members are required to own a certain amount of stock based on the level of borrowings and other factors. In addition, the Bank is a member of its regional Federal Reserve Bank ("FRB"). FHLB and FRB stock are carried at cost, classified as a restricted stock, at cost, in the consolidated balance sheets and periodically evaluated for impairment based on the ultimate recovery of par value. Both cash and stock dividends are reported as interest and dividends on other interest-earning assets in the accompanying consolidated statements of income.

Equity Securities

The Company also has restricted securities in the form of capital stock invested in two different banker's bank stocks and other limited partnership investments. These investments do not have a readily determinable fair value, and they are measured at cost less impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer. Any impairment will be recorded through earnings. These investments are included in other assets in the accompanying consolidated balance sheets.

Loans

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at their outstanding unpaid principal balances reduced by any charge-offs and net of any deferred fees or costs on originated loans, or unamortized premiums or discounts on purchased loans. Purchase discounts and premiums and net deferred loan origination fees and costs on loans are accreted or amortized in interest income as an adjustment of yield, using the interest method, over the expected life of the loans. Amortization of deferred loan fees and costs are discontinued when a loan is placed on nonaccrual status.

Impaired loans

Loans on which the accrual of interest has been discontinued are designated as nonaccrual loans. The accrual of interest on loans is generally discontinued when principal or interest is past due 90 days based on the contractual terms of the loan or earlier when, in the opinion of management, there is reasonable doubt as to collectability. On a case-by-case basis, loans past due 90 days may remain on accrual, if the loan is well collateralized, actively in process of collection and, in the opinion of management, likely to be paid current within the next payment cycle. When loans are placed on nonaccrual status, all interest previously accrued but not collected is generally reversed against current period interest income. Income on nonaccrual loans is subsequently recognized only to the extent that cash is received and the loan's principal balance is deemed collectible. Interest accruals are resumed on such loans only when they are brought current with respect to interest and principal and when, in the judgment of management, the loans are estimated to be fully collectable as to all principal and interest.

Troubled debt restructurings (TDR)

A loan is classified as a TDR when the Company grants a concession to a borrower experiencing financial difficulties that it otherwise would not consider under our normal lending policies. These concessions may include a reduction of the interest rate, principal or accrued interest, extension of the maturity date or other actions intended to minimize potential losses. All modifications of criticized loans are evaluated to determine whether such modifications are TDR as outlined under ASC Subtopic 310-40, Troubled Debt Restructurings by Creditors. Loans restructured with an interest rate equal to or greater than that of a new loan with comparable market risk at the time the loan is modified may be excluded from certain restructured loan disclosures in years subsequent to the restructuring if the loans are in compliance with their modified terms. The Coronavirus Aid, Relief, and Economic Security Act of 2020 (CARES Act) and the Consolidated Appropriations Act, 2021 (CAA) provided guidance around the modification of loans as a result of the COVID-19 pandemic, which outlined, among other criteria, that short-term modifications made on a good faith basis to borrowers who were current as defined under the CARES Act prior to any relief, are not TDRs. This includes short-term (e.g. six months) modifications such as payment deferrals, fee waivers, extensions of repayment terms, or other delays in payment that are insignificant. Borrowers are considered current under the CARES Act and regulatory guidance if they are less than 30 days past due on their contractual payments at the time a modification program is implemented. The CAA extends relief offered under the CARES Act related to TDRs as a result of COVID-19 through January 1, 2022.

A loan that has been placed on nonaccrual status that is subsequently restructured will usually remain on nonaccrual status until the borrower is able to demonstrate repayment performance in compliance with the restructured terms for a sustained period of time, typically for six months. A restructured loan may return to accrual status sooner based on other significant events or mitigating circumstances. A loan that has not been placed on nonaccrual status may be restructured and such loan may remain on accrual status after such restructuring. In these circumstances, the borrower has made payments before and after the restructuring. Generally, this restructuring involves maturity extensions, a reduction in the loan interest rate and/or a change to interest-only payments for a period of time. The restructured loan is considered impaired despite the accrual status and a specific reserve is calculated based on the present value of expected cash flows discounted at the loan's original effective interest rate or based on the fair value of the collateral if the loan is collateral-dependent.

Purchased Credit Impaired Loans

Purchased credit impaired loans ("PCI loans") are accounted for in accordance with ASC Subtopic 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*. A purchased loan is deemed to be credit impaired when there is evidence of credit deterioration since its origination and it is probable at the acquisition date that collection of all contractually required payments is unlikely. These PCI loans are recorded at the amount paid, such that there is no carryover of the seller's allowance for loan losses.

Such purchased credit impaired loans are accounted for individually or aggregated into pools of loans based on common risk characteristics such as credit score, loan type, and date of origination.

As of December 31, 2021 and 2020, the total carrying value of purchased credit impaired loans was approximately $414 thousand and $846 thousand, net of discounts to contractual value of approximately $118 thousand and $1.4 million, which will be accreted to income in the future if cash flows are greater than expected.

Allowance for Loan Losses

The allowance for loan losses ("ALLL") is a valuation allowance for probable incurred credit losses. Loan charge-offs are recognized when management believes the collectability of the principal balance outstanding is unlikely. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged-off. Amounts are charged-off when available information confirms that specific loans or portions thereof, are uncollectible. This methodology for determining charge-offs is consistently applied to each segment.

The Company determines a separate allowance for each portfolio segment. The allowance consists of specific and general reserves. Specific reserves relate to loans that are individually classified as impaired. The Company considers a loan to be impaired when it is probable that the Company will not be able to collect all amounts due, principal and interest, according to the contractual terms of the loan agreement. Factors considered in determining impairment include payment status, collateral value and the probability of collecting all amounts when due. Measurement of impairment is based on the expected future cash flows of an impaired loan, which are to be discounted at the loan's effective interest rate, or measured by reference to an observable market value, if one exists, or the fair value of the collateral for a collateral-dependent loan. The Company selects the measurement method on a loan-by-loan basis except that collateral-dependent loans for which foreclosure is probable are measured at the net realizable value of the collateral. Loans, for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired with measurement of impairment as described above.

If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Troubled debt restructurings are separately identified for impairment disclosures and are measured at the present value of estimated future cash flows using the loan's effective interest rate at inception. If a troubled debt restructuring is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral. For troubled debt restructurings that subsequently default, the Company determines the amount of reserve in accordance with the accounting policy for the allowance for loan losses.

General reserves cover non-impaired loans and are based on historical loss rates for each portfolio segment, adjusted for the effects of qualitative or environmental factors that are likely to cause estimated credit losses as of the evaluation date to differ from the portfolio segment's historical loss experience.

The Company reviews the historical loss rates for each portfolio segment and utilizes peer loss rates when the Company does not have sufficient historical experience or otherwise feels historical experience is not indicative of the current loan portfolio. Qualitative factors include consideration of the following: changes in lending policies and procedures; changes in economic conditions, changes in the nature and volume of the portfolio; changes in the experience, ability and depth of lending management and other relevant staff; changes in the volume and severity of past due, nonaccrual and other adversely graded loans; changes in the loan review system; the existence and effect of any concentrations of credit; the effect of other external factors such as competition and legal and regulatory requirements; the quality and effectiveness of the risk rating system; and the quality of regulatory and other external credit reviews.

Portfolio segments identified by the Company include construction and land development, real estate, commercial and industrial and consumer loans. Relevant risk characteristics for these portfolio segments generally include debt to income ratios or debt service coverage, credit scores, collateral type and loan-to-value ratios and financial performance.

Allowance for Credit Losses on Off-Balance Sheet Credit Exposures

The Company also maintains a separate allowance for off-balance sheet commitments. Management estimates anticipated losses using historical data and utilization assumptions. The allowance for off-balance sheet commitments totaled $804 thousand and $145 thousand at December 31, 2021 and 2020. Provisions for allowance for off-balance sheet commitments are included in other noninterest expense and added to the allowance for off-balance sheet commitments, which is included in the Accrued interest payable and other liabilities of the consolidated balance sheets.

Other Real Estate Owned

Real estate acquired by foreclosure or deed in lieu of foreclosure is recorded at fair value less costs to sell at the date of foreclosure, establishing a new cost basis by a charge to the allowance for loan losses, if necessary. Subsequent to foreclosure, other real estate owned is carried at the lower of the Company's carrying value of the property or its fair value, less estimated carrying costs and costs of disposition. Fair value is generally based on current appraisals, which are frequently adjusted by management to reflect current conditions and estimated selling costs. Write-downs are expensed and recognized as a valuation allowance. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in other operating expenses. There were no foreclosures in process as of December 31, 2021 and 2020.

Bank Owned Life Insurance

Bank owned life insurance is recorded at the amount that can be realized under insurance contracts at the date of the consolidated balance sheets, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when: (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before maturity.

Loan Sales and Servicing of Financial Assets

The Company originates SBA loans that may be sold in the secondary market. Servicing rights are recognized separately when they are acquired through sale of loans. Servicing rights are initially recorded at fair value with the income statement effect recorded in gain on sale of loans. Fair value is based on a valuation model that calculates the present value of estimated future cash flows from the servicing assets. The valuation model uses assumptions that market participants would use in estimating cash flows from servicing assets, such as the cost to service, discount rates and prepayment speeds. The Company compares the valuation model inputs and results to published industry data in order to validate the model results and assumptions. Servicing assets are subsequently measured using the amortization method which requires servicing rights to be amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying loans.

Servicing fee income, which is reported on the consolidated statements of income with servicing and related income on loans, net, is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal and recorded as income when earned. The amortization of servicing rights and changes in the valuation allowance are netted against loan servicing income. Net servicing fees totaled $82 thousand and $94 thousand for the years ended December 31, 2021 and 2020 including contractually specified servicing fees of $218 thousand and $269 thousand, offset by the servicing rights amortization of $136 thousand and $175 thousand.

Premises and Equipment

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

Right-of-Use ("ROU") Assets and Lease Liabilities

The Company determines if an arrangement contains a lease at contract inception and recognizes a ROU asset and operating lease liability based on the present value of lease payments over the lease term. While operating leases may include options to extend the term, the Company does not take into account the options in calculating the ROU asset and lease liability unless it is reasonably certain such options will be exercised. The present value of lease payments is determined based on the Company’s incremental borrowing rate and other information available at lease commencement. Leases with an initial term of 12 months or less are not recorded on the consolidated balance sheets. Lease expense is recognized on a straight-line basis over the lease term. The Company has elected to account for lease agreements with lease and non-lease components as a single lease component.

Employee Benefit Plans

The Company has a retirement savings 401(k) plan in which substantially all employees may participate. Pursuant to the Company’s safe harbor election, matching contributions up to 4.0% of salary are made to the plan. Total contribution expense for the plan was $705 thousand in 2021 and $340 thousand in 2020 and is included in salaries and employee benefits expense in the consolidated statements of income. Deferred compensation and supplemental retirement plan expense is recognized over the years of service.

Advertising Costs

The Company expenses the costs of advertising in the period incurred. Total advertising costs were $188 thousand and $233 thousand for the years ended December 31, 2021 and 2020.

Income Taxes

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

The Company has adopted guidance issued by the Financial Accounting Standards Board (“FASB”) that clarifies the accounting for uncertainty in tax positions taken or expected to be taken on a tax return and provides that the tax effects from an uncertain tax position can be recognized in the financial statements only if, based on its merits, the position is more likely than not to be sustained on audit by the taxing authorities. Management believes that all tax positions taken to date are highly certain and, accordingly, no accounting adjustment has been made to the consolidated financial statements. Interest and penalties related to uncertain tax positions are recorded as part of income tax expense.

Comprehensive Income

Changes in unrealized gains and losses on available-for-sale securities is the only component of accumulated other comprehensive income for the Company. The amount reclassified out of other accumulated comprehensive income relating to realized gains on sales of securities was $46 thousand and $574 thousand, with a related tax effect of $13 thousand and $166 thousand for December 31, 2021 and 2020.

Financial Instruments

In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit, commercial letters of credit, and standby letters of credit. Such financial instruments are recorded in the financial statements when they are funded, or related fees are incurred or received.

Earnings Per Share (“EPS”)

Earnings per share present the net income or loss per common share, after consideration of the preferred shareholders interest in the net income or loss. Basic EPS excludes dilution and is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity.

Business Combinations

Business combinations are accounted for using the acquisition method of accounting under ASC Topic 805 - *Business Combinations*. Under the acquisition method, the Company measures the identifiable assets acquired, including identifiable intangible assets, and liabilities assumed in a business combination at fair value on acquisition date. Goodwill is generally determined as the excess of the fair value of the consideration transferred, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. The Company accounts for merger-related costs, which may include advisory, legal, accounting, valuation, other professional fees, data conversion fees, contract termination charges and branch consolidation costs, as expenses in the periods in which the costs are incurred and the services are received.

Goodwill and Other Intangible Assets

Goodwill and other intangible assets acquired in a purchase business combination and determined to have indefinite useful lives are not amortized but tested for impairment no less than annually or when circumstances arise indicating impairment may have occurred. Goodwill is the only intangible asset with an indefinite life recorded in the Company’s consolidated balance sheets. The determination of whether impairment has occurred, includes the considerations of a number of factors including, but not limited to, operating results, business plans, economic projections, anticipated future cash flows, and current market data. Any impairment identified as part of this testing is recognized through a charge to net income. The Company has selected to perform its annual impairment test in the fourth quarter of each fiscal year.

There was no impairment recognized related to goodwill for the years ended December 31, 2021 and 2020.

Core deposit intangible ("CDI") is a measure of the value of depositor relationships resulting from whole bank acquisitions. Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values.

Loss Contingencies

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

Revenue Recognition – Noninterest Income

The core principle of Topic 606, *Revenue from Contracts with Customers*, is that an entity recognize revenue at an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring goods or services to a customer. Topic 606 requires entities to exercise more judgment when considering the terms of a contract than under Topic 605, *Revenue Recognition*. Topic 606 applies to all contracts with customers to provide goods or services in the ordinary course of business, except for contracts that are specifically excluded from its scope. Topic 606 does not apply to revenue associated with interest income on financial instruments, including loans and securities. Additionally, certain noninterest income streams, such as income from bank owned life insurance and gain and losses on sales of investment securities and loans, are out of scope of Topic 606.

Topic 606 is applicable to noninterest revenue streams such as (i) service charges and fees on deposit accounts, including account maintenance, transaction-based and overdraft services, and (ii) interchange fees, which represent fees earned when a debit card issued by the Company is used. These revenue streams are largely transaction-based and revenue is recognized upon completion of a transaction.

All of the Company's revenue from contracts with customers within the scope of ASC 606 is recognized in non-interest income in the consolidated statements of income.

Gains/losses on the sale of OREO are included in non-interest income/expense in the consolidated statements of income and are generally recognized when the performance obligation is complete. This is typically at delivery of control over the property to the buyer at the time of each real estate closing.

Stock-Based Compensation

Compensation cost is recognized for stock options, time-based restricted stock unit awards and performance-based restricted stock unit awards issued to employees and directors, based on the fair value of these awards at the date of grant. A Black-Scholes model is utilized to estimate the fair value of stock options, while the market price of the Company's common stock at the date of grant is used for time-based and performance-based restricted stock unit awards. Performance-based restricted stock unit awards contain vesting conditions which are based on predetermined performance targets that impact the number of shares that ultimately vest based on the level of targets achievement. These costs are recognized over the period in which the awards are expected to vest, on a straight-line basis. The costs for performance-based restricted unit awards are recognized over the period in which the awards are expected to vest as the Company believes the predetermined performance targets are probable to be fulfilled. For performance-based awards that do not vest because the predetermined performance targets are not fulfilled, no compensation cost is recognized, and any previously recognized compensation is reversed. The Company has elected to account for forfeitures of stock-based awards as they occur. Excess tax benefits and tax deficiencies relating to stock-based compensation are recorded as income tax expense or benefit in the consolidated statements of income when incurred.

Fair Value Measurement

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Current accounting guidance establishes 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 guidance 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 Company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Recent Accounting Guidance Not Yet Effective

In June 2016, the FASB issued ASU No. 2016-13, *Measurement of Credit Losses on Financial Instruments (Topic 326).* This ASU significantly changes how entities will measure credit losses for most financial assets and certain other instruments that aren't measured at fair value through net income. In issuing the standard, the FASB is responding to criticism that today's guidance delays recognition of credit losses. The standard will replace today's "incurred loss" approach with an "expected loss" model. The new model, referred to as the current expected credit loss ("CECL") model, will apply to: (1) financial assets subject to credit losses and measured at amortized cost, and (2) certain off-balance sheet credit exposures. This includes, but is not limited to, loans, leases, held-to-maturity securities, loan commitments, and financial guarantees. The CECL model does not apply to available-for-sale ("AFS") debt securities. ASU 2016-13 also expands the disclosure requirements regarding an entity's assumptions, models, and methods for estimating the allowance for loan and lease losses. In addition, public business entities will need to disclose the amortized cost balance for each class of financial asset by credit quality indicator, disaggregated by the year of origination. ASU No. 2016-13 is effective for interim and annual reporting periods beginning after December 15, 2022 for all entities, other than SEC filers that do not qualify as a Smaller Reporting Company as defined by the SEC. Entities will apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (i.e., modified retrospective approach). Management selected a third-party software and modeling solution to implement the new guidance and engaged the same third-party service provider to assist with the implementation and has subscribed to a third-party application vendor for economic forecasts. The Company has not yet determined the potential impact of the adoption of ASU 2016-13 to the consolidated financial statements.

In January 2017, the FASB issued ASU No. 2017-04, *Intangibles – Goodwill and Other (Topic 350): Simplifying the Accounting for Goodwill Impairment.* This guidance removes Step 2 of the goodwill impairment test, which requires a hypothetical purchase price allocation, and goodwill impairment will simply be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. All other goodwill impairment guidance will remain largely unchanged. Entities will continue to have the option to perform a qualitative assessment to determine if quantitative impairment test is necessary. The amendments in this Update are required for public business entities and other entities that have goodwill reported in their financial statements and have not elected the private company alternative for the subsequent measurement of goodwill. ASU No. 2017-04 is effective for interim and annual reporting periods beginning after December 15, 2022 for public business entities who are not SEC filers and one year later for all other entities. The Company is currently evaluating the effects of ASU 2017-04 on its financial statements and disclosures.

In April 2019, the FASB issued ASU 2019-04, Codification Improvements to Topic 326, Financial Instruments – Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments. This update made several clarifications and improvements to various topics. Topic A: Codification Improvements Resulting from the June and November 2018 Credit Losses Transition Resource Group (“TRG”) Meetings; Topic B: Codification Improvements to ASU 2016-13; Topic C: Codification improvements to ASU 2017-12, Derivatives and Hedging; Topic D: Codification improvements to ASU 2016-01 Financial Instruments Overall; and Topic E: Codification Improvements Resulting from the November 2018 Credit Losses TRG Meeting. Topics A, B and E, in ASU 2019-04 impact CECL implementation by clarifying guidance related to accrued interest receivable, recoveries, the effect of prepayments in determining the effective interest rate, vintage disclosure requirements related to line-of-credit arrangements and others. Transition requirements for these amendments are the same as ASU 2016-13, and will be adopted by the Company with ASU 2016-13. Topics C and D are not applicable to the Company, and therefore had no impact to the Company’s consolidated financial results.

In May 2019, the FASB issued ASU 2019-05, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instrument (ASU 2019-05) which grants entities with transition relief upon the adoption of ASU 2016-13 by providing an option to elect the fair value option on certain financial instruments measured at amortized cost. This ASU will be effective upon adoption of ASU 2016-13 (Topic 326). The impact of adopting the Topic 326 amendments is included within the impact of adoption of ASU 2016-13. The Company does not expect the adoption of these amendments will have a material impact to the consolidated financial statements.

In November 2019, the FASB issued ASU 2019-11, *Codification Improvements to Financial Instruments - Credit Losses* (Topic 326). The amendments in this Update clarify certain aspects of Topic 326 guidance issued in ASU 2016-13 including guidance providing transition relief for troubled debt restructurings ("TDRs"). This ASU will be effective upon adoption of ASU 2016-13 (Topic 326). The Company has not yet determined the potential impact of the adoption of ASU 2019-11 to the consolidated financial statements.

In December 2019, the FASB issued ASU 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes* (ASU 2019-12). The amendments in this Update simplify the accounting for income taxes by removing certain exceptions for investments, intraperiod allocations, and interim calculations, and add guidance to reduce the complexity of applying Topic 740. This ASU is effective for fiscal years beginning after December 15, 2021 and interim periods beginning after December 15, 2022, with early adoption permitted. The Company has not yet determined the potential impact of the adoption of ASU 2019-12 to the consolidated financial statements.

On March 12, 2020, the FASB issued ASU 2020-04, Facilitation of the Effects of Reference Rate Reform on Financial Reporting (ASU 2020-04), which provides optional expedients and exceptions for applying generally accepted accounting principles (GAAP) to contracts, hedging relationships, and other transactions affected by reference rate reform if certain criteria are met. The amendments apply only 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 are effective for all entities as of March 12, 2020 and may be adopted through December 31, 2022. The expedients and exceptions provided by the amendments do not apply to contract modifications made and hedging relationships entered into or evaluated after December 31, 2022, except for hedging relationships existing as of December 31, 2022, that an entity has elected certain optional expedients for and that are retained through the end of the hedging relationship. The Company is still currently evaluating the impact of ASU 2020-04 to the consolidated financial statements.

In January 2021, the FASB issued ASU 2021-01, Reference Rate Reform (Topic 848), which clarifies that certain optional expedients and exceptions in Topic 848 for contract modifications and hedge accounting apply to derivatives that are affected by the discounting transition. Specifically, certain provisions in Topic 848, if elected by an entity, apply to derivative instruments that use an interest rate for margining, discounting, or contract price alignment that is modified as a result of reference rate reform. Amendments in this Update to the expedients and exceptions in Topic 848 capture the incremental consequences of the scope clarification and tailor the existing guidance to derivative instruments affected by the discounting transition. The amendments in ASU 2021-01 are elective and apply to all entities that have derivative instruments that use an interest rate for margining, discounting, or contract price alignment that is modified as a result of reference rate reform. The amendments also optionally apply to all entities that designate receive-variable-rate, pay-variable-rate cross-currency interest rate swaps as hedging instruments in net investment hedges that are modified as a result of reference rate reform. The amendments in ASU 2021-01 are effective immediately for all entities. The Company is currently evaluating the amount, reviewing the contracts of our LIBOR-based products to ensure that our credit documentation provides for the flexibility to move to alternative reference rates, and choosing the substitute index. The Company does not expect the adoption of ASU 2021-01 will have a material impact to the consolidated financial statements.

In October 2021, the FASB issued ASU 2021-08, Business Combinations - Accounting for Contract Assets and Contract Liabilities from Contracts with Customers (Update). The amendments in this Update address how to determine whether a contract liability is recognized by an acquirer in a business combination. In addition, the Update addresses inconsistencies in the recognition and measurement of acquired contract assets and contract liabilities from revenue contracts in a business combination. The amendments in this Update are effective for the Company in fiscal years beginning after December 15, 2022 as well as all interim periods within those years. Early adoption is permitted. An entity that early adopts in an interim period should apply the amendments (1) retrospectively to all business combinations for which the acquisition date occurs on or after the beginning of the fiscal year that includes the interim period of early application, and (2) prospectively to all business combinations that occur on or after the date of initial application. The Company has not yet adopted the provisions of this Update. The Company does not currently anticipate the adoption of this Update will have a material impact on the Company's consolidated financial statements.

NOTE 2 – BUSINESS COMBINATIONS

Bank of Santa Clarita Acquisition

Following receipt of all necessary regulatory and shareholder approvals, on October 1, 2021, the Company completed its merger with BSCA, a California state-chartered bank headquartered in Santa Clarita, California, and operated one full-service branch in Santa Clarita. The acquisition of BSCA provides the Company with the opportunity to expand its footprint in Southern California.

Under the terms and conditions of the merger, each share of BSCA common stock was converted into the right to receive one (1) share of BCAL common stock. The Company issued 4,102,254 shares of BCAL common stock in exchange for the outstanding shares of BSCA's common stock. In addition, the

Company assumed each outstanding, unexercised option to acquire shares of BSCA common stock held by BSCA officers and employees who continued to be employed by the Company immediately following the merger, other than any stock options held by BSCA's Chairman & Chief Executive Officer (BSCA CEO). Total unexercised stock options were 90,731, of which 65,261 shares were vested and 25,470 shares were unvested. Total fair value of the assumed stock options was $832 thousand, of which $692 thousand for the vested stock options was included in the consideration and $141 thousand for the unvested stock options was considered unrecognized compensation cost and is being amortized over the remaining life of the stock options. BSCA's former CEO is a continuing employee and his unvested stock options will not be part of the assumed awards as BSCA's former CEO negotiated that such unvested options would become fully vested as a result of the merger. The Company recognized $84 thousand of compensation cost attributed to the accelerated vesting of his unvested awards upon the closing of the merger.

The following table represents the preliminary fair value of assets acquired and liabilities assumed of BSCA, as of October 1, 2021, recorded using the acquisition method of accounting:

(dollars in thousands)	**Fair Value**
Assets acquired:	
Cash and cash equivalents	$ 115,420
Securities available-for-sale	14,005
Loans held for investment:	268,811
Investments in restricted stocks	1,585
Other equity securities	62
Premises and equipment, net	13,131
Prepaid expenses	29
Income tax receivable	1,138
Deferred taxes, net	(1,226)
Accrued interest receivable	689
Cash surrender value of bank owned life insurance	8,884
Core deposit intangible	802
Other assets	2,281
Total assets acquired	**425,611**
Liabilities assumed:	
Deposits	342,263
FHLB advances	34,551
Accrued interest payable	20
Accrued expenses	419
Reserve for unused commitments	59
Other liabilities	93
Total liabilities assumed	**377,405**
Net assets acquired	**$ 48,206**
Purchase consideration:	

(dollars in thousands)		Fair Value
Fair value of shares of BCAL issued in the merger	$	64,596
Fair value of unvested stock options assumed		692
Less: repurchase of dissenter's rights		(21)
Total purchase consideration		**65,267**
Goodwill recognized	**$**	**17,061**

As the final BSCA tax return has not yet been completed, initial accounting for taxes was incomplete as of December 31, 2021. These preliminary fair values are estimates and are subject to adjustment for up to one year after the acquisition date or when additional information relative to the closing date fair values becomes available and such information is considered final, whichever is earlier. These changes could differ materially from what is presented above.

Goodwill represents the excess of the purchase consideration over the fair value of the net assets acquired and was primarily attributable to the expected synergies and economies of scale expected from combining the operations of the Company and BSCA. Goodwill is not deductible for U.S. income tax purposes and is not amortized. Rather, goodwill is tested for impairment annually, or more frequently if events or changes in circumstances indicate that it might be impaired, by comparing its carrying value to the reporting unit's fair value.

The core deposit intangible will be amortized over the expected account retention period, which was originally estimated at approximately 10 years or 120 months. The core deposit intangible will be evaluated periodically to determine the reasonableness of the projected amortization period by comparing actual deposit retention to projected retention.

The following table presents the amounts that comprise the fair value of loans acquired, excluding PCI loans, from BSCA at October 1, 2021:

(dollars in thousands)		Loans
Contractual amounts receivable	$	323,047
Contractual cash flows not expected to be collected		(2,625)
Expected cash flows, net		320,422
Interest component of expected cash flows		(51,611)
Fair value of acquired loans	$	268,811

There were no PCI loans acquired from BSCA at October 1, 2021.

The following table presents the total revenue and net income amounts related to BSCA's operations included in the Company's consolidated statements of income from the acquisition date of October 1, 2021 through December 31, 2021:

	Year Ended December 31,	
(dollars in thousands)	2021	
Net interest income and noninterest income	$	3,058
Net income	$	1,832

The following supplemental pro forma information presents certain financial results for the years ended December 31, 2021 and 2020 as if the acquisition of BSCA was effective as of January 1, 2020. The supplemental unaudited pro forma financial information included in the table below is based on various estimates and is presented for informational purposes only and does not indicate the financial condition or results of operations of the combined company that would have been achieved for the periods presented had the transactions been completed as of the date indicated or that may be achieved in the future.

Supplemental unaudited pro forma financial information:	**Year Ended December 31,**	
(dollars in thousands)	**2021**	**2020**
Net interest income and noninterest income	$ 77,839	$ 58,549
Net income	11,427	7,957
Net income per share:		
Basic	$ 0.79	$ 0.84
Diluted	$ 0.77	$ 0.82

<u>CalWest Bancorp Acquisition</u>

At the end of May 2020, the Company acquired CalWest Bancorp of Irvine, California, and its subsidiary, CalWest Bank ("CalWest"), which operated four branch offices, in Irvine, Rancho Santa Margarita, and Huntington Beach in Orange County, and Redlands, located in San Bernardino County. Pursuant to a definitive agreement dated October 19, 2019, as amended April 28, 2020, CalWest Bancorp shareholders received $0.35 per share in a cash only transaction for a total consideration of $25.9 million. The acquisition of CalWest provides the Company with the opportunity to expand its footprint in Southern California. The acquisition was accounted for using the acquisition method of accounting. The following table represents the fair value of assets and liabilities acquired from CalWest.

(dollars in thousands)	**Fair Value**
Assets acquired:	
Cash and cash equivalents	$ 62,878
FHLB stock and investment securities	10,912
Loans	220,432
Premises and equipment	555
Deferred tax assets, prepaids and other assets	15,966
Core deposit intangible	47
Total assets acquired	310,790
Liabilities assumed:	
Deposits	241,010
Borrowings	43,101
Other liabilities	4,269
Total liabilities assumed	288,380
Net assets acquired	22,410

(dollars in thousands)		**Fair Value**
Total consideration		**25,913**
Goodwill recognized	**$**	**3,503**

Goodwill represents the excess of the purchase consideration over the fair value of the net assets acquired and was primarily attributable to the expected synergies and economies of scale expected from combining the operations of the Company and CalWest. Goodwill is not deductible for U.S. income tax purposes and is not amortized. Rather, goodwill is tested for impairment annually, or more frequently if events or changes in circumstances indicate that it might be impaired, by comparing its carrying value to the reporting unit's fair value.

The core deposit intangible will be amortized over the expected account retention period, which was originally estimated at approximately 10 years or 120 months. The core deposit intangible will be evaluated periodically to determine the reasonableness of the projected amortization period by comparing actual deposit retention to projected retention.

As part of this transaction, the Bank purchased three related loans that were classified as purchased credit impaired loans. These loans were participations in a shared national credit which, at acquisition, showed evidence of deterioration of credit quality since origination and it was probable, at acquisition, that not all contractually required payments would be collected. The contractual balance of these loans at acquisition was $1.4 million and the carrying amount, or fair value was $252 thousand.

The following table presents the amounts that comprise the fair value of loans acquired, excluding PCI loans, from CalWest at May 31, 2020:

(dollars in thousands)		**Loans**
Contractual amounts receivable	$	277,162
Contractual cash flows not expected to be collected		(2,906)
Expected cash flows, net		274,256
Interest component of expected cash flows		(54,076)
Fair value of acquired loans	$	220,180

NOTE 3 - DEBT SECURITIES

Debt securities have been classified as available-for-sale securities in the consolidated balance sheets according to management's intent. The carrying amount of available-for-sale debt securities and their approximate fair values at December 31 were as follows:

(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
December 31, 2021				
U.S. government and agency and government sponsored enterprise securities:				
Mortgage-backed securities	$ 17,419	$ 10	$ (114)	$ 17,315
SBA securities	11,421	37	(58)	11,400
U.S. Treasury	2,863	—	(82)	2,781
U.S. Agency	6,500	—	(21)	6,479
Collateralized mortgage obligations	10,398	12	(122)	10,288
Taxable municipal	5,314	228	(20)	5,522
Tax exempt bank-qualified municipals	1,706	76	—	1,782
	$ 55,621	$ 363	$ (417)	$ 55,567
December 31, 2020				
U.S. government and agency securities:				
Mortgage-backed securities	$ 5,419	$ 21	$ (10)	$ 5,430
SBA securities	9,860	11	(27)	9,844
Taxable municipals	4,799	338	—	5,137
Tax exempt bank-qualified municipals	1,708	83	—	1,791
Corporate debt securities	2,500	—	—	2,500
	$ 24,286	$ 453	$ (37)	$ 24,702

The amortized cost and estimated fair value of all available-for-sale debt securities as of December 31, 2021 by contractual maturities are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(dollars in thousands)	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 915	$ 928
Due after one year through five years	8,723	8,931
Due after five years through ten years	23,638	23,530
Due after ten years	22,344	22,178
	$ 55,620	$ 55,567

At December 31, 2021, there were no holdings of securities of any one issuer in an amount greater than 10% of our shareholders' equity.

There were $4.0 million and $10.6 million in sales and maturities of available-for-sale debt securities, resulting a net gain of $46 thousand and $574 thousand during the years ended December 31, 2021 and 2020. There were $4.4 million and $1.4 million in paydowns of available-for-sale debt securities during the years ended December 31, 2021 and 2020. There were $26.0 million and $13.7 million in purchases of available-for-sale debt securities during the years ended December 31, 2021 and 2020. The Company acquired $14.0 million of available-for-sale debt securities from the merger with BSCA in 2021.

The gross unrealized losses and related estimated fair values of all available-for-sale debt securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2021 and 2020 are summarized as follows:

	Less than Twelve Months		Over Twelve Months		Total	
(dollars in thousands)	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Estimated Fair Value
December 31, 2021:						
U.S. government and agency and government sponsored enterprise securities:						
Mortgage-backed securities:	$ (114)	$ 14,834	$ —	$ —	$ (114)	$ 14,834
SBA securities	(58)	6,406	—	—	(58)	6,406
U.S. Treasury	(82)	2,781	—	—	(82)	2,781
Agency	(21)	6,479	—	—	(21)	6,479
Collateralized mortgage obligations	(122)	7,856	—	—	(122)	7,856
Taxable municipals	(20)	490	—	—	(20)	490
Tax exempt bank-qualified municipals	—	—	—	—	—	—
	$ (417)	$ 38,846	$ —	$ —	$ (417)	$ 38,846
December 31, 2020:						
U.S. government and agency securities:						
Mortgage-backed securities:	$ (4)	$ 1,506	$ (6)	$ 341	$ (10)	$ 1,847
SBA securities	(27)	8,298	—	—	(27)	8,298
	$ (31)	$ 9,804	$ (6)	$ 341	$ (37)	$ 10,145

As of December 31, 2021, there was no debt security that had been in a continual loss position for over twelve months. As of December 31, 2020, there was one debt security, that had been in a continual loss position for over twelve months. Management evaluates debt securities for other-than-temporary impairment, taking into consideration the extent and length of time the fair value has been less than cost, the financial condition of the issuer and whether the Company has the intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in fair value. As of December 31, 2021 and 2020, no unrealized losses are deemed to be other-than-temporary.

Debt securities with a carrying value of $7.9 million and $8.5 million were pledged to secure credit facilities at the Federal Home Loan Bank of San Francisco ("FHLB") at December 31, 2021 and 2020, respectively,

Restricted Stock

As a member of the FRB System, the Bank must hold FRB stock in an amount equal to 3% of the Bank's common stock and additional paid-in capital. An investment in the equity stock of the FHLB of San Francisco is required for membership; the amount of the required investment is a function of the Bank's outstanding mortgage assets and outstanding advances from the FHLB. During the year ended December 31, 2021, the Company acquired $1.6 million in FHLB stock in the BSCA merger and purchased $1.3 million of FRB stock and $1.0 million of FHLB stock. During the year ended December 31, 2020, the Company acquired $783 thousand in FRB stock and $998 thousand in FHLB stock in the CalWest Bank acquisition and purchased $426 thousand of FRB stock and $280 thousand of FHLB stock.

The table below summarizes the Bank's restricted stock investments at December 31:

(dollars in thousands)	2021	2020
Federal Reserve Bank	$ 5,268	$ 3,955
Federal Home Loan Bank	7,225	4,630
	$ 12,493	$ 8,585

Other Equity Securities Without A Readily Determinable Fair Value

The Company also has equity securities in the form of capital stock invested in two different banker's bank stocks which totaled $350 thousand and $288 thousand at December 31, 2021 and 2020. These equity securities are reported in other assets in the consolidated balance sheets. During the years ended December 31, 2021 and 2020, the Company evaluated the carrying value of these equity securities and determined that they were not impaired, and no loss related to changes in the fair value of these equity securities was recognized.

In connection with the BSCA merger, the Company acquired a $1.8 million limited partnership investment in WNC California Preservation Equity Fund, L.P. ("CAPEF") and a $5.0 million commitment in WNC California Preservation Equity Fund 2, L.P. ("CAPEF II"). Both equity funds were formed for the purpose of acquiring, holding, selling and disposing of direct or indirect equity in multi-family projects that qualify as affordable housing. These equity securities are recorded at cost and are included in other assets in the consolidated balance sheets. Cash distributions from the partnerships that are considered earnings are recorded in noninterest income in the consolidated statements of income while distributions considered return of capital are recorded as a reduction of the Company's investment included in other assets in the consolidated balance sheets. During the year ended December 31, 2021, there were no capital contributions made to these equity securities and there was a $9 thousand cash distribution that was recorded in the noninterest income. At December 31, 2021, the Company evaluated the carrying value of these equity investments and determined that it was not impaired, and no loss was recognized related to changes in the fair value.

NOTE 4 - LOANS

The Company's loan portfolio consists primarily of loans to borrowers within its markets of Counties of San Diego, Orange and Los Angeles, California, as well as the Coachella Valley in Riverside County, California. Although the Company seeks to avoid concentrations of loans to a single industry or based upon a single class of collateral, real estate and real estate associated businesses are among the principal industries in the Company's market area. The Company's loan portfolio in real estate secured credit represented 77% of total loans at December 31, 2021.

The composition of the Company's loan portfolio at December 31, 2021 and 2020 was as follows:

(dollars in thousands)	**2021**	**2020**
Construction and land development	$ 77,629	$ 31,375
Real estate - other:		
1-4 family residential	133,993	103,367
Multifamily residential	175,751	111,816
Commercial real estate and other	766,824	404,856
Commercial and industrial [(1)]	349,023	577,609
Consumer	1,528	4,858
Loans [(2)]	1,504,748	1,233,881
Allowance for loan losses	(11,657)	(10,255)
Net loans	$ 1,493,091	$ 1,223,626

1. *Includes PPP loans with total outstanding principal of $60.3 million and $412.1 million and net unearned fees of $1.6 million and $5.3 million at December 31, 2021 and 2020.*
2. *Loans held for investment includes net unearned fees of $2.8 million and $5.3 million and net unearned discount of $2.8 million and $4.1 million at December 31, 2021 and 2020.*

The Company has originated loans that are serviced for others, including loans partially guaranteed by the SBA, some of which have been sold in the secondary market, as well as commercial real estate loans for investors and other participating financial institutions. The portfolio of loans serviced for other parties was approximately $29.6 million and $39.0 million at December 31, 2021 and 2020.

The Company has pledged loans with a carrying value of $323.2 million to collateralize credit facilities at the FHLB of San Francisco and the FRB as of December 31, 2021.

A summary of the changes in the allowance for loan losses as of December 31 follows:

(dollars in thousands)	**2021**	**2020**
Balance, beginning of year	$ 10,255	$ 5,363
Provision for loan losses	1,200	4,552
Charge-offs	—	(105)
Recoveries	202	445
Net recoveries	202	340
Balance, end of year	$ 11,657	$ 10,255

A summary of allowance of loan losses and loan balance disclosed by portfolio segment and also by loans individually evaluated and loans collectively evaluated for impairment as of December 31, 2021 and 2020 and for the years then ended follows:

(dollars in thousands)	**Construction and Land Development**	**Real Estate - Other**	**Commercial & Industrial**	**Consumer**	**Total**
December 31, 2021					
Allowance for loan losses:					
Beginning of year	$ 443	$ 7,356	$ 2,413	$ 43	$ 10,255
Provisions (reversals)	223	1,064	(42)	(45)	1,200
Charge-offs	—	—	—	—	—
Recoveries	—	21	177	4	202
End of year	$ 666	$ 8,441	$ 2,548	$ 2	$ 11,657
Specific reserves	$ —	$ 15	$ 16	$ —	$ 31
General reserves	666	8,426	2,532	2	11,626
	$ 666	$ 8,441	$ 2,548	$ 2	$ 11,657
Loans evaluated for impairment:					
Individually	$ —	$ 743	$ 58	$ 8	$ 809
Collectively	77,629	1,075,825	348,965	1,520	1,503,939
	$ 77,629	$ 1,076,568	$ 349,023	$ 1,528	$ 1,504,748
December 31, 2020					
Allowance for loan losses:					
Beginning of year	$ 233	$ 3,876	$ 1,239	$ 15	$ 5,363
Provisions	210	3,561	746	35	4,552
Charge-offs	—	(92)	—	(13)	(105)
Recoveries	—	11	428	6	445
End of year	$ 443	$ 7,356	$ 2,413	$ 43	$ 10,255
Specific reserves	$ —	$ —	$ —	$ —	$ —
General reserves	443	7,356	2,413	43	10,255
	$ 443	$ 7,356	$ 2,413	$ 43	$ 10,255
Loans evaluated for impairment:					
Individually	$ —	$ 130	$ 734	$ —	$ 864
Collectively	31,375	619,909	576,875	4,858	1,233,017
	$ 31,375	$ 620,039	$ 577,609	$ 4,858	$ 1,233,881

The Company's methodology for estimating the allowance for loan losses results in a range of potential reserves, including an estimate primarily based on the Company's historical loss factors for collective impairment and also a high and low range based on analysis of peer data for collective impairment factors.

The Company categorizes loans using risk ratings based on relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, collateral adequacy, credit documentation, and current economic trends, among other factors. Larger, non-homogeneous loans such as commercial real estate and commercial and industrial loans are analyzed individually for risk rating assessment. For purposes of risk classification, 1-4 Family Residential loans for investment purposes are evaluated with commercial real estate loans. This analysis is performed on an ongoing basis as new information is obtained. The Company uses the following definitions for risk ratings:

Pass - Loans classified as pass include loans not meeting the risk ratings defined below.

Special Mention - Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

Substandard - Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Impaired - A loan is considered impaired, when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Additionally, all loans classified as troubled debt restructurings are considered impaired.

Based on the most recent analysis performed, the risk category of loans by class of loans as of December 31, 2021 and 2020 follows:

(dollars in thousands)	Pass	Special Mention	Substandard	Impaired	Total
December 31, 2021					
Construction and land development	$ 77,519	$ —	$ 110	$ —	$ 77,629
Real estate - other:					
1-4 family residential	133,872	—	53	68	133,993
Multifamily residential	175,751	—	—	—	175,751
Commercial real estate and other	764,864	39	1,246	675	766,824
Commercial and industrial	346,702	1,775	488	58	349,023
Consumer	1,520	—	—	8	1,528
	$ 1,500,228	$ 1,814	$ 1,897	$ 809	$ 1,504,748

(dollars in thousands)	Pass	Special Mention	Substandard	Impaired	Total
December 31, 2020					
Construction and land development	$ 31,256	$ —	$ 119	$ —	$ 31,375
Real estate - other:					
1-4 family residential	99,156	4,088	—	123	103,367
Multifamily residential	111,816	—	—	—	111,816
Commercial real estate and other	403,481	241	1,127	7	404,856
Commercial and industrial	576,332	—	543	734	577,609
Consumer	4,858	—	—	—	4,858
	$ 1,226,899	$ 4,329	$ 1,789	$ 864	$ 1,233,881

A summary of past due loans, loans still accruing and nonaccrual loans as of December 31, 2021 and 2020 follows:

	Still Accruing		
(dollars in thousands)	30-89 Days Past Due	Over 90 Days Past Due	Nonaccrual
December 31, 2021			
Construction and land development	$ —	$ —	$ —
Real estate:			
1-4 family residential	569	—	68
Multifamily residential	—	—	—
Commercial real estate and other	—	—	675
Commercial and industrial	477	—	58
Consumer	—	—	8
	$ 1,046	$ —	$ 809

	Still Accruing		
(dollars in thousands)	30-89 Days Past Due	Over 90 Days Past Due	Nonaccrual
December 31, 2020			
Construction and land development	$ —	$ —	$ —
Real estate:			
1-4 family residential	87	—	123
Multifamily residential	—	—	—
Commercial real estate and other	2,198	—	7
Commercial and industrial	—	—	734
Consumer	—	—	—
	$ 2,285	$ —	$ 864

Below is a summary of the Company's recorded investment in impaired loans disclosed by loan type outstanding at December 31, 2021 and 2020.

(dollars in thousands)	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2021					
Construction and land development	$ —	$ —	$ —	$ —	$ —
Real estate:					
1-4 family residential	182	68	15	77	—
Multifamily residential	—	—	—	—	—
Commercial real estate and other	1,023	675	—	172	—
Commercial and Industrial	992	66	16	99	—
Consumer	—	—	—	—	—
	$ 2,197	$ 809	$ 31	$ 348	$ —

(dollars in thousands)	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2020					
Construction and land development	$ —	$ —	$ —	$ —	$ —
Real estate:					
1-4 family residential	292	123	—	148	2
Multifamily residential	—	—	—	—	—
Commercial real estate and other	52	7	—	10	—
Commercial and industrial	3,280	735	—	895	—
Consumer	13	—	—	7	—
	$ 3,637	$ 865	$ —	$ 1,060	$ 2

No additional funds are committed to be advanced on impaired loans. The principal balance of impaired loans that was guaranteed by the SBA was $45 thousand and $523 thousand at December 31, 2021 and 2020.

The Company did not have any loans that have been modified in troubled debt restructurings as of December 31, 2021 and 2020. No loans were modified during 2021 and 2020 which resulted in a troubled debt restructuring.

NOTE 5 - PREMISES AND EQUIPMENT

A summary of premises and equipment as of December 31 follows:

(dollars in thousands)	2021	2020
Land	$ 8,916	$ 1,506
Building	7,536	1,946
Leasehold improvements	3,774	3,655
Furniture & fixtures	1,900	1,532
Computer & other equipment	3,046	2,519
	25,172	11,158
Less: Accumulated depreciation and amortization	(5,533)	(4,641)
Total	$ 19,639	$ 6,517

Depreciation and amortization expense on premises and equipment was $1.4 million and $1.1 million for 2021 and 2020.

Substantially all leases are operating leases for corporate offices and branch locations and loan production offices. The amount of the lease liability and ROU asset is impacted by the lease term and the discount rate applied to determine the present value of future lease payments. The remaining terms of operating leases range from 4 months to 7.1 years.

Most leases include one or more options to renew, with renewal terms that can extend the lease term by varying amounts. The exercise of renewal options is at the sole discretion of the Company. Renewal option periods were not included in the measurement of ROU assets and lease liabilities as they are not considered reasonably certain of exercise.

During the year ended December 31, 2021, Management decided to halt the opening of a new branch office in La Jolla, California and the Company recognized a $287 thousand impairment of the ROU assets. The impairment of the ROU assets was based on a discounted cash flow of lease payments net of sublease income. The impairment charge is included in occupancy and equipment expenses in the consolidated statements of income for the year ended December 31, 2021. There were no such impairment charges for the year ended December 31, 2020.

The ROU assets, lease liabilities and supplemental information at December 31 are shown below.

(dollars in thousands)	2021	2020
Operating lease ROU assets	$ 8,069	$ 8,534
Operating lease liability	$ 9,002	$ 9,397
Weighted average remaining lease term, in years	5.04	5.82
Weighted average discount rate	5.5%	5.3%

Variable lease cost primarily represents variable payments such as common area maintenance and utilities. The following table represents lease costs and other lease information for the years ending December 31:

(dollars in thousands)	2021	2020
Lease costs:		
Operating lease	$ 2,247	$ 1,965
Variable lease	366	301
Short-term lease	157	51
Total lease costs	$ 2,770	$ 2,317
Other information:		
Cash paid for amounts included in lease liabilities	$ 2,404	$ 2,164
ROU assets obtained for new operating lease obligations	$ 3,463	$ 2,224

Lease liabilities as of December 31, 2021, mature as indicated below:

(dollars in thousands)	Amount
Twelve months ending December 31:	
2022	$ 2,356
2023	2,313
2024	1,834
2025	1,169
2026	1,021
Thereafter	1,685
Total future minimum lease payments	10,378
Less: imputed interest	1,376
Present value of net future minimum lease payments	$ 9,002

NOTE 6 - GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill is the excess purchase price over the fair value of all identifiable assets and liabilities acquired and totals $36.8 million and $19.7 million at December 31, 2021 and 2020, which included $17.1 million recognized in the BSCA acquisition and $3.5 million recognized in the CalWest acquisition (refer to Note 2 – Business Combinations). Current accounting standards require that goodwill be reviewed for impairment at least annually. The Company has performed a qualitative assessment for potential impairment as of December 31, 2021 and 2020, and as a result of that assessment has determined that there has been no impairment to the goodwill that was recorded as a result of fair value accounting for business combinations. The following table presents changes in the carrying amount of goodwill for the periods indicated:

(dollars in thousands)	2021	2020
Beginning of the year	$ 19,723	$ 16,221
Goodwill from business combination	17,061	3,502
End of year	$ 36,784	$ 19,723

As a result of three acquisitions completed from 2010 through 2014, each of which included branch offices in the Coachella Valley, the Company recorded core deposit intangibles totaling $1.1 million. In 2018, the Company recorded $2.5 million of core deposit intangibles for the branch offices located in the Los Angeles market as a result of the Americas United Bank acquisition. In 2020, the Company acquired CalWest Bank and recorded core deposit intangibles of $47 thousand related to branch offices primarily in Orange County. In 2021, the Company acquired BSCA and recorded core deposit intangibles of $802 thousand. The core deposit intangibles are being amortized over periods of seven to ten years. Amortization expense for the years ended December 31, 2021 and 2020 was $364 thousand and $386 thousand, respectively. Accumulated amortization as of December 31, 2021 and 2020 was $2.2 million and $1.8 million.

For the years ended December 31, 2021 and 2020, the Company recognized the CDI amortization indicated in the table below.

(dollars in thousands)	**2021**	**2020**
Gross balance, beginning of year	$ 3,675	$ 3,628
Additions	802	47
Reduction from branch sale	(292)	—
Gross balance, end of year	$ 4,185	$ 3,675
Accumulated amortization:		
Balance, beginning of year	$ (1,799)	$ (1,413)
Amortization	(364)	(386)
Balance, end of period	(2,163)	(1,799)
Net core deposit intangible, end of year	$ 2,022	$ 1,876

Future estimated amortization expense for each of the next five years is as follows:

(dollars in thousands)	**Amount**
2022	$ 398
2023	355
2024	271
2025	248
2026	227
Thereafter	523
	$ 2,022

NOTE 7 - DEPOSITS

Time deposits that exceeded the FDIC insurance limit of $250,000 amounted to $66.6 million and $67.2 million as of December 31, 2021 and 2020. The Company participates in a state public deposits program that allows it to receive deposits from the state or from political subdivisions within the state in amounts that would not be covered by the FDIC. This program provides a stable source of funding to the Company. As of December 31, 2021, total collateralized deposits, including the deposits of State of California and their public agencies, were $10.1 million and were collateralized by letters of credit issued by the FHLB under the Company's secured line of credit with the FHLB. See Note 8 – *Borrowing Arrangements* for additional information regarding the FHLB secured line of credit.

At December 31, 2021, the scheduled maturities of time deposits are as follows:

(dollars in thousands)	**Amount**
2022	$74,037
2023	12,899
2024	9,322
2025	2,069
2026	3,963
	$102,290

NOTE 8 - BORROWING ARRANGEMENTS

A summary of outstanding borrowings as of December 31 follows:

(dollars in thousands)	**2021**	**2020**
FHLB advances	$ —	$ 10,000
FRB PPP liquidity facility	—	169,383
Subordinated notes	17,675	17,580
Subordinated debentures	2,734	2,685
Total borrowings	$ 20,409	$ 199,648

The Company has a credit facility with the Federal Home Loan Bank of San Francisco ("FHLB"), under which the Company may enter borrowing agreements under various terms and conditions, subject to pledging qualifying collateral, such as investment securities and loans. The Company has investment securities with a carrying value of $7.9 million and loans with an unpaid principal balance of approximately $302.0 million pledged with the FHLB at December 31, 2021. Subsequent to the BSCA merger, the Company paid off $34 million in FHLB fixed rate advances prior to maturity and incurred a prepayment penalty of $551 thousand, which was considered in the initial fair value.

The Company had no outstanding FHLB borrowings at December 31, 2021. At December 31, 2020, the Company participated in the FHLB San Francisco's new Recovery Advance loan program for $10.0 million at zero percent interest with a maturity date in May 2021. As of December 31, 2021, FHLB has also issued a $12 million letter of credit to secure public deposits of the Company. Available remaining borrowing capacity from the FHLB at December 31, 2021, based upon collateral pledged was approximately $116.0 million.

The Company has credit availability at the Federal Reserve discount window to the extent of collateral pledged. The Company has pledged loan collateral at December 31, 2021 with a book value of $19.1 million. The Company had no discount window borrowings at December 31, 2021 or 2020. Additionally, the Company participated in the FRB Paycheck Protection Program Liquidity Facility (PPPLF) in 2020 and had pledged PPP loans of $169.4 million as collateral to secure advances under this program at December 31, 2020. The PPPLF advances had an interest at a fixed rate of 0.35%, had maturities of less than two years, but must be repaid as PPP loans are paid off, unless previously paid off by the Company, at its option. The PPPLF advances were paid off in March 2021.

On May 28, 2020, the Company issued $18 million of 5.50% Fixed-to-Floating Rate Subordinated Notes Due 2030 (the "Notes"). The Notes mature March 25, 2030, accrue interest at a fixed rate of 5.50% through the fixed rate period to March 26, 2025, after which interest accrues at a floating rate of 90-day SOFR plus 350 basis points, until maturity, unless redeemed early, at the Company's option, after the end of the fixed rate period. Issuance costs of $475,000 were incurred and are being amortized over the first 5-year fixed term of the Notes; unamortized issuance costs at December 31, 2021 and 2020, were $325 thousand and $420 thousand. The net unamortized issuance costs are netted against the balance and recorded in the borrowings in the consolidated balance sheets. The amortization expenses are recorded in the interest expense on the consolidated statements of income. At December 31, 2021, the Company was in compliance with all covenants and terms of the Notes.

In the acquisition of CalWest Bancorp, the Company assumed $3.1 million of junior subordinated deferrable interest debentures (the "Debentures") which were issued to CalWest Statutory Trust I (the "Trust"). The Debentures mature September 17, 2033, and accrue interest at three-month LIBOR plus 2.95%, with an effective rate was 3.02% at December 31, 2021. The Company also acquired a 3% common interest in the Trust, which is comprised of mandatorily redeemable preferred securities. At acquisition, the Debentures were valued at a premium of $408 thousand which was included in the initial carrying value of subordinated securities, which is being amortized over the remaining term of the borrowing.

The Company has two overnight unsecured credit lines from correspondent banks totaling $60.0 million. The lines are subject to annual review. There were no outstanding borrowings under these lines at December 31, 2021 or 2020.

NOTE 9 - INCOME TAXES

The income tax expense for the years ended December 31, is comprised of the following:

(dollars in thousands)	2021	2020
Current tax expense:		
Federal	$ 2,152	$ 2,604
State	1,188	1,533
Total current tax expense	3,340	4,137
Deferred taxes	137	(2,091)
Total income tax expense	$ 3,477	$ 2,046

A comparison of the federal statutory income tax rates to the Company's effective income tax rates at December 31 follows:

	2021		2020	
(dollars in thousands)	**Amount**	**Rate**	**Amount**	**Rate**
Statutory federal income tax provision	$ 2,979	21.0 %	$ 1,421	21.0 %
State taxes	1,246	8.8 %	593	8.8 %
Employee stock-based compensation	(876)	(6.2)%	45	0.7 %
Merger expenses	185	1.3 %	60	0.9 %
Other	(57)	(0.4)%	(73)	(1.0)%
	$ 3,477	24.5 %	$ 2,046	30.4 %

The Company is subject to Federal and California franchise tax. Income tax returns for the years ended after December 31, 2017 are open to audit by the Federal authorities and income tax returns for the years ending after December 31, 2016 are open to audit by California authorities. There were no interest and penalties related to unrecognized tax benefits in income tax expense at December 31, 2021 and 2020. The total amount of unrecognized tax benefits was zero at December 31, 2021 and 2020.

Deferred taxes are a result of differences between income tax accounting and generally accepted accounting principles with respect to income and expense recognition. The following is a summary of the components of the net deferred tax asset accounts recognized in the accompanying consolidated balance sheets at December 31:

(dollars in thousands)	**2021**	**2020**
Deferred tax assets:		
Allowance for loan losses	$ 3,449	$ 2,918
Organizational expenses	92	111
Stock-based compensation	582	433
Fair value adjustment on acquired loans	759	1,085
Net operating loss carryforward	1,643	1,723
Accrued expenses	860	1,324
California franchise tax	250	322
Unrealized loss on securities available for sale	16	—
Other	3,300	343
Total deferred tax assets	$ 10,951	$ 8,259
Deferred tax liabilities:		
Deferred loan costs	$ (1,233)	$ (873)
Core deposit intangibles	(550)	(493)
Depreciation differences	(1,098)	(424)
Unrealized gain on securities available for sale	—	(121)
Other	(3,001)	(52)
Total deferred tax liabilities	(5,882)	(1,963)
Net deferred tax assets	$ 5,069	$ 6,296

Section 382 of the Internal Revenue Code imposes an annual limitation on a corporation's ability to use any net unrealized built-in losses and other tax attributes, such as net operating loss and tax credit carryforwards, when it undergoes a 50% ownership change over a designated testing period not to exceed three years.

On June 29, 2020, California Assembly Bill 85 (A.B. 85) was signed into law. A.B. 85 suspends the use of the net operating loss ("NOL") for the 2020, 2021, and 2022 tax years. For NOL incurred in tax years before 2020 for which a deduction is denied, the carryover period is extended by three years. On February 9, 2022, Senate Bill 113 ("S.B. 113") S.B. 113 was signed into law, and among other changes, S.B. 113 reinstates the California NOL deductions for tax years beginning in 2022, in effect shortening the suspension period for NOL deductions from A.B. 85 by one year.

As a result of the acquisition of CalWest, the Company has federal and California Section 382 limited net operating loss carryforwards of approximately $5.4 million and $6.0 million at December 31, 2021, which are scheduled to begin expiring in 2029 for federal and 2031 for California. The federal and California net operating loss carryforwards are subject to annual limitations of $381 thousand each. The Company expects to fully utilize the recorded federal and California net operating loss carryforwards before they expire.

NOTE 10 - EARNINGS PER SHARE ("EPS")

The following is a reconciliation of net income and shares outstanding to the income and number of shares used to compute EPS:

(dollars in thousands, except share and per share data)	**2021**	**2020**
Net Income	$ 10,709	$ 4,722
Weighted average common shares outstanding - basic	14,404,767	9,480,736
Dilutive effect of outstanding:		
Stock options and unvested stock grants	507,773	219,667
Weighted average common shares outstanding - diluted	14,912,540	9,700,403
Earnings per common share - basic	$ 0.74	$ 0.50
Earnings per common share - diluted	$ 0.72	$ 0.49

A total of 275,171 and 465,883 unvested performance based restricted stock grants have been excluded from the computation of diluted EPS for 2021 and 2020 because the performance conditions had not been met as of December 31, 2021 and 2020. At December 31, 2021 and 2020, there were 85,858 and zero restricted stock units and 180,804 and 204,500 stock options, respectively, that were not included in the computation of diluted earnings per share, because they were anti-dilutive.

NOTE 11 - RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Company has granted loans to certain directors and their related interests with which they are associated. In the Company's opinion, all loans and loan commitments to such parties are made on substantially the same terms including interest rates, and collateral, as those prevailing at the time for comparable transactions with unrelated clients.

The balance of these loans outstanding and activity in related party loans for the periods ended December 31, 2021 and 2020 follows:

(dollars in thousands)	**2021**	**2020**
Balance at beginning of year	$ 7,033	$ 3,179
New credit granted	3,324	5,250
Credit repayments	(98)	(1,396)
Balance at end of year	$ 10,259	$ 7,033

Directors and related interests deposits at December 31, 2021 and 2020, amounted to approximately $5.6 thousand and $2.9 million.

The Company leases the Ramona branch office from a principal shareholder under an operating lease expiring in 2022 on terms considered to be prevailing in the market at the time of the lease. Total lease expense for each of 2021 and 2020 was $40 thousand and $38 thousand and future minimum lease payments under the lease were $13 thousand as of December 31, 2021.

NOTE 12 - COMMITMENTS AND CONTINGENCIES

In the ordinary course of business, the Company enters into financial commitments to meet the financing needs of its customers. These financial commitments include commitments to extend credit and standby letters of credit. Those instruments involve to varying degrees, elements of credit and interest rate risk not recognized in the Company's financial statements.

Commitments to extend credit are agreements to lend to a client as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total amounts do not necessarily represent future cash requirements. The Company evaluates each client's credit worthiness on a case-by-case basis. Collateral may or may not be required based on management's credit evaluation of the customer. The majority of the Company's commitments to extend credit and standby letters of credit are secured by real estate.

The Company's exposure to loan loss in the event of nonperformance on commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments as it does for loans reflected in the consolidated financial statements.

In connection with the BSCA merger, the Company assumed a $5.0 million commitment in WNC California Preservation Equity Fund 2, L.P. ("CAPEF II"). Such equity fund was formed for the purpose of acquiring, holding, selling and disposing of direct or indirect equity in multi-family projects that qualify as affordable housing. Capital contributions are called for up to an amount specified in the partnership agreement. At December 31, 2021, the Company had unfunded commitments to contribute capital to this partnership investment totaling $5.0 million.

The Company had the following outstanding financial commitments whose contractual amount represents potential credit risk at December 31:

(dollars in thousands)	2021	2020
Commitments to extend credit	$ 405,507	$ 203,348
Letters of credit issued to customers	12,210	7,004
Commitments to contribute capital to other equity investments	5,000	—
	$ 422,717	$ 210,352

The Company evaluates the loss exposure for unfunded commitments to extend credit following the same principles used for the allowance for loan losses, with consideration for experienced utilization rates on client credit lines and the inherently lower risk of unfunded commitments relative to disbursed commitments. The Company recognized $600 thousand provision for unfunded loan commitments for the year ended December 31, 2021 and did not recognize any provision for unfunded loan commitments for the year ended December 31, 2020. The provision for unfunded loan commitments is included in other expense in the consolidated statements of income. The reserve for unfunded commitments was $804 thousand and $145 thousand at December 31, 2021 and 2020. The reserve for unfunded commitments is included in other liabilities in the consolidated balance sheets.

In 2016 and 2021, the Company entered into deferred compensation agreements with certain key officers. Under these agreements, the Company is obligated to provide, upon retirement, a 10-year benefit to the officers. The annual benefits range from $16 thousand to $75 thousand. The estimated present value of future benefits to be paid is being accrued over the period from the effective date of the agreements until the expected retirement dates of the participants. The expense incurred for these agreements in 2021 and 2020 was $311 thousand and $186 thousand. The Company is a beneficiary of life insurance policies that have been purchased as a method of financing the benefits under these agreements.

In the normal course of business, the Company is named or threatened to be named as a defendant in various lawsuits. The Company is from time to time engaged in various litigation matters including the defense of claims of improper or fraudulent loan practices or lending violations, and other matters, and the Company has a number of unresolved claims pending. In addition, as part of the ordinary course of business, the Company is party to litigation involving claims to the ownership of funds in particular accounts, the collection of delinquent accounts, challenges to security interests in collateral, and foreclosure interests that are incidental to our regular business activities. While the ultimate liability with respect to these other litigation matters and claims cannot be determined at this time, the Company believes that damages, if any, and other amounts relating to pending matters are not likely to be material to the consolidated balance sheets or consolidated statements of income.

NOTE 13 - STOCK-BASED COMPENSATION PLAN

Under the Company's 2001 Stock Option Plan (the "2001 Plan"), as amended, stock options were granted to eligible employees and directors. The 2001 Plan terminated November 8, 2011, in accordance with its term; however, stock options previously granted under the Plan remain valid in accordance with their terms. Under the terms of the 2001 Plan, officers and key employees were granted either nonqualified or incentive stock options and directors, who were not also an officer or employee, were granted nonqualified stock options.

In November 2011, the Company adopted the Omnibus Equity Incentive Plan (the "2011 Omnibus Plan") providing for shares of common stock that could be issued pursuant to awards of stock options, including incentive stock options, and restricted share awards. The 2011 Omnibus Plan provides that any director, employee, or consultant of the Company shall be eligible to be designated a participant in the 2011 Omnibus Plan for purposes of receiving awards.

In June 2019, the Company adopted the 2019 Omnibus Equity Incentive Plan (the "2019 Omnibus Plan"), providing for up to 1,150,000 shares of common stock that could be issued pursuant to awards of options, including incentive stock options, and restricted share awards. Upon adoption of the 2019 Omnibus Plan, the 2011 Omnibus Plan was terminated; however, options previously granted under the 2011 Omnibus Plan remain valid in accordance with their terms.

In contemplation of the holding company reorganization, in November 2019 the Company's Board of Directors adopted the Southern California Bancorp 2019 Omnibus Equity Incentive Plan (the "SCB Plan"). The SCB Plan was approved by shareholders in April 2020 with a maximum number of shares of common stock that may be issued or paid out under the plan of 2,200,000. In October 2020, the Company's Board of Directors approved increasing the maximum number of shares under the SCB Plan by 300,000 to 2,500,000. In June 2021, the Company's Board of Directors approved increasing the maximum number of shares under the SCB Plan by 900,000 to 3,400,000.

Under the SCB Plan, options and restricted share units outstanding under the 2001 Plan, the 2011 Omnibus Plan and the 2019 Omnibus Plan became equivalent awards under the SCB Plan. In addition, the SCB Plan permits the Company to grant additional stock options and restricted share units. The Plan provides for the granting to eligible participants such incentive awards as the Board of Directors or a committee established by the Board, in its sole discretion, to administer the Plan (the "Committee") may from time to time approve. The Board has the power to determine the terms of the awards, including the exercise price, the number of shares subject to each award, the vesting and exercisability of the awards and the form of consideration payable upon exercise. Stock options expire no later than ten years from the date of the grant. The SCB Plan provides for accelerated vesting if there is a change of control, as defined in the Plan. Restricted share units generally vest over a period of one to five years.

In connection with the Merger, the Company assumed each outstanding, unexercised options to acquire shares of BSCA common stock held by BSCA officers and employees who continue to be employed by the Company immediately following the merger, other than any stock options held by BSCA's former CEO. Total unexercised stock options were 90,731, of which 65,261 shares were vested and 25,470 shares were unvested. The remaining term on the assumed stock options ranges from 2.4 years to 9.2 years. Each such option assumed by BCAL, were immediately following the merger, represented a stock option to purchase the same number of shares as immediately prior to the merger, except that the assumed options represented the right to purchase shares of BCAL instead of shares of BSCA. Each assumed option has the same exercise price and is subject to substantially the same terms and conditions as immediately prior to merger, including the original vesting schedule and conditions. All outstanding unexercised options to acquire shares of BSCA common stock held by employees who are not continuing employees or by BSCA's former CEO were canceled and terminated at the effective time of the merger.

Total stock-based compensation cost related to stock options and restricted units was \$5.5 million and \$2.7 million in 2021 and 2020, respectively, and related tax benefits were approximately \$1.6 million and \$706 thousand in 2021 and 2020, respectively.

As of December 31, 2021, there was \$503 thousand of total unrecognized compensation cost related to the outstanding stock options. The intrinsic value of stock options exercised was approximately \$1.7 million and \$216 thousand in 2021 and 2020, respectively.

Stock Options

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model. There were no options granted for the year ended December 31, 2021.

The following table provides the weighted-average assumptions used in the pricing model, and the weighted-average grant date fair value, for option grants made in 2020:

	2020
Expected volatility	37.24%
Expected term (years)	6.5
Expected dividends	None
Risk-free rate	0.29%
Weighted-average grant date fair value	$ 9.11

A summary of changes in outstanding stock options during the years ended December 31, 2021 and December 31, 2020 are presented below:

(dollars in thousands, except share data)	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
December 31, 2021				
Outstanding at beginning of year	783,000			
Granted	—	$ —		
Rollover options (1)	90,731	$ 7.40		
Exercised	(303,100)	$ 8.06		
Forfeited	(33,980)	$ 12.51		
Outstanding at end of year	536,651	$ 9.36	5.0 Years	$ 3,021
Options exercisable	391,661	$ 8.51	4.3 Years	$ 2,538

(1) Amounts relate to rollover stock options issued to BSCA officers and employees in connection with the BSCA acquisition.

(dollars in thousands, except share data)	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
December 31, 2020				
Outstanding at beginning of year	863,100	$ 9.11		
Granted	18,500	$ 9.30		
Exercised	(58,500)	$ 6.31		
Forfeited	(40,100)	$ 11.12		
Outstanding at end of year	783,000	$ 9.22	5.8 Years	$ 2,764
Options exercisable	504,900	$ 8.18	5.0 Years	$ 2,307

Restricted Share Awards

A summary of the changes in outstanding unvested restricted share awards during the years ended December 31, 2021 and December 31, 2020 are presented below:

December 31, 2021	**Restricted Shares**	**Weighted Average Grant Date Fair Value**
Unvested at beginning of year	1,276,106	$ 9.37
Granted	232,347	$ 14.16
Vested	(466,164)	$ 8.97
Forfeited	(31,788)	$ 12.91
Unvested at end of year	1,010,501	$ 10.55

December 31, 2020	**Restricted Shares**	**Weighted Average Grant Date Fair Value**
Unvested at beginning of year	47,500	$ 12.96
Granted	1,420,701	$ 9.19
Vested	(188,345)	$ 8.78
Forfeited	(3,750)	$ 12.96
Unvested at end of year	1,276,106	$ 9.37

As of December 31, 2021, there was $9.0 million of total unrecognized compensation expense related to the outstanding restricted stock units that will be recognized over the weighted-average period of 3.4 years. The total grant date fair value of restricted stock units vested during 2021 and 2020 was $4.2 million and $1.6 million.

Of the total unvested restricted share awards outstanding as of December 31, 2021, vesting related to 275,171 shares is subject to various financial performance conditions being met by December 31, 2023, which the Company has assumed will be achieved for purposes of recognizing compensation cost. The associated cost is being charged to expense ratably over the requisite service period which extends to December 31, 2023. If the performance conditions are not achieved by 2023, the previously recognized compensation cost will be fully reversed. For the year ended December 31, 2021, stock-based compensation for performance-based restricted stock units totaled $2.4 million, of which $1.7 million related to the accelerated stock-based compensation expense for the settlement of a former executive's preexisting employment contract. For the year ended December 31, 2020, stock-based compensation for performance-based restricted stock units totaled $259 thousand.

Future levels of compensation cost recognized related to stock-based compensation awards may be impacted by new awards and/or modifications, repurchases and cancellations of existing awards. Under the terms of the SCB Plan, vested options generally expire ninety days after the director or employee terminates the service affiliation with the Company.

NOTE 14 - REGULATORY MATTERS

At December 31, 2021 and 2020, the Company qualified for treatment under the Small Bank Holding Company Policy Statement (Regulation Y, Appendix C) and, therefore, is not subject to consolidated capital rules at the bank holding company level.

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Banks considered to be “adequately capitalized” are required to maintain a minimum total capital ratio of 8.0%, a minimum Tier 1 capital ratio of 6.0%, a minimum common equity Tier 1 capital ratio of 4.5%, and a minimum leverage ratio of 4.0%. Banks considered to be “well capitalized” must maintain a minimum total capital ratio of 10.0%, a minimum Tier 1 capital ratio of 8.0%, a minimum common equity Tier 1 capital ratio of 6.5%, and a minimum leverage ratio of 5.0%. As of December 31, 2021 and 2020, the most recent notification date to the regulatory agencies, the Bank is “well capitalized” under the regulatory framework for prompt corrective action (PCA). There are no conditions or events since that notification that management believes have changed the Bank’s categories.

Management believes, as of December 31, 2021 and 2020, that the Bank met all capital adequacy requirements to which we are subject.

Basel III, the comprehensive regulatory capital rules for U.S. banking organizations, requires all banking organizations to maintain a capital conservation buffer above the minimum risk-based capital requirements in order to avoid certain limitations on capital distributions, stock repurchases and discretionary bonus payments to executive officers. The capital conservation buffer is exclusively comprised of common equity Tier 1 capital, and it applies to each of the three risk-based capital ratios but not to the leverage ratio. Effective January 1, 2019, the capital conservation buffer increased by 0.625% to its fully phased-in 2.5%, such that the common equity Tier 1, Tier 1 and total capital ratio minimums inclusive of the capital conservation buffers were 7.0%, 8.5%, and 10.5% at December 31,2021. At December 31, 2021, the Bank was in compliance with the capital conservation buffer requirements. To be categorized as well-capitalized, the Bank must maintain minimum ratios as set forth in the table below. The following table also sets forth the Bank's actual capital amounts and ratios:

			Amount of Capital Required			
			To be Adequately Capitalized		**To be Well-Capitalized under PCA Provisions**	
(dollars in thousands)	**Actual Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
As of December 31, 2021:						
Total Capital (to Risk-Weighted Assets)	$ 237,478	15.0%	$ 126,728	8.0%	$ 158,411	10.0%
Tier 1 Capital (to Risk-Weighted Assets)	225,017	14.2%	95,046	6.0%	126,728	8.0%

			Amount of Capital Required			
			To be Adequately Capitalized		To be Well-Capitalized under PCA Provisions	
(dollars in thousands)	Actual Amount	Ratio	Amount	Ratio	Amount	Ratio
CET1 Capital (to Risk-Weighted Assets)	225,017	14.2%	71,285	4.5%	102,967	6.5%
Tier 1 Capital (to Average Assets)	225,017	10.0%	90,153	4.0%	112,691	5.0%
As of December 31, 2020:						
Total Capital (to Risk-Weighted Assets)	$ 172,316	20.4%	$ 67,448	8.0%	$ 84,310	10.0%
Tier 1 Capital (to Risk-Weighted Assets)	161,916	19.2%	50,586	6.0%	67,448	8.0%
CET1 Capital (to Risk-Weighted Assets)	161,916	19.2%	37,939	4.5%	54,801	6.5%
Tier 1 Capital (to Average Assets)	161,916	12.0%	53,767	4.0%	67,208	5.0%

The primary source of funds for the Company is dividends from the Bank. Under federal law, the Bank may not declare a dividend in excess of its undivided profits and, absent the approval of the OCC, the Bank's primary banking regulatory, if the total amount of dividends declared by the Bank in any calendar year exceeds the total of the Bank's retained net income of that current period, year to date, combined with its retained net income for the preceding two years. The Bank also is prohibited from declaring or paying any dividend if, after making the dividend, the Bank would be considered "undercapitalized" (as defined by reference to other OCC regulations). Federal bank regulatory agencies have authority to prohibit banking institutions from paying dividends if those agencies determine that, based on the financial condition of the bank, such payment will constitute an unsafe or unsound practice.

The Federal Reserve limits the amount of dividends that bank holding companies may pay on common stock to income available over the past year, and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. It is also the Federal Reserve's policy that bank holding companies should not maintain dividend levels that undermine their ability to be a source of strength to its banking subsidiaries. Additionally, in consideration of the current financial and economic environment, the Federal Reserve has indicated that bank holding companies should carefully review their dividend policies.

NOTE 15 - FAIR VALUE

The fair value of a financial instrument is the amount at which the asset or obligation could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Fair value estimates are made at a specific point in time based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the entire holdings of a particular financial instrument. Because no market value exists for a significant portion of the financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature, involve uncertainties and matters of judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value of financial instruments

Fair value estimates are based on financial instruments both on and off the balance sheet without attempting to estimate the value of anticipated future business, and the value of assets and liabilities that are not considered financial instruments. Additionally, tax consequences related to the realization of the unrealized gains and losses can have a potential effect on fair value estimates and have not been considered in many of the estimates.

The following methods and assumptions were used to estimate the fair value of significant financial instruments:

Cash and Due from Banks: The carrying amounts of cash and short-term instruments approximate fair values because of the liquidity of these instruments.

Fed Funds and Interest-Bearing Balances: The carrying amount is assumed to be the fair value given the short-term nature of these deposits.

Debt Securities Available for Sale: The fair values of securities available for sale are determined by obtaining quoted prices on nationally recognized securities exchanges or matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for specific securities but rather by relying on the securities' relationship to other benchmark quoted securities.

Loans: The fair value of loans, which is based on an exit price notion, is generally determined using an income based approach based on discounted cash flow analysis. This approach utilizes the contractual maturity of the loans and market indications of interest rates, prepayment speeds, defaults and credit risk in determining fair value. For impaired loans, an asset-based approach is applied to determine the estimated fair values of the underlying collateral. This approach utilizes the estimated net sales proceeds to determine the fair value of the loans when deemed appropriate. The implied sales proceeds value provides a better indication of value than using an income-based approach as these loans are not performing or exhibit strong signs indicative of non-performance.

Restricted Stock Investments: Investments in FHLB and Federal Reserve stocks are recorded at cost and measured for impairment. Ownership of FHLB and Federal Reserve stocks are restricted to member banks and the securities do not have a readily determinable market value. Purchases and sales of these securities are at par value with the issuer. The fair value of investments in FHLB and Federal Reserve stock is equal to the carrying amount.

Other Equity Securities: The fair value of equity securities is based on quoted prices in active markets for identical assets to determine the fair value. If quoted prices are not available to determine fair value, the Company estimates the fair values by using independent pricing models, quoted prices of securities with similar characteristics, or discounted cash flows.

Other Real Estate Owned: Nonrecurring adjustments to certain commercial and residential real estate properties classified as other real estate owned (OREO) are measured at the lower of the carrying amount or fair value, less costs to sell. The fair value of OREO is generally based on recent real estate appraisals or broker opinions, obtained from independent third parties, which are frequently adjusted by management to reflect current conditions and estimated selling costs.

Deposits: The fair values disclosed for demand deposits, including interest and non-interest demand accounts, savings, and certain types of money market accounts are, by definition based on carrying value. Fair value for fixed-rate certificates of deposit is estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregate expected monthly maturities on time deposits. Early withdrawal of fixed-rate certificates of deposit is not expected to be significant.

Borrowings: The fair values of the Company's overnight borrowings from Federal Home Loan Bank approximates their carrying value as the advances were recently borrowed at market rate. The fair value of fixed-rated term borrowings is estimated using a discounted cash flow through the remaining maturity dates based on the current borrowing rates for similar types of borrowing arrangements. Paycheck Protection Program Liquidity Facility. The fair value of advances under the FRB PPP Liquidity Facility were considered to be the carrying value due to the ongoing availability of the facility. The fair values of subordinated debentures and subordinated debt are based on rates currently available to the Company for debt with similar terms and remaining maturities.

Accrued Interest Payable: The fair value of accrued interest payable approximates their carrying amounts.

Off-Balance Sheet Financial Instruments: The fair value of commitments to extend credit and standby letters of credit is estimated using the fees currently charged to enter into similar agreements. The fair value of these financial instruments is not material.

The estimated fair value hierarchy level and estimated fair value of financial instruments at December 31 is summarized as follows:

		2021		2020	
(dollars in thousands)	**Fair Value Hierarchy**	**Carrying Value**	**Estimated Fair Value**	**Carrying Value**	**Estimated Fair Value**
Financial assets:					
Cash and due from banks	Level 1	$ 22,435	$ 22,435	$ 11,951	$ 11,951
Fed funds and interest-bearing balances	Level 1	557,571	557,571	238,866	238,866
Debt securities available for sale	Level 2	55,567	55,567	24,702	24,702
Loans, net	Level 3	1,493,091	1,498,804	1,223,626	1,218,871
Restricted stock, at cost	Level 2	12,493	12,493	8,585	8,585
Other Equity Securities	Level 2	2,136	2,136	288	288
Accrued interest receivable	Level 2	4,137	4,137	6,126	6,126
Financial liabilities:					
Deposits	Level 2	1,973,098	1,972,610	1,194,739	1,195,497
Borrowings	Level 2	20,409	21,580	199,648	199,641
Accrued interest payable	Level 2	67	67	454	454

Recurring fair value measurements

The following table provides the hierarchy and fair value for each major category of assets and liabilities measured at fair value on a recurring basis at the periods indicated:

	Recurring Fair Value Measurements			
(dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
December 31, 2021				
Securities available for sale:				
U.S. government and agency and government sponsored enterprise securities:				
Mortgage-backed securities	$ —	$ 17,315	$ —	$ 17,315
SBA securities	—	11,400	—	11,400
U.S. Treasury	—	2,781	—	2,781
U.S. Agency	—	6,479	—	6,479
Collateralized mortgage obligations	—	10,288	—	10,288
Taxable municipal	—	5,522	—	5,522
Tax exempt bank-qualified municipals	—	1,782	—	1,782
	$ —	$ 55,567	$ —	$ 55,567
December 31, 2020				
Securities available for sale:				
U.S. government and agency and government sponsored enterprise securities:				
Mortgage-backed securities	$ —	$ 5,430	$ —	$ 5,430
SBA securities	—	9,844	—	9,844
Taxable municipal	—	5,137	—	5,137
Tax exempt bank-qualified municipals	—	1,791	—	1,791
Corporate Debt Securities	—	2,500	—	2,500
December 31, 2020	$ —	$ 24,702	$ —	$ 24,702

Nonrecurring fair value measurements

Certain assets and liabilities may be required to be measured at fair value on a nonrecurring basis in periods subsequent to their initial recognition. These assets and liabilities are not measured at fair value on an ongoing basis; however, they are subject to fair value adjustments in certain circumstances, such as when there is evidence of impairment. At December 31, 2021, the Company determined the amounts measured at fair value on a nonrecurring basis were immaterial and the Company did not have any nonrecurring fair value measurements at December 31, 2020.

NOTE 16 - CONDENSED FINANCIAL INFORMATION OF PARENT COMPANY ONLY

On May 15, 2020, the Company was involved in a corporate reorganization whereby the Bank became a wholly owned subsidiary of the Company. This reorganization was accounted for like a pooling of interest. The earnings of the subsidiary are recognized using the equity method of accounting. The following tables present the parent company only condensed balance sheets at December 31, 2021 and

2020 and the related condensed statements of income and condensed statements of cash flows for the years ended December 31, 2021 and 2020.

Southern California Bancorp (Parent Company Only)
CONDENSED BALANCE SHEETS

(dollars in thousands)	December 31, 2021	December 31, 2020
ASSETS		
Cash	$ 2,838	$ 3,968
Investment in Bank of Southern California	263,605	184,896
Other investments	93	93
Accrued interest and other assets	443	381
Total assets	$ 266,979	$ 189,338
LIABILITIES		
Subordinated debt and other borrowings	$ 20,409	$ 20,265
Accrued interest and other liabilities	42	188
Total liabilities	20,451	20,453
SHAREHOLDERS' EQUITY		
Common stock	214,163	146,896
Retained earnings	32,403	21,694
Accumulated other comprehensive (loss) income	(38)	295
Total shareholders’ equity	246,528	168,885
Total liabilities and shareholders’ equity	$ 266,979	$ 189,338

CONDENSED STATEMENTS OF INCOME

	Year Ended December 31,	
(dollars in thousands)	2021	2020
INCOME		
Other interest and dividends	$ 3	$ 2
Dividends from bank subsidiary	—	12,100
Total income	3	12,102
EXPENSES		
Interest on borrowings	1,224	727
Merger and related expenses	347	349
Other noninterest expense	86	86
Total expenses	1,657	1,162
(Loss) income before income tax benefit	(1,654)	10,940
Income tax benefit	436	344
(Loss) income before equity in undistributed earnings (dividends in excess of equity in earnings) of subsidiary	(1,218)	11,284
Equity in undistributed earnings (dividends in excess of equity in earnings) of subsidiary	11,927	(6,562)
Net income	$ 10,709	$ 4,722

CONDENSED STATEMENTS OF CASH FLOWS

	Year Ended December 31,	
(dollars in thousands)	**2021**	**2020**
OPERATING ACTIVITIES		
Net Income	$ 10,709	$ 4,722
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Amortization of debt issuance costs	95	—
Amortization of TRUPS fair value adjustment	49	—
(Equity in undistributed earnings) dividends in excess of equity in earnings of subsidiary	(11,927)	6,562
Other Items	(207)	(191)
Net cash (used in) provided by operating activities	(1,281)	11,093
INVESTING ACTIVITIES		
Investment in subsidiaries	—	(40,000)
Cash paid in business combination	(21)	(25,641)
Net cash used in investing activities	(21)	(65,641)
FINANCING ACTIVITIES		
Proceeds from issuance of subordinated debt	—	17,525
Decrease in short-term borrowings	—	(11)
Issuance of common stock, net of costs	—	40,624
Proceeds from exercise of stock options	172	369
Net cash provided by financing activities	172	58,507
(Decrease) increase in cash and cash equivalents	(1,130)	3,959
Cash and cash equivalents, beginning of year	3,968	9
Cash and cash equivalents, end of year	$ 2,838	$ 3,968

NOTE 17 - SUBSEQUENT EVENTS

The Bank has evaluated subsequent events for recognition and disclosure through April 25, 2022, the date the consolidated financial statements were available to be issued.

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