FRIENDLY HILLS BANK | FRIENDLY HILLS BANCORP

CONNECTING YOU TO OPPORTUNITIES

2021 ANNUAL REPORT

FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT

2021 HIGHLIGHTS

- $293 million in Total Assets
- $258 million in Total Deposits
- $135 million in Noninterest-Bearing Demand Deposits
- $89 million in Total Loans
- Acquired Three Branches with $82.4 million in Deposits
- Formed Holding Company: Friendly Hills Bancorp

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SHAREHOLDER LETTER

To our Shareholders, Customers, and Communities,

2021 was a year of historic growth and transformation for Friendly Hills Bancorp and its wholly owned subsidiary, Friendly Hills Bank. We expanded our banking operations, transitioned to new leadership, and laid the foundation for the future—all while being faced with a global pandemic and ongoing uncertainty and disruption around the world. As we closed the year, we are confident that even greater opportunities lie ahead.

2021 FINANCIAL RESULTS

The Bank's 2021 financial results were fundamentally strong. On September 24, 2021, we completed the strategic acquisition of three branch offices from Bank of Southern California with deposits totaling $82 million. The acquisition demonstrated our commitment to growing the company and serving Southern California's diverse business community with our entrance into Orange County and the Inland Empire. Despite the incremental costs of the branch acquisition and other transitional changes in 2021, we survived through another year of COVID-19 and reported net income for the year of $189 thousand.

The Bank is "well-capitalized," the highest regulatory capital category

- Total assets ended the year at $293 million, an increase of $89 million over the prior year.
- Total deposits ended the year at $258 million, an increase of $96 million over the prior year. Noninterest-bearing deposits continued to reflect strong, relationship-based deposit sources at 52% of total deposits.
- Total risk-based capital ratio for Friendly Hills Bank was 15.8% at December 31, 2021, and considered "well-capitalized," the highest regulatory capital category.

A YEAR OF TRANSITION

2021 marked an important year in our company's history. Shaped by the strategic formation of a holding company, changes in management, and a realignment of the Board, signifying a new direction for the Bank.

- During 2021, Friendly Hills Bank successfully reorganized into a holding company structure, providing additional corporate and capital flexibility.
- In November 2021, Jeff Ball, the Bank's co-founder and long-standing CEO and President, announced plans to resign from the Bank by year end, but continue to serve on the Board of Directors and has since been named Vice Chairman.
- In December 2021, Nathan Rogge was appointed President and CEO and Board member, and the Board of Directors was restructured, including the addition of Joe Matranga to serve as Chairman.

"AS WE CLOSED THE YEAR, WE ARE CONFIDENT THAT **EVEN GREATER OPPORTUNITIES** LIE AHEAD."

SHAREHOLDER LETTER

A STRONG FOUNDATION FOR GROWTH

Launched a specialty lending group to serve underserved market

Expanded to San Diego with plans to open a full-service branch

As we look ahead, the company has established a solid foundation for the creation of future shareholder value.

- During the first quarter of 2022, a new Executive Leadership Team was instituted to better position the company for long-term growth and success. This included the addition of four experienced leaders, further strengthening the Bank's infrastructure, and bringing the team to six members.
- In April 2022, a specialty lending group was formed dedicated to providing financing solutions for commercial trucks and vehicles. New loans are already being booked and we feel this niche market is an opportunity to grow our commercial lending expertise and will begin to show incremental results after a short ramp-up period.
- Earlier this year, the company expanded to San Diego and plans to open a full-service branch in Del Mar by the third quarter of 2022.

CONNECTING YOU TO OPPORTUNITIES

2021 was a meaningful year. We expanded our footprint, increased our customer base, established new leadership, realigned our Board, and repositioned the company for long-term growth and success. This translates to more opportunities for our shareholders, our customers, and our communities.

As we look to the future, we remain focused on supporting your business needs and connecting you to even greater opportunities across Southern California.

On behalf of the entire team at Friendly Hills Bank, we thank you for your support.

Nathan Rogge
President and CEO
of Friendly Hills Bank and Friendly Hills Bancorp

Joe Matranga
Chairman of the Board
of Friendly Hills Bank and Friendly Hills Bancorp

"WE REMAIN FOCUSED ON **SUPPORTING YOUR BUSINESS NEEDS** AND CONNECTING YOU TO EVEN GREATER OPPORTUNITIES."

Independent Auditor's Report

The Board of Directors and Shareholders
Friendly Hills Bancorp and Subsidiary
Whittier, California

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of Friendly Hills Bancorp and Subsidiary, which comprise the consolidated balance sheets as of December 31, 2021 and 2020, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Friendly Hills Bancorp and Subsidiary as of December 31, 2021 and 2020, and the results of their operations and their cash flows for years then ended, in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are required to be independent of Friendly Hills Bancorp and Subsidiary, and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Consolidated Financial Statements

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

In preparing the consolidated financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about Friendly Hills Bancorp and Subsidiary's ability to continue as a going concern for one year after the date that the consolidated financial statements are available to be issued.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the consolidated financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Friendly Hills Bancorp and Subsidiary's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the consolidated financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Friendly Hills Bancorp and Subsidiary's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control–related matters that we identified during the audit.

Eide Bailly LLP

Laguna Hills, California
April 21, 2022

	2021	2020
Assets		
Cash and due from banks	$ 6,498,403	$ 2,802,365
Interest bearing deposits with other financial institutions	58,529,324	48,109,409
Cash and cash equivalents	65,027,727	50,911,774
Debt securities available for sale	118,313,949	20,070,410
Debt securities held to maturity (fair value - $7,991,062 and $1,839,124 for 2021 and 2020, respectively)	8,544,323	2,000,000
Loans, net of unearned income	88,923,169	123,229,996
Allowance for loan losses	(1,800,021)	(1,464,131)
Loans, net	87,123,148	121,765,865
Restricted stock	1,471,850	1,471,850
Equity securities	1,160,000	1,160,000
Premises and equipment, net	542,484	263,746
Right of use asset	1,771,071	587,676
Bank owned life insurance	4,951,387	4,842,600
Goodwill	1,361,938	384,000
Core Deposit Intangible	425,847	-
Accrued interest receivable and other assets	2,325,619	750,254
Total assets	$ 293,019,343	$ 204,208,175
Liabilities and Shareholders' Equity		
Liabilities		
Deposits		
Noninterest-bearing deposits	$ 134,624,786	$ 78,996,654
Interest-bearing deposits	122,935,055	82,532,578
Total deposits	257,559,841	161,529,232
FHLB advances	12,000,000	20,500,000
Accrued interest payable and other liabilities	3,729,753	1,664,313
Total liabilities	273,289,594	183,693,545
Shareholders' Equity		
Common stock, no par value, 10,000,000 shares authorized; 2,006,393 shares issued and outstanding	15,957,620	15,957,620
Additional paid-in-capital	1,637,821	1,570,413
Accumulated earnings	2,870,258	2,681,729
Accumulated other comprehensive income (loss), net of tax	(735,950)	304,868
Total shareholders' equity	19,729,749	20,514,630
Total liabilities and shareholders' equity	$ 293,019,343	$ 204,208,175

	2021	2020
Interest Income		
Interest and fees on loans	$ 4,959,916	$ 5,244,242
Interest on debt securities	727,735	648,261
Interest on deposits with other financial institutions	114,841	146,603
Dividends on restricted stock and equity securites	141,782	128,102
Total interest income	5,944,274	6,167,208
Interest Expense		
Interest expense on deposits	225,359	244,916
Interest expense on borrowings	333,832	490,765
Total interest expense	559,191	735,681
Net Interest Income	5,385,083	5,431,527
Provision for Loan Losses	-	150,000
Net Interest Income After Provision for Loan Losses	5,385,083	5,281,527
Noninterest Income		
Service charges on deposit accounts	75,484	52,939
Employee retention tax credit	491,307	-
Increase in cash surrender value of life insurance	108,787	112,663
Payroll service	240,090	245,660
Other fees and miscellaneous income	219,682	193,339
Total noninterest income	1,135,350	604,601
Noninterest Expense		
Salaries and other employee benefits	3,696,282	2,962,346
Occupancy	585,360	339,168
Advertising and marketing	43,228	54,782
Professional services	537,221	171,594
Data processing	488,783	392,968
Stationary and supplies	38,393	35,265
Corporate insurance	73,136	60,398
Supervisory charges	117,192	53,078
Other	721,286	407,707
Total noninterest expense	6,300,881	4,477,306
Income before provision for income taxes	219,552	1,408,822
Provision for income taxes	31,023	387,032
Net income	$ 188,529	$ 1,021,790
Earnings per share basic	$ 0.09	$ 0.51
Earnings per share diluted	$ 0.09	$ 0.50

	2021	2020
Net Income	$ 188,529	$ 1,021,790
Other Comprehensive Income (Loss)		
Change in unrealized (loss) gain on securities available for sale	(1,484,162)	460,242
Income tax effect relating to securities available for sale	443,344	(113,800)
Total other comprehensive income (loss)	(1,040,818)	346,442
Total comprehensive income (loss)	$ (852,289)	$ 1,368,232

	Common Stock		Additional		Accumulated Other	Total
	Shares Outstanding	Amount	Paid-In Capital	Accumulated Earnings	Comprehensive Income (Loss)	Shareholders' Equity
Balance, December 31, 2019	1,997,993	$ 15,957,620	$ 1,470,077	$ 1,659,939	$ (41,574)	$ 19,046,062
Net income	-	-	-	1,021,790	-	1,021,790
Stock-based compensation expense	-	-	67,408	-	-	67,408
Stock options exercised	8,400	-	32,928	-	-	32,928
Other comprehensive income, net of tax	-	-	-	-	346,442	346,442
Balance, December 31, 2020	2,006,393	15,957,620	1,570,413	2,681,729	304,868	20,514,630
Net income	-	-	-	188,529	-	188,529
Stock-based compensation expense	-	-	67,408	-	-	67,408
Other comprehensive loss, net of tax	-	-	-	-	(1,040,818)	(1,040,818)
Balance, December 31, 2021	2,006,393	$ 15,957,620	$ 1,637,821	$ 2,870,258	$ (735,950)	$ 19,729,749

	2021	2020
Operating Activities		
Net income	$ 188,529	$ 1,021,790
Adjustments to reconcile net income to net cash from operating activities		
Net amortizations of premiums and discounts on debt securities available for sale	205,046	15,849
Depreciation and amortization	130,572	99,265
Provision for loan losses	-	150,000
Stock-based compensation expense	67,408	67,408
Change in deferred income taxes	3,000	(58,000)
Increase in cash surrender value of life insurance	(108,787)	(112,663)
Change in other assets and liabilities	(593,797)	241,898
Net Cash (Used in) Provided by Operating Activities	(108,029)	1,425,547
Investing Activities		
Purchase of debt securities available for sale	(108,360,427)	-
Purchase of debt securities held to maturity	(6,577,680)	-
Principal paydowns on debt securities available for sale	8,461,037	11,071,006
Change in FHLB and FRB stock	-	72,800
Net decrease (increase) in loans	34,642,717	(29,259,818)
Cash acquired in branch acquisition, net of consideration paid	81,068,323	-
Purchase of premises and equipment	(156,473)	(54,358)
Net Cash Provided by (Used in) Investing Activities	9,077,497	(18,170,370)
Financing Activities		
Increase in deposits	13,646,485	43,316,040
Exercise of stock options	-	32,928
Proceeds from FHLB advances	-	48,755,000
Payments on FHLB advances	(8,500,000)	(48,505,000)
Net Cash Provided by Financing Activities	5,146,485	43,598,968
Net Increase in Cash and Cash Equivalents	14,115,953	26,854,145
Cash and Cash Equivalents, Beginning of Year	50,911,774	24,057,629
Cash and Cash Equivalents, End of Year	$ 65,027,727	$ 50,911,774
Supplemental Disclosure of Cash Flow Information		
Interest paid	$ 567,728	$ 725,065
Taxes paid	409,079	320,000
Assets acquired in acquisition plus goodwill recognized, net	3,215,140	-
Liabilities assumed in acquisition	84,283,463	-
Lease liabilities arising from obtaining right-of-use assets	1,899,339	-

Note 1 - Significant Accounting Policies

Nature of Operations

The Company consists of Friendly Hills Bancorp ("Bancorp") and its wholly-owned subsidiary Friendly Hills Bank (the "Bank"). Friendly Hills Bancorp was formed in 2021 as a one-bank holding company. Bancorp and the Bank are collectively referred to herein as the Company. Friendly Hills Bank was incorporated in the State of California, commenced operations on September 18, 2006, and is organized as a single operating segment. The Bank operates full-service branches in Whittier, Santa Fe Springs, Orange and Redlands, California. Its principal source of revenue is providing loans to customers, who are predominately small and middle-market businesses and individuals located primarily in the Los Angeles, Orange and San Bernardino County areas of California.

Basis of Presentation and Consolidation

The accompanying consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and general practices within the banking industry. The consolidated financial statements of the Company include the accounts of Friendly Hills Bancorp and its wholly-owned subsidiary Friendly Hills Bank. All significant intercompany balances and transactions have been eliminated in consolidation.

Subsequent Events

The Company has evaluated subsequent events for recognition and disclosure through April 21, 2022, which is the date the financial statements were available to be issued.

Use of Estimates

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet 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 changes in the near term relate to the determination of the allowance for loan losses.

Acquisition Activities

The Company accounts for business combinations under the acquisition method of accounting. Assets acquired and liabilities assumed are measured and recorded at fair value at the date of acquisition, including identifiable intangible assets. Fair values are subject to refinement after the closing date of an acquisition as information relative to closing date fair values becomes available, but not beyond one year from the acquisition. All identifiable intangible assets that are acquired in a business combination are recognized at fair value on the acquisition date. Identifiable intangible assets are recognized separately if they arise from contractual or other legal rights or if they are separable (i.e., capable of being sold, transferred, licensed, rented, or exchanged separately from the entity).

Deposit liabilities and the related depositor relationship intangible assets may be exchanged in observable exchange transactions. As a result, the depositor relationship intangible asset (the core deposit intangible) is considered identifiable, because the separability criterion has been met.

Cash and Cash Equivalents

For the purposes of the consolidated statements of cash flows, cash and cash equivalents include cash and balances due from banks and federal funds sold, all of which have original maturities of 90 days or less.

Balances in transaction accounts at other financial institutions may exceed amounts covered by federal deposit insurance. Management regularly evaluates the credit risk associated with other financial institutions and believes that the Company is not exposed to any significant credit risks on cash and cash equivalents.

Cash and Due from Banks

Banking regulations require that banks maintain a percentage of their deposits as reserves in cash or on deposit with the Federal Reserve Bank (FRB). The Company was in compliance with its reserve requirements as of December 31, 2021 and 2020.

Debt Securities

The Company classifies its debt securities as available for sale or held to maturity. Securities classified as available for sale are recorded at fair value, with unrealized gains and losses excluded from earnings and reported in comprehensive income. Securities, which the Company has the positive intent and ability to hold to maturity, are classified as held to maturity and are carried at amortized cost. Equity securities are carried at fair value, with changes in fair value reported in net income. Equity securities without readily determinable fair values are carried at cost, minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or similar investment.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method. Purchases are accounted for on the trade date.

The Company follows the accounting guidance related to recognition and presentation of other-than-temporary impairment. This guidance specifies that (a) if a bank does not have the intent to sell a debt security prior to recovery and (b) it is more likely than not that it will not have to sell the debt security prior to recovery, the security would not be considered other-than-temporarily impaired unless there is a credit loss. When an entity does not intend to sell the security, and it is more likely than not, the entity will not have to sell the security before recovery of its cost basis, it will recognize the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income.

Equity Securities

Equity securities include investments in bankers bank and other stock without readily determinable fair values. These securities are carried at cost, minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or similar investment.

Loans

The Company grants real estate, commercial and industrial and consumer loans to borrowing customers. A substantial portion of the loan portfolio is represented by real estate loans in the Los Angeles and Orange County metropolitan areas. The ability of the Company's borrowers to honor their contracts is dependent upon many factors, including the real estate market and general economic conditions in the Company's area.

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding unpaid principal balances reduced by any charge-offs or specific valuation allowances and net of deferred fees or costs on originated loans, or unamortized premiums or discounts on purchased loans. Loan origination fees and certain direct origination costs are capitalized and recognized as an adjustment of the yield of the related loan. Amortization of deferred loan fees is discontinued when a loan is placed on nonaccrual status.

Loans on which the accrual of interest has been discontinued are designated as nonaccrual loans. The accrual of interest on loans is discontinued when principal or interest is past due 90 days based on the contractual terms of the loan or when, in the opinion of management, there is reasonable doubt as to collectability. When loans are placed on nonaccrual status, all interest previously accrued but not collected is 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 collectible as to all principal and interest.

Allowance for Loan Losses

The allowance for loan losses is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. 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 allowance consists of specific and general reserves. Specific reserves relate to loans that are individually classified as impaired. A loan is 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. 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 fair value of the collateral.

The Company recognizes interest income on impaired loans based on its existing methods of recognizing interest income on nonaccrual loans. 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 based on expected future cash flows discounted using the loan's effective rate immediately prior to the restructuring.

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. Smaller balance, homogeneous loans are collectively evaluated for impairment.

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. 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; changes in the value of the underlying collateral for collateral-dependent loans; concentrations of credit and the effect of other external factors such as competition and legal and regulatory requirements.

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

Premises and Equipment

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. 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.

Leases

The Company determines if an arrangement contains a lease at contract inception and recognizes right-of-use ("ROU") assets and operating lease liabilities 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 in the statements of financial condition. 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. The Company may sublease its leased assets to an unrelated third party. Rental income received from the sublease is included in noninterest income and recorded on a straight-line basis over the term of the sublease.

Restricted Stock

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, and may invest in additional amounts. 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 security, and periodically evaluated for impairment based on the ultimate recovery of par value. Both cash and stock dividends are reported as income.

Bank Owned Life Insurance

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

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 $44,398 at December 31, 2021 and 2020, and is included in other liabilities in the consolidated balance sheet.

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 reasonable estimated. Management does not believe there now are such matters that will have a material effect on the financial statements.

Advertising Costs

The Company expenses the costs of advertising in the period incurred.

Goodwill and Other Intangible Assets

Goodwill is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill resulting from acquisitions is not amortized, but tested for impairment at least annually. The Company has selected December 31 as the date to perform the annual impairment test. Goodwill amounted to $1,361,938 and $384,000 as of December 31, 2021 and December 31, 2020, respectively, and is the only intangible asset with an indefinite life on the balance sheet. No impairment was recognized on goodwill during 2021 or 2020.

Other intangible assets consist of core deposit intangible ("CDI") assets arising from the acquisition of deposits. CDI assets are amortized on an accelerated method over their estimated useful life of approximately 10 years. CDI of $443,000 was recognized in the 2021 acquisition disclosed in Note 16. The unamortized balance as of December 31, 2021 was $425,847. CDI amortization expense was $17,153 in 2021. Estimated CDI amortization expense for the next 5 years and thereafter, is as follows:

Year Ending December 31,	Amount
2022	$ 66,826
2023	59,884
2024	53,714
2025	48,226
2026	43,339
Thereafter	153,858
Total	$ 425,847

Income Taxes

Income taxes are provided for the tax effects of transactions reported in the financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the basis of property and equipment, intangible assets, and accrued expenses for financial and income tax reporting. The deferred tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

The Company evaluates its tax positions that have been taken or are expected to be taken on income tax returns to determine if an accrual is necessary for uncertain tax positions. As of December 31, 2021, and 2020, the unrecognized tax benefit accrual was zero. The Company will recognize future accrued interest and penalties related to unrecognized tax benefits in income tax expense if incurred.

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 as described in Note 12. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received.

Earnings Per Share

The basic earnings per share ratio 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 earnings per share 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. For the years ended December 31, 2021 and 2020 weighted average shares outstanding used in the computation of basic and diluted earnings per share was 2,006,393 and 2,052,901 in 2021 and 2,006,393 and 2,029,184 in 2020, respectively. There were no anti-dilutive shares as of December 31, 2021 and 2020.

Stock-Based Compensation

Stock-based compensation expense reflects the fair value of stock-based awards measured at the grant date and recognized over the relevant vesting period. A Black-Scholes option valuation model is utilized to estimate the fair value of stock options granted, while the market price of the Company's common stock at the date of grant is used for restricted stock unit awards.

Compensation cost is recognized over the requisite service period and adjusted to reflect forfeitures as they occur and for awards with performance conditions changes in the probability that the performance condition will be met. If the grantee of performance condition award does not earn the award, the Company reverses any compensation cost previously recognized during the requisite service period.

Comprehensive Income (Loss)

Comprehensive income (loss) is reported in addition to net income for all periods presented. Comprehensive income (loss) is a more inclusive financial reporting methodology that includes disclosure of other comprehensive income or loss that historically has not been recognized in the calculation of net income. Unrealized gains and losses on the Company's debt securities available for sale are included in other comprehensive income, adjusted for realized gains or losses included in net income. Total comprehensive income or loss and the components of accumulated other comprehensive income or loss is presented in the statement of changes in shareholders' equity and comprehensive income (loss).

Revenue Recognition – Noninterest Income

In accordance with Topic 606, revenues are recognized when control of promised goods or services is transferred to customers in an amount that reflects the consideration the Company expects to be entitled to in exchange for those goods or services. To determine revenue recognition for arrangements that an entity determines are within the scope of Topic 606, the Company performs the following five steps: (i) identify the contract(s) with a customer; (ii) identify the performance obligation in the contract; (iii) determine the transaction price; (iv) allocate the transaction price to the performance obligation in the contract; and (v) recognize revenue when (or as) the Company satisfies a performance obligation. The Company only applies the five-step model to contracts when it is probable that the entity will collect the consideration it is entitled to in exchange for the goods or services it transfers to the customer. At contract inception, once the contract is determined to be within the scope of Topic 606, the Company assesses the goods or services that are promised within each contract and identifies those that contain performance obligation, and assesses whether each promised good or service is distinct.

The Company then recognizes as revenue the amount of the transaction price that is allocated to the respective performance obligation when (or as) the performance obligation is satisfied.

The following is a discussion of key revenues within the scope of the new revenue guidance.

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

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

Payroll Processing Fees
Payroll processing fees are earned primarily by processing payroll and related transactions for third party employers. The Company earns fees from the processing of payroll, direct deposit and check origination, payroll related reporting services, the processing of related payroll tax payments to regulatory agencies, the filing of payroll tax returns and employee time management solutions. The performance obligation is satisfied and the fees recognized when the transactions occur and when each specific service is provided to the customer.

Fair Value Measurements

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:

The following provides a summary of the hierarchical levels used to measure fair value:

Level 1 - Quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at 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 an entity's own assumptions about the factors that market participants would use in pricing an asset or liability.

See Note 10 for more information and disclosures relating to the Company's fair value measurements.

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. 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. For AFS debt securities with unrealized losses, entities will measure credit losses in a manner similar to what they do today, except that the losses will be recognized as allowances rather than reductions in the amortized cost of the 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. This ASU is effective for interim and annual reporting periods beginning after December 15, 2022. A cumulative-effect adjustment to retained earnings will be reflected as of the beginning of the first reporting period in which the guidance is effective (i.e., modified retrospective approach). The Company is currently evaluating the provisions of ASU No. 2016-13 for potential impact on its consolidated financial statements.

Note 2 - Debt Securities

Debt securities have been classified in the consolidated balance sheets according to management's intent. The amortized cost and fair value of securities, with gross unrealized gains and losses, at December 31, 2021, follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities Available for Sale				
CMO securities	$ 58,486,290	$ 96,419	$ (693,322)	$ 57,889,387
Corporate securities	8,798,716	12,941	(116,582)	8,695,075
Mortgage-backed securities	39,188,726	1,009	(451,727)	38,738,008
Municipal securities	8,481,032	39,234	(44,484)	8,475,782
SBA securities	4,410,541	105,156	-	4,515,697
Total	$ 119,365,305	$ 254,759	$ (1,306,115)	$ 118,313,949
Securities Held to Maturity				
Corporate securities	$ 8,544,323	$ -	$ (553,261)	$ 7,991,062

The amortized cost and fair value of securities, with gross unrealized gains and losses, at December 31, 2020, follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities Available for Sale				
CMO securities	$ 13,348,169	$ 275,082	$ -	$ 13,623,251
Corporate securities	4,550,000	-	(24,194)	4,525,806
Mortgage-backed securities	79,537	2,691	-	82,228
SBA securities	1,659,899	179,226	-	1,839,125
Total	$ 19,637,605	$ 456,999	$ (24,194)	$ 20,070,410
Securities Held to Maturity				
Corporate securities	$ 2,000,000	$ -	$ (160,482)	$ 1,839,518

The amortized cost and fair value of debt securities by contractual maturity at December 31, 2021, follows:

	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 459,954	$ 471,846	$ -	$ -
Due from one to five years	8,202,033	8,202,447	-	-
Due from five to ten years	5,047,175	5,005,618	8,544,323	7,991,062
Due after ten years	7,981,127	8,006,643	-	-
CMO's and mortgage-backed securities	97,675,016	96,627,395	-	-
	$ 119,365,305	$ 118,313,949	$ 8,544,323	$ 7,991,062

The Company pledged investment securities with a carrying value of approximately $0.2 million as of December 31, 2021 for Federal Reserve Discount Window borrowings.

At December 31, 2021, the Company had 25 debt securities with an unrealized loss of $1,859,376, which have depreciated approximately 1.71% from the amortized cost basis. Substantially all have been in a continuous loss position for less than 12 months. Unrealized losses on debt securities have not been recognized into income because the bonds are of high credit quality, management does not intend to sell and it is likely that management will not be required to sell the securities prior to their anticipated recovery, and the decline in fair value is largely due to change in interest rates and other market conditions. The fair value is expected to recover as the bonds approach maturity.

Note 3 - Loans and Allowance for Loan Losses

Loans consist of the following at December 31:

	2021	2020
Real estate	$ 76,580,117	$ 87,730,987
Commercial and industrial	12,388,806	35,717,596
Consumer	68,339	14,136
	89,037,262	123,462,719
Allowance for loan losses	(1,800,021)	(1,464,131)
Deferred loan fees, net	(114,093)	(232,723)
Net Loans	$ 87,123,148	$ 121,765,865

Changes in the allowance for loan losses are as follows:

	2021	2020
Balance, beginning of year	$ 1,464,131	$ 1,331,982
Provision for loan losses	-	150,000
Loan charge-offs	(5,131)	(17,851)
Loan recoveries	341,021	-
Balance, end of year	$ 1,800,021	$ 1,464,131

The following tables presents the recorded investment in loans and impairment method as of December 31, 2021 and 2020, and the activity in the allowance for loan losses for the year then ended, by portfolio segment:

December 31, 2021	Real Estate	Commercial and Industrial	Consumer	Total
Allowance for Loan Losses				
Beginning of Year	$ 1,265,549	$ 198,035	$ 547	$ 1,464,131
Provisions	245,061	(248,252)	3,191	-
Charge-offs	-	(5,131)	-	(5,131)
Recoveries	-	341,021	-	341,021
End of Year	$ 1,510,610	$ 285,673	$ 3,738	$ 1,800,021
Reserves				
Specific	$ -	$ -	$ -	$ -
General	1,510,610	285,673	3,738	1,800,021
	$ 1,510,610	$ 285,673	$ 3,738	$ 1,800,021
Evaluated for impairment				
Individually	$ -	$ -	$ -	$ -
Collectively	76,580,117	12,388,806	68,339	89,037,262
	$ 76,580,117	$ 12,388,806	$ 68,339	$ 89,037,262
December 31, 2020				
Allowance for Loan Losses				
Beginning of Year	$ 1,073,323	$ 257,884	$ 775	$ 1,331,982
Provisions	192,226	(41,998)	(228)	150,000
Charge-offs	-	(17,851)	-	(17,851)
End of Year	$ 1,265,549	$ 198,035	$ 547	$ 1,464,131
Reserves				
Specific	$ -	$ -	$ -	$ -
General	1,265,549	198,035	547	1,464,131
	$ 1,265,549	$ 198,035	$ 547	$ 1,464,131
Evaluated for impairment				
Individually	$ -	$ 55,870	$ -	$ 55,870
Collectively	87,730,987	35,661,726	14,136	123,406,849
	$ 87,730,987	$ 35,717,596	$ 14,136	$ 123,462,719

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, collateral adequacy, credit documentation, and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis typically includes larger, non-homogeneous loans such as commercial real estate and commercial and industrial 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 considered as pass meet all of the Company's underwriting criteria and are categorized into four different risk categories based on the level of protection provided to the Company by the paying capacity of the borrower and the value and marketability of the collateral.

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 pledge, 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.

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

December 31, 2021	Pass	Special Mention	Substandard	Impaired	Total
Real estate					
Construction	$ 85,275	$ -	$ -	$ -	$ 85,275
1-4 family	22,324,073	-	-	-	22,324,073
Commercial real estate	53,799,375	-	371,394	-	54,170,769
Commercial and industrial	11,701,167	687,639	-	-	12,388,806
Consumer	68,339	-	-	-	68,339
	$ 87,978,229	$ 687,639	$ 371,394	$ -	$ 89,037,262

December 31, 2020	Pass	Special Mention	Substandard	Impaired	Total
Real estate					
1-4 family	$ 23,989,927	$ -	$ 873,721	$ -	$ 24,863,648
Commercial real estate	59,684,406	3,182,933	-	-	62,867,339
Commercial and industrial	35,661,726	-	-	55,870	35,717,596
Consumer	14,136	-	-	-	14,136
	$ 119,350,195	$ 3,182,933	$ 873,721	$ 55,870	$ 123,462,719

The following table summarizes the payment status of the loan portfolio as of December 31:

December 31, 2021	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Not Past Due	Total	Nonaccrual
Real estate						
Construction	$ -	$ -	$ -	$ 85,275	$ 85,275	$ -
1-4 family	-	-	-	22,324,073	22,324,073	-
Commercial real estate	-	-	-	54,170,769	54,170,769	-
Commercial and industrial	-	-	-	12,388,806	12,388,806	-
Consumer	-	-	-	68,339	68,339	-
	$ -	$ -	$ -	$ 89,037,262	$ 89,037,262	$ -

December 31, 2020	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Not Past Due	Total	Nonaccrual
Real estate						
1-4 family	$ -	$ -	$ -	$ 24,863,648	$ 24,863,648	$ -
Commercial real estate	-	-	-	62,867,339	62,867,339	-
Commercial and industrial	-	-	-	35,717,596	35,717,596	55,870
Consumer	-	-	-	14,136	14,136	-
	$ -	$ -	$ -	$ 123,462,719	$ 123,462,719	$ 55,870

Information relating to individually impaired loans presented by class of loans was as follows as of December 31, 2020:

December 31, 2020	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
Without a Related Allowance Recorded					
Commercial real estate	$ 55,870	$ 55,870	$ -	$ 195,058	$ -

The Company had no impaired loans as of December 31, 2021. The Company had no loans classified as Troubled Debt Restructurings (TDR's) as of December 31, 2021 and 2020, respectively.

Note 4 - Premises and Equipment

Premises and equipment are as follows:

	2021	2020
Leasehold improvements	$ 890,212	$ 730,561
Furniture, fixtures, and equipment	446,871	371,859
Computers	1,432,291	1,274,797
	2,769,374	2,377,217
Accumulated depreciation and amortization	(2,226,890)	(2,113,471)
	$ 542,484	$ 263,746

Total depreciation expense for the years ended December 31, 2021 and 2020, was $113,419 and $99,265, respectively.

Note 5 - Leases

The Company has entered into leases for all of its branch locations. The leases expire at various dates through August of 2025. These leases also include provisions for periodic rent increases as well as payment by the lessee of certain operating expenses. 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.

Balance sheet and other information relating to leases at December 31, 2021 and 2020 is shown below.

	2021	2020
Operating Lease Right-of-Use Assets	$ 1,771,071	$ 587,676
Operating Lease Liabilities (included in other liabilities)	$ 2,207,435	$ 610,936
Weighted-Average Remaining Lease Term, in Years	2.95	3.83
Weighted-Average Discount Rate	5.00%	5.00%

The Company elected, for all classes of underlying assets, not to separate lease and non-lease components and instead to account for them as a single lease component. 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 year ended December 31, 2021 and 2020:

	2021	2020
Operating lease cost	$ 270,953	$ 179,403
Variable lease cost	58,919	6,027
Total lease costs	$ 329,872	$ 185,430

The Company subleases space in one branch location acquired in the branch acquisition that closed in September 2021 and recognized rental income of $47,061 in 2021.

	2021	2020
Other Information		
Cash Paid for Amounts Included in the Measurement of Lease Liabilities	$ 352,332	$ 188,752
Right-of-Use Assets Obtained in Exchange for Lease Obligations	$ 1,454,346	$ -

Maturities of lease liabilities for periods indicated:

Year Ending	
2022	$ 844,476
2023	763,280
2024	618,275
2025	155,136
Total lease payments	2,381,167
Less imputed interest	(173,732)
Present value of net future minimum lease payments	$ 2,207,435

Note 6 - Deposits

Interest-bearing and noninterest-bearing deposits consist of the following:

	2021	2020
NOW accounts	$ 29,261,783	$ 19,613,440
Savings and money market	85,385,412	55,238,250
Time certificate of deposit accounts under $250,000	5,343,350	2,391,577
Time certificate of deposit accounts $250,000 and over	2,944,510	5,289,311
Total interest-bearing deposits	122,935,055	82,532,578
Total noninterest-bearing deposits	134,624,786	78,996,654
Total deposits	$ 257,559,841	$ 161,529,232

As of December 31, 2021, all noninterest-bearing deposits are demand deposits. The maturity of time certificates of deposit is as follows:

	2021	2020
Within one year	$ 5,110,633	$ 3,609,890
One year to three years	3,173,806	3,279,643
Over three years	3,421	791,355
	$ 8,287,860	$ 7,680,888

Note 7 - Income Taxes

Income tax expense included in the statements of income consist of the following:

	2021	2020
Current		
Federal	$ 24,593	$ 280,032
State	3,430	165,000
	28,023	445,032
Deferred taxes	3,000	(58,000)
Total income tax expense	$ 31,023	$ 387,032

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:

	2021	2020
Deferred Tax Assets		
Accrual to cash	$ 111,000	$ 14,000
Allowance for loan losses due to tax limitations	101,000	101,000
Depreciation differences	65,000	75,000
Deferred compensation	57,000	-
Unrealized loss on debt securities available for sale	315,000	-
Other, net	212,000	156,000
	861,000	346,000
Deferred Tax Liabilities		
Deferred loan costs	59,000	69,000
Unrealized gain on debt securities available for sale	-	128,000
Goodwill	185,000	44,000
Other, net	212,000	140,000
	456,000	381,000
Net deferred tax assets (liabilities)	$ 405,000	$ (35,000)

The Company does not expect the total amount of unrecognized tax benefits to significantly increase or decrease in the next twelve months.

The Company is subject to federal income tax and franchise tax of the state of California. Income tax returns for the years ending after December 31, 2017 are open to audit by the federal authorities and for the years ending after December 31, 2016 are open to audit by California state authorities.

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

	2021		2020	
	Amount	Rate	Amount	Rate
Statutory Federal tax	$ 46,000	21.0%	$ 296,000	21.0%
State franchise tax, net of Federal benefit	(30,000)	-13.7%	116,000	8.2%
Other items, net	15,023	6.8%	(24,968)	-1.8%
Actual tax expense	$ 31,023	14.1%	$ 387,032	27.4%

The Company has determined that a valuation allowance is not required as it appears that it is more likely than not that the deferred tax asset will be realized, based upon an estimate of future taxable income.

Note 8 - Stock-Based Compensation

The Company's Stock Option Plan (the Plan) provides that officers and key employees may be granted both nonqualified and incentive stock options and directors and other consultants, who are not also an officer or employee, may only be granted nonqualified stock options. The Plan also permits the grant of stock appreciation rights, restricted shares, restricted stock units, performance shares and performance unit awards. The maximum aggregate number of shares that may be issued pursuant to awards granted under the Plan is 200,000 shares.

Stock options expire no later than ten years from the date of the grant and generally vest over five years. The Plan provides for accelerated vesting if there is a change of control, as defined in the Plan. The Company had stock-based compensation cost in 2021 and 2020 of $67,408 and related tax benefits were $15,900, per year. The fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model.

A summary of the status of the Company's stock option plan and changes during the year is presented below:

	2021	
	Shares	Weighted-Average Exercise Price
Balance, beginning of year	160,250	$ 6.80
Options granted	-	-
Options exercised	-	-
Options forfeited	(6,900)	6.80
Options expired	-	-
Balance, end of year	153,350	$ 6.80
Options exercisable, end of year	92,010	$ 6.80

As of December 31, 2021, the Company had $120,326 of unrecognized compensation cost related to the outstanding stock options that will be recognized over a weighted-average period of 1.4 years. There was $248,427 and $199,013 in intrinsic value in the options outstanding and exercisable as of December 31, 2021.

A summary of the status of unvested restricted stock units awarded under the Plan as of December 31, 2021 and changes during the year then ended is presented below:

	2021	
	Unvested Shares	Weighted-Average Grant Date Fair Value
Balance, beginning of year	-	$ -
Granted	200,000	9.50
Vested	-	-
Forfeited or expired	-	-
Balance, end of year	200,000	$ 9.50

One half of the outstanding unvested restricted stock units at December 31, 2021 are subject to various performance conditions which the Company has assumed will be achieved for purposes of recognizing compensation cost and will be recognized ratably over the 5 year requisite service period. All restricted stock units were granted on December 31, 2021 and therefore no compensation expense was recognized in 2021. As of December 31, 2021, the Company had $1.9 million of unrecognized compensation cost related to restricted stock units that will be recognized over a weighted-average period of 3.0 years.

Note 9 - Other Borrowings

At year-end, advances from the FHLB were as follows:

	2021	2020
Balance at end of year	$ 12,000,000	$ 20,500,000
Weighted average interest rate at end of year	2.12%	1.63%
Weighted average interest rate for the year	1.64%	2.05%

FHLB advances are secured with eligible collateral consisting of the unpaid principal balance of $82.3 million of pledged loans.

Advances from the FHLB are subject to the FHLB's collateral and underwriting requirements. Unused borrowing capacity based on pledged collateral was $43.5 million and $30.5 million as of December 31, 2021 and 2020, respectively.

The maturities of FHLB advances were as follows:

Year Ending December 31,	Amount	Average Interest Rate
2027	$ 3,000,000	2.17%
2030	9,000,000	2.10%
Total	$ 12,000,000	

At December 31, 2021 and 2020, the Company has an unsecured revolving line of credit with Pacific Coast Bankers Bank and Zions Bank, providing for Federal fund purchases up to a total of $9,000,000. Borrowings are payable on demand and interest on outstanding borrowings accrues at rates negotiated at the time of the borrowing. In addition, the Company has a borrowing relationship with the Federal Reserve Bank and has borrowing capacity of approximately $184,000 based on securities pledged with a carrying value of approximately $180,000. As of December 31, 2021 and 2020, the Company did not have any outstanding borrowings on these lines of credit.

Note 10 - Fair Value Measurements

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

Debt Securities: The fair value of debt securities available for sale are determined by obtaining quoted prices on nationally recognized exchanges (Level 1) or matrix pricing which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather relying on the security's relationship to other benchmark quoted securities resulting in a Level 2 classification.

The following table provides a summary of the financial instruments the Company measures at fair value on a recurring basis as of December 31, 2021:

	Fair Value Measurements Using			
As of December 31, 2021	(Level 1)	(Level 2)	(Level 3)	Total
Assets and liabilities measured on a recurring basis				
Debt securities available for sale	$ -	$ 118,313,949	$ -	$ 118,313,949

The following table provides a summary of the financial instruments the Company measures at fair value on a recurring basis as of December 31, 2021:

	Fair Value Measurements Using			
As of December 31, 2020	(Level 1)	(Level 2)	(Level 3)	Total
Assets and liabilities measured on a recurring basis				
Debt securities available for sale	$ -	$ 20,070,410	$ -	$ 20,070,410

Note 11 - Fair Value of Financial Statements

The fair value of financial instruments 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 the current interest rate environment and future expected loss experience, economic conditions, cash flows, and 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 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 fair value hierarchy level and estimated fair value of significant financial instruments at December 31, 2021 and 2020, are summarized as follows (dollars in thousands):

		2021		2020	
	Fair Value Hierarchy	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets					
Cash and cash equivalents	Level 1	$ 65,028	$ 65,028	$ 50,912	$ 50,912
Debt securities available for sale	Level 2	118,314	118,314	20,070	20,070
Debt securities held to maturity	Level 2	8,544	7,991	2,000	1,840
Loans, net	Level 3	87,123	87,256	121,766	119,306
Restricted stock and equity securities	Level 2	2,632	2,632	2,632	2,632
Liabilities					
Deposits	Level 2	$ 257,560	$ 258,354	$ 161,529	$ 150,459
FHLB borrowings	Level 2	12,000	12,320	20,500	20,764

Note 12 - Financial Instruments with Off Balance Sheet Risk

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

The Company's exposure to credit losses in the event of nonperformance by the other parties for commitments to extend credit and standby letters of credit is represented by the contractual amount of these instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

The following is a summary of contractual or notional amounts of off-balance sheet financial instruments that represent credit risk:

	2021	2020
Financial instruments whose contract amounts represent credit risks:		
Commitments to extend credit	$ 22,931,000	$ 20,944,457

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any conditions established in the contract. Except for home equity lines of credit, commitments generally have fixed expiration dates of not more than 12 months and may require payment of a fee. Since many of the commitments are not expected to be drawn upon, the total commitment amounts may not represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include marketable investment securities, accounts receivable, inventory, property, plant and equipment, and real properties.

Note 13 - Related Party Transactions

In the ordinary course of business, the Company may grant loans to certain officers and directors and the companies with which they are associated. In the Company's opinion, all loans and loan commitments to such parties will be made on substantially the same terms including interest rates and collateral, as those prevailing at the time of comparable transactions with other persons. The Company had no related party loans outstanding as of December 31, 2021 and $536,488 of related party loans outstanding as of December 31, 2020. In addition, the Company had an unused letter of credit to a related party for $249,000 and $618,000 as of December 31, 2021 and 2020, respectively.

Deposits from certain directors, executives, and shareholders and their related interest with which they are associated held by the Company at December 31, 2021 and 2020, amounted to $3,180,824 and $10,758,951, respectively.

The Bank’s former Chief Executive Officer and current Board member is a member of the Board of Directors for the company that provides core data processing services to the Bank.

Note 14 - Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Capital adequacy guidelines and prompt corrective action regulations involve quantitative measures of assets, liabilities and certain off balance sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital. Management believes, as of December 31, 2021 and 2020, that the Bank met all capital adequacy requirements to which it was subject.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and capital restoration plans are required. As of December 31, 2021 and 2020, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the Bank's category.

The following table presents actual and required capital ratios as of December 31, 2021 and 2020 (dollars in thousands):

	Actual		For Capital Adequacy Purposes		Under Prompt Corrective Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2021						
Total capital (to risk-weighted assets)	$ 19,796	15.79%	$ 10,032	8.0%	$ 12,541	10.0%
Tier 1 capital (to risk-weighted assets)	18,226	14.53%	7,524	6.0%	10,032	8.0%
Common Equity Tier 1 Capital (to Risk-Weighted Assets)	18,226	14.53%	13,939	4.5%	20,134	6.5%
Tier 1 capital (to average assets)	18,226	5.88%	5,016	4.0%	6,270	5.0%
As of December 31, 2020						
Total capital (to risk-weighted assets)	$ 21,103	20.05%	$ 8,421	8.0%	$ 10,526	10.0%
Tier 1 capital (to risk-weighted assets)	19,785	18.80%	6,316	6.0%	8,421	8.0%
Common Equity Tier 1 Capital (to Risk-Weighted Assets)	19,785	18.80%	4,737	4.5%	6,842	6.5%
Tier 1 capital (to average assets)	19,785	9.30%	8,506	4.0%	10,633	5.0%

The California Financial Code provides that a bank may not make a cash distribution to its stockholders in excess of the lesser of the Bank's undivided profits or the bank's net income for its last three fiscal years, less the amount of any distribution made to the bank's stockholders during the same period.

Note 15 - Employee Retention Tax Credit

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) provided an employee retention credit (the Credit) which is a refundable tax credit against certain employment taxes of up to $5,000 per employee for eligible employers. The Credit is equal to 50% of qualified wages paid to employees, capped at $10,000 of qualified wages through December 31, 2020.

The Consolidated Appropriations Act of 2021 and the American Rescue Plan Act of 2021 (collectively the Acts) expanded the availability of the Credit and extended the Credit through December 31, 2021. The Infrastructure Investment and Jobs Act subsequently terminated the Credit program effective October 1, 2021. The Acts increased the credit to 70% of qualified wages, capped at $10,000 per quarter. As a result of the changes to the Credit, the maximum credit per employee increased from $5,000 in 2020 to $21,000 in 2021.

The Company was eligible for the credit in various quarters in 2020 and 2021 and during the year ended December 31, 2021 recorded a benefit of $491,307, which is included in noninterest income in the consolidated statement of income.

The Company has filed for refunds of the Credit in the 4th quarter 2021 and cannot reasonably estimate when it will receive any or all of the claimed refunds. Refunds claimed are included in accrued interest receivable and other assets in the December 31, 2021 consolidated balance sheet.

Note 16 - Acquisitions

On September 24, 2021, the Company acquired three branch locations from the Bank of Southern California, N.A, in Orange, Redlands and Santa Fe Springs, California. The acquisition included customer deposits totaling $82,384,124, assignment of the lease agreements for the three locations and several employees. The cash purchase price was $975,945.

The items acquired were deemed to constitute a business under Generally Accepted Accounting Principles and therefore the acquisition was accounted for as a business combination.

The Company acquired the branches to strategically increase its existing presence in the Los Angeles and surrounding area. Goodwill in the amount of $977,938 was recognized in this acquisition. Goodwill represents the future economic benefits arising from net assets acquired that are not individually identified and separately recognized and is attributable to synergies expected to be derived from the acquisition. Goodwill recorded on this transaction is deductible for income tax purposes.

The following table represents the assets acquired and liabilities assumed as of September 24, 2021 and the fair value adjustments and amounts recorded by the Company in 2021 under the acquisition method of accounting.

	Book Value	Fair Value Adjustments	Fair Value
ASSETS ACQUIRED			
Cash and cash equivalents	$ 82,044,268	$ -	$ 82,044,268
Right of use asset	1,899,339	(444,993)	1,454,346
Core deposit intangible	-	443,000	443,000
Fixed and other assets	339,856	-	339,856
Total Assets Acquired	$ 84,283,463	$ (1,993)	$ 84,281,470
LIABILITIES ASSUMED			
Deposits	$ 82,384,124	$ -	$ 82,384,124
Lease liabilities	1,899,339	-	1,899,339
Total Liabilities Assumed	84,283,463	-	84,283,463
Excess	-	1,993	1,993
	$ 84,283,463	$ 1,993	
Cash consideration			975,945
Goodwill recognized			$ 977,938

The Company accounted for this transaction under the acquisition method of accounting which requires purchased assets and liabilities assumed to be recorded at their respective fair values at the date of acquisition. The Company determined the fair value of the core deposit intangible with the assistance of a third-party appraisal. The fair value of other assets acquired and liabilities assumed was determined by various methods including estimation of cash flows expected to result from those assets and liabilities.

Note 17 - Formation of Friendly Hills Bancorp

During 2021, Friendly Hills Bank became a wholly-owned subsidiary of Friendly Hills Bancorp in an exchange of stock between entities under common control. Friendly Hills Bancorp issued 2,006,393 shares of common stock in exchange for the surrender of all outstanding shares of the Bank’s common stock. There was no cash involved in this transaction. The transaction was accounted for like a pooling of interest and the consolidated financial statements contained herein have been restated to give full retroactive effect to the transaction.

COMPANY PROFILE

BOARD OF DIRECTORS

Nathan Rogge
President and
Chief Executive Officer

Joe Matranga
Chairman of the Board

Jeffrey K. Ball
Vice Chairman of the Board

Jason Baker
Director

Mercedes Broening
Director

Richard A. Casford
Director

W.C. ("Chris") Greenbeck
Director

Christopher Naghibi
Director

Sara Nofeliyan
Director

EXECUTIVE OFFICERS

Nathan Rogge
President and
Chief Executive Officer

James Burgess
Executive Vice President,
Chief Financial Officer

Elizabeth M. Buckingham
Executive Vice President,
Chief Operating Officer

Robert A. Marshall
Executive Vice President,
Chief Credit Officer

Azim Sheikh
Executive Vice President,
Chief Information and
Technology Officer

Paulette Silva
Executive Vice President,
Chief Administration Officer

LOCATIONS

Del Mar Office
3579 Valley Centre Drive,
Suite 175
San Diego, CA 92130

Orange Office
625 The City Drive South,
Suite 140
Orange, CA 92868

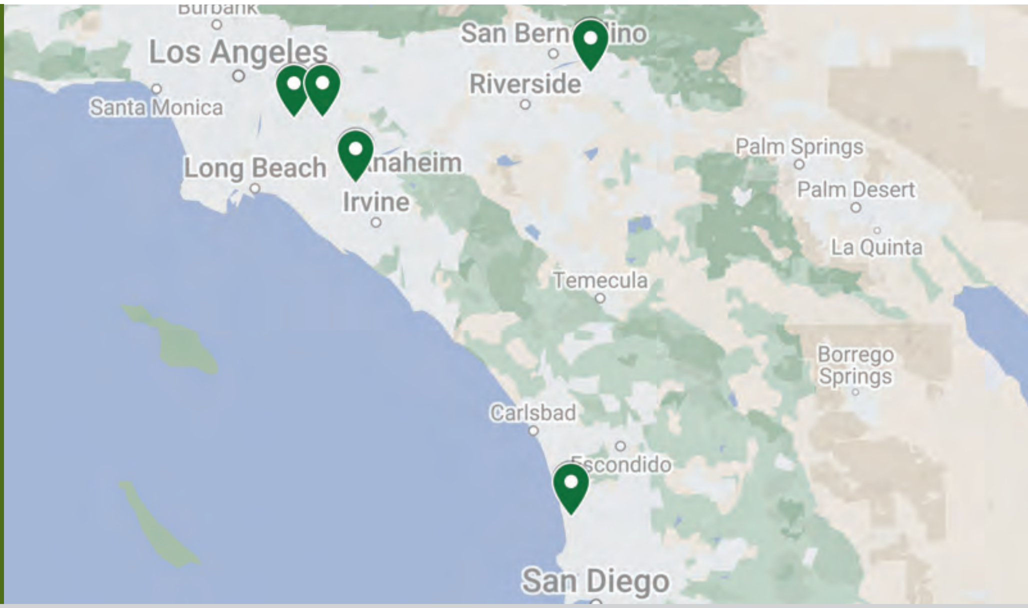
Redlands Office
408 E State St.
Redlands, CA 92373

Santa Fe Springs Office
12070 Telegraph Road,
Suite 100
Santa Fe Springs, CA 90670

Whittier Office
16011 Whittier Blvd.
Whittier, CA 90603

COMMON STOCK

The common stock trades
on OTC Markets (OTC Pink)
under the symbol FHLB.



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