



Financial Statements
December 31, 2023

Beach Cities Commercial Bank

Independent Auditor’s Report	1
Statement of Financial Condition	3
Statement of Operations and Comprehensive Loss	4
Statement of Changes in Shareholders’ Equity.....	5
Statement of Cash Flows	6
Notes to Financial Statements	7



Independent Auditor's Report

The Board of Directors and Shareholders of
Beach Cities Commercial Bank
Irvine, California

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Beach Cities Commercial Bank, which comprise the statement of financial condition as of December 31, 2023, and the related statement of operations and comprehensive loss, changes in shareholders' equity, and cash flows for the year then ended, and the related notes to the financial statements.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of Beach Cities Commercial Bank as of December 31, 2023, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit 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 Financial Statements section of our report. We are required to be independent of Beach Cities Commercial Bank, and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. 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 Financial Statements

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

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

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the 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 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 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 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 Beach Cities Commercial Bank'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 financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Beach Cities Commercial Bank'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
January 30, 2024

Beach Cities Commercial Bank
Statement of Financial Condition
December 31, 2023

	2023
Assets	
Cash and due from banks	\$ 996,078
Interest-bearing balance at the Federal Reserve Bank	20,985,000
Total cash and cash equivalents	21,981,078
Debt securities available for sale, at fair value (amortized cost of \$980,335)	979,802
Loans	
Real estate	10,750,084
Commercial	11,358,825
Total loans	22,108,909
Deferred loan fees, net of costs	(27,972)
Allowance for credit losses	(301,000)
Net loans	21,779,937
Premises and equipment, net	267,726
Right-of-use asset	1,741,353
Accrued interest and other assets	1,206,876
Total assets	\$ 47,956,772
Liabilities and Shareholders' Equity	
Deposits	
Noninterest-bearing	\$ 6,672,688
Interest-bearing	19,185,720
Total deposits	25,858,408
Lease liability	1,833,916
Accrued interest and other liabilities	877,648
Total liabilities	28,569,972
Commitments and Contingencies - Notes 5 and 12	
Shareholders' Equity	
Preferred stock - 20,000,000 shares authorized, none outstanding	-
Common stock - 20,000,000 shares authorized, no par value;	
2,556,112 shares issued and outstanding	25,019,375
Additional paid in capital	199,443
Accumulated deficit	(5,831,485)
Accumulated other comprehensive loss	(533)
Total shareholders' equity	19,386,800
Total liabilities and shareholders' equity	\$ 47,956,772

Beach Cities Commercial Bank
Statement of Operations and Comprehensive Loss
Year Ended December 31, 2023

	2023
Interest Income	
Interest and fees on loans	\$ 336,181
Interest on debt securities	17,320
Interest on federal funds sold and other interest-bearing deposits	821,283
Total interest income	1,174,784
Interest Expense	
Interest on savings, NOW and money market accounts	336,838
Interest on time deposits	11,864
Total interest expense	348,702
Net interest income	826,082
Provision for Credit Losses	
Loans	301,000
Unfunded commitments	16,000
Total provision for credit losses	317,000
Net interest income after provision for credit losses	509,082
Noninterest Income	
Service charges, fees and other	1,706
Noninterest Expense	
Salaries and employee benefits	2,318,336
Occupancy and equipment expenses	408,909
Organization expenses	1,045,800
Other expenses	1,096,480
Total noninterest expense	4,869,525
Loss before income taxes	(4,358,737)
Income Tax Expense	800
Net loss	\$ (4,359,537)
Net loss per share - basic and diluted	\$ (1.71)
Other comprehensive loss - unrealized loss on debt securities available for sale	(533)
Comprehensive loss	\$ (4,360,070)

Beach Cities Commercial Bank
Statement of Changes in Shareholders' Equity
Year Ended December 31, 2023

	Common Stock		Additional Paid In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total
	Number of Shares	Amount				
Balance at January 1, 2023	-	\$ -	\$ -	\$ -	\$ -	\$ -
Initial capitalization	2,556,112	25,561,120	-	-	-	25,561,120
Capital raise expenses	-	(541,745)	-	-	-	(541,745)
Organization expenses incurred prior to 2023	-	-	-	(1,471,948)	-	(1,471,948)
Stock-based compensation	-	-	199,443	-	-	199,443
Net loss	-	-	-	(4,359,537)	-	(4,359,537)
Other comprehensive loss	-	-	-	-	(533)	(533)
Balance at December 31, 2023	<u>2,556,112</u>	<u>\$ 25,019,375</u>	<u>\$ 199,443</u>	<u>\$ (5,831,485)</u>	<u>\$ (533)</u>	<u>\$ 19,386,800</u>

Beach Cities Commercial Bank
Statement of Cash Flows
Year Ended December 31, 2023

	2023
Operating Activities	
Net Loss	\$ (4,359,537)
Adjustments to Reconcile Net Loss to Net Cash used in Operating Activities	
Debt securities accretion	(17,320)
Depreciation and amortization	55,118
Provision for credit losses	317,000
Stock-based compensation	199,443
Other items	(244,768)
	(4,050,064)
Net Cash used in Operating Activities	(4,050,064)
Investing Activities	
Purchase of debt securities available for sale	(963,015)
Net increase in loans	(22,080,937)
Purchases of premises and equipment	(322,844)
	(23,366,796)
Net Cash used in Investing Activities	(23,366,796)
Financing Activities	
Net change in noninterest bearing deposits	6,664,791
Net change in interest bearing deposits	19,185,720
Proceeds from initial capitalization	25,019,375
Organization expenses incurred prior to 2023	(1,471,948)
	49,397,938
Net Cash provided by Financing Activities	49,397,938
Increase in Cash and Cash Equivalents	21,981,078
Cash and Cash Equivalents at Beginning of Year	-
	21,981,078
	\$ 21,981,078
Supplemental Disclosures of Cash Flow Information	
Interest Paid	\$ 343,647
Taxes Paid	\$ 800
Lease liabilities arising from obtaining right of use assets	\$ 2,064,117

Note 1 - Summary of Significant Accounting Policies

Nature of Operations

Beach Cities Commercial Bank (the Bank) was incorporated under the laws of the State of California on April 11, 2022. The Bank opened for business on June 12, 2023 after receiving bank regulatory approval and began providing a full range of banking services from its locations in Irvine and Encinitas California. The Bank operates primarily in the Southern California market, offering checking and savings accounts and certificates of deposit as well as commercial and real estate loans.

Subsequent Events

The Bank has evaluated subsequent events for recognition and disclosure through January 30, 2024, which is the date the financial statements were available to be issued.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. An estimate that is particularly susceptible to significant change in the near term is the determination of the allowance for credit losses.

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 Bank is not exposed to any significant credit risks on cash and cash equivalents.

Debt Securities

The Bank 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 (loss). Securities, which the Bank has the positive intent and ability to hold to maturity, are classified as held-to-maturity and are carried at amortized cost. As of December 31, 2023 the Bank had only securities available for sale.

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.

Allowance for Credit Losses (ACL) – Available-for-Sale Securities

For available-for-sale debt securities, the Bank evaluates, on an individual basis, whether a decline in fair value below the amortized cost basis has resulted from a credit loss or other factors. The portion of the decline attributable to credit losses is recognized through an ACL, and changes in the ACL on available-for-sale debt securities are recorded as a provision for credit losses in the consolidated statements of operations. The portion of decline in fair value below the amortized cost basis not attributable to credit is recognized through other comprehensive income (loss), net of applicable taxes.

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 or specific valuation accounts and net of any 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 Credit Losses (ACL) - Loans

The ACL for loans is a valuation account that is deducted from the loan's amortized cost basis to present the net amount expected to be collected on the loans. Loans are charged-off against the allowance when management believes the recorded loan balance is confirmed as uncollectible. Expected recoveries do not exceed the aggregate of amounts previously charged-off and expected to be charged-off.

Management estimates the allowance balance using relevant information for each loan segment, from internal and external sources, relating to past events, current conditions, and reasonable and supportable forecasts. The ACL for loans is measured on a pooled basis when similar risk characteristics exist. The Bank uses publicly available data from Schedule RI-C of the Call Report to derive initial proxy expected lifetime loss rates. This data is obtained using the Scaled CECL Allowance for Losses Estimator (SCALE) developed by the Federal Reserve Bank to assist smaller community institutions in calculating CECL. Management adjusts the proxy expected lifetime loss rates to reflect Bank-specific facts and circumstances to arrive at the final ACL estimate.

Adjustments by management at December 31, 2023 included a concentration adjustment on real estate loans and a negative adjustment on commercial loans relating to presence of certain loan guarantees.

A loan is considered to be collateral dependent when repayment is expected to be provided substantially through the operation or sale of the collateral. The ACL on collateral dependent loans is measured using the amortized cost basis of the financial asset less the fair value of the underlying collateral, adjusted for costs to sell, when applicable. If the value of the underlying collateral is determined to be less than the recorded amount of the loan, a specific reserve for that loan is recorded. If the Bank determines that the loss represented by the specific reserve is uncollectible it records a charge-off for the uncollectible portion.

Portfolio segments identified by the Bank include real estate and commercial 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 and collateral type.

Allowance for Credit Losses – Unfunded Commitments

The Bank also maintains a separate allowance for unfunded commitments. Management estimates anticipated losses using expected loss factors consistent with those used for the ACL methodology for loans described above, and utilization assumptions based on historical experience. Provision for credit losses for unfunded commitments is included in provision for credit losses in the statements of operations and added to the allowance for unfunded commitments, which is included in accrued interest and other liabilities in the statement of financial condition.

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, equipment and computer 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 Bank determines if an arrangement contains a lease at contract inception and recognize 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 Bank does not take into account the options in calculating the ROU asset and lease liability unless it is reasonably certain such options will be reasonably exercised. As of December 31, 2023, no lease extension options have been included in the calculating the ROU asset and lease liability.

The present value of lease payments is determined based on the Bank'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 statement of financial condition. Lease expense is recognized on a straight-line basis over the lease term. The Bank has elected to account for lease agreements with lease and non-lease components as a single lease component.

Commitments to Extend Credit

In the ordinary course of business, the Bank has entered into off-balance sheet financial instruments consisting of commitments to extend 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.

Advertising Costs

The Bank expenses the costs of advertising in the period incurred. Such costs totaled \$654 for the year ended December 31, 2023.

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 carry forwards depends on having sufficient taxable income of an appropriate character within the carry forward periods.

The Bank 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. Interest and penalties related to uncertain tax positions are recorded as part of income tax expense.

Comprehensive Loss

Comprehensive loss consists of net loss and other comprehensive loss. Other comprehensive loss includes unrealized losses on securities available-for-sale.

Earnings Per Share (EPS)

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. The Bank has an operating loss for the year and therefore basic and diluted EPS are the same. Weighted-average outstanding shares used the calculation of EPS was 2,556,112.

Stock-Based Compensation

Compensation cost is recognized for stock options and restricted stock awards issued to employees, 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 Bank's common stock at the date of grant is used for restricted stock awards.

Compensation cost is recognized over the required service period, generally defined as the vesting period, on a straight-line basis. The Bank 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 statement of operations when incurred. See Note 9 for additional information on the Bank's stock option plan.

Revenue Recognition

The majority of the Bank's revenues come from interest income on bank deposits, debt securities and loans, which is outside the scope of Topic 606. The Bank's services that fall within the scope of Topic 606 are presented within Non-Interest Income and are recognized as revenue as the Bank satisfies its obligation to the customer. Services within the scope of Topic 606 include service charges on deposits.

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 15 for more information and disclosures relating to the Bank's fair value measurements.

Note 2 - Debt Securities

The following table summarizes the amortized cost and fair value of the available-for-sale debt securities portfolio at December 31, 2023 and the corresponding amounts of gross unrealized gains and losses recognized in accumulated other comprehensive income (loss):

Available-for-Sale Securities	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2023				
U.S. Treasury securities	\$ 980,335	\$ -	\$ (533)	\$ 979,802

Available-for-sale debt securities consisted of U.S. Treasury securities, which are explicitly guaranteed by the U.S. government. Consequently, the Bank did not record a related allowance for credit losses at December 31, 2023.

U.S. Treasury securities all mature within one year. All securities are pledged at the Federal Reserve Bank to secure borrowing arrangements.

Note 3 - Loans and Allowance for Credit Losses (ACL)

The Bank's loan portfolio consists primarily of loans to borrowers within California. Although the Bank 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 Bank's market area and, as a result, the Bank's loan and collateral portfolios are, to some degree, concentrated in those industries.

The following table presents the activity in the ACL on loans and unfunded commitments for the year ended December 31, 2023:

	Real Estate	Commercial	Total
Allowance for Credit Losses - Loans			
Beginning of Year	\$ -	\$ -	\$ -
Provisions	163,856	137,144	301,000
End of Year	\$ 163,856	\$ 137,144	\$ 301,000
Allowance for Credit Losses - Unfunded Commitments			
Beginning of Year	\$ -	\$ -	\$ -
Provisions	1,213	14,787	16,000
End of Year	\$ 1,213	\$ 14,787	\$ 16,000

The Bank categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, collateral adequacy, credit documentation, and current economic trends, among other factors. The Bank 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 Bank 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.

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

The risk category of loans by class of loans was as follows as of December 31, 2023:

	Pass	Special Mention	Substandard	Doubtful	Total
Real Estate					
Commercial	\$ 8,830,584	\$ -	\$ -	\$ -	\$ 8,830,584
1-4 Residential	1,919,500	-	-	-	1,919,500
Commercial	11,358,825	-	-	-	11,358,825
	<u>\$ 22,108,909</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 22,108,909</u>

All loans were originated during the year 2023.

The Bank had no past due or nonaccrual loans as of December 31, 2023.

Note 4 - Premises and Equipment

A summary of premises and equipment as of December 31, 2023 follows:

	2023
Leasehold improvements	\$ 137,424
Furniture, fixtures, and equipment	185,420
	322,844
Less accumulated depreciation and amortization	(55,118)
	\$ 267,726

Depreciation and amortization expense for the year ended December 31, 2023 was \$55,118.

Note 5 - Leases

The Bank leases office facilities under long-term, non-cancelable operating lease agreements. The leases provide for increases in future minimum annual rental payments based on defined increases. Also, the agreements require the Bank to pay real estate taxes, insurance, utilities and common area maintenance.

The weighted-average discount rate is based on an applicable incremental borrowing rate, which is estimated using the Bank's applicable borrowing rates and the contractual lease term. The weighted-average remaining lease term and discount rate was 4.7 years and 5.5% at December 31, 2023, respectively.

Operating lease cost was \$326,799 for the period from the opening of business on June 12, 2023 through December 31, 2023 and is included in occupancy and equipment expense in the statement of operations. Cash paid for amounts included in the measurement of lease liabilities was \$415,787.

The future minimum lease payments under noncancelable operating leases are as follows as of December 31, 2023:

Year Ending		
2024	\$	440,432
2025		455,150
2026		470,191
2027		428,032
2028		152,250
After 2028		144,750
Total lease payments		2,090,805
Less imputed interest		(256,889)
Present value of net future minimum lease payments	\$	1,833,916

Note 6 - Deposits

At December 31, 2023, time deposits totaled \$646,348, all of which mature within one year. Time deposits with balances over the FDIC insured limit of \$250,000 totaled \$508,761.

Note 7 - Borrowings

The Bank has unused unsecured lines of credit with correspondent banks with a total borrowing capacity of \$8.0 million at December 31, 2023. The Bank has financing availability at the Federal Home Loan Bank of San Francisco of approximately \$9.8 million, subject to pledged collateral requirements. The Bank also can borrow from the Federal Reserve Bank discount window, based on pledged securities with a par value of \$1.0 million.

Note 8 - Income Taxes

The income tax expense for the year ended December 31, 2023 is comprised of the following:

	2023
Current	
Federal	\$ -
State	800
	800
Deferred	1,708,000
Valuation Allowance	(1,708,000)
	\$ 800

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 statement of financial condition at December 31, 2023:

	2023
Deferred Tax Assets	
Organization expenses	\$ 417,000
Allowance for loan losses	82,000
Net operating loss carryover	1,176,000
Other items	33,000
	1,708,000
Valuation Allowance	(1,708,000)
	\$ -
Net deferred tax assets	

The valuation allowance was established because the Bank has not reported earnings sufficient enough to support the recognition of the net deferred tax assets. As of December 31, 2023, the Bank has federal and state net operating loss carryovers of approximately \$4.0 million each, which begin to expire for California franchise tax purposes in 2043. Federal net operating loss carryovers do not expire.

Note 9 - Stock-Based Compensation

The Bank's 2023 Stock Plan (the Plan) was approved by its Board of Directors on May 31, 2023. The 2023 Plan has authorized 30% of issued and outstanding shares of common stock (766,833 shares) that may subject of awards, of which no more than 600,000 shares may be awarded in the form of incentive stock options.

Stock-based compensation expense for the year ended December 31, 2023 was \$199,443.

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions:

	<u>2023</u>
Expected Volatility	22.3%
Expected Term	7.5 years
Expected Dividend Yield	0%
Risk Free Rate	3.86%
Grant Date Fair Value	\$3.57

Since the Bank has a limited amount of historical stock activity, the expected volatility is based on the historical volatility of similar banks that have a more active trading history.

A summary of the status of the Bank's stock option plan as of December 31, 2023, and changes during the year then ended, is presented below:

	<u>Shares</u>	<u>Weighted- Average Exercise Price</u>	<u>Weighted- Average Remaining Contractual Term</u>	<u>Aggregate Intrinsic Value</u>
Outstanding at Beginning of Year	-	\$ -		
Granted	425,000	10.00		
Forfeited	(10,000)	10.00		
Outstanding at End of Year	<u>415,000</u>	<u>10.00</u>	<u>9.6 Years</u>	<u>\$ -</u>
Options Exercisable	<u>-</u>	<u>\$ 10.00</u>	<u>9.6 Years</u>	<u>\$ -</u>

A summary of the status of unvested restricted stock units awarded under the Plan as of December 31, 2023 and changes during the year then ended is presented below:

	Unvested Shares	Weighted- Average Grant Date Fair Value
Balance, Beginning of Period	-	\$ -
Granted	91,500	\$ 10.00
Shares Vested	-	\$ -
Forfeited	(20,000)	\$ 10.00
Balance, End of Year	71,500	\$ 10.00

As of December 31, 2023, there was unrecognized compensation cost related to awards granted and outstanding under the Plan of \$2,212,473, to be recognized over a weighted-average life of 2.8 years.

Note 10 - Other Expenses

Other expenses as for the year ended December 31, 2023 are comprised of the following:

	2023
Data processing	\$ 332,424
Legal	36,578
Audit	80,000
Professional and consulting	352,532
Insurance	25,376
Loan expense	17,281
Regulatory assessments	25,134
Director expense	74,652
Supplies	24,266
Business development	36,138
Other	92,099
	\$ 1,096,480

Note 11 - Organizational Period

The Bank incorporated on April 11, 2022. It subsequently received conditional approval from the State of California to organize as a state-chartered bank and opened for business on June 12, 2023. Prior to that date, organizers of the Bank incurred costs in connection with the organizational process and the initial capitalization of the Bank. These organization expenses were reimbursed by the Bank to the organizers and comprised of the following, with costs incurred prior to 2023 charged directly to retained earnings:

	2023	Before 2023
Consulting fees to future employees	\$ 572,468	\$ 1,157,044
Outside consulting fees	82,851	48,017
Legal and professional	25,300	90,647
Occupancy	273,071	34,985
Other	92,110	141,255
	\$ 1,045,800	\$ 1,471,948

Note 12 - Commitments

In the ordinary course of business, the Bank enters into financial commitments to meet the financing needs of its customers. These financial commitments include commitments to extend credit. Those instruments involve to varying degrees, elements of credit and interest rate risk not recognized in the Bank's financial statements. The Bank'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 Bank uses the same credit policies in making commitments as it does for loans reflected in the financial statements.

As of December 31, 2023, the Bank had the following outstanding financial commitments whose contractual amount represents credit risk:

	2023
Commitments to Extend Credit	\$ 9,893,258

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total amounts do not necessarily represent future cash requirements. The Bank evaluates each client's credit worthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Bank is based on management's credit evaluation of the customer. The majority of the Bank's commitments to extend credit generally are secured by real estate.

Note 13 - Related Party Transactions

In the ordinary course of business, certain employees and executive officers, directors and companies with which they are associated have deposits with the Bank. The balance of these deposits at December 31, 2023 was approximately \$509,000.

Note 14 - Employee 401k Plan

The Bank has adopted a 401(k) for its employees. Under the plan, eligible employees may defer a portion of their salaries. The plan also provides for matching contributions up to 100% of any deferrals not exceeding 5% of compensation. There were no Bank contributions to the 401k Plan for the year ended December 31, 2023.

Note 15 - Fair Value Measurement

The following is a description of valuation methodologies used for assets recorded at fair value:

Debt Securities: The fair values of debt securities available for sale, which include U.S. Treasury securities are determined by quoted market prices.

The following table provides the hierarchy and fair value for each major category of assets and liabilities measured at fair value at December 31, 2023:

December 31, 2023	Fair Value Measurements Using			Total
	Level 1	Level 2	Level 3	
Assets measured at fair value on a recurring basis				
Securities Available-for-Sale	\$ 979,802	\$ -	\$ -	\$ 979,802

Note 16 - Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the federal and state 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.

Effective January 1, 2020, the federal banking agencies jointly issued a final rule that provides for an optional, simplified measure of capital adequacy for qualifying community banking organizations and generally exempts an institution from the risk-based capital and capital conversion buffer requirements. The Community Bank Leverage Ratio (CBLR) final rule will allow qualifying banks that opt-in to the CLBR framework to calculate and report a leverage ratio to measure capital adequacy replacing the risk-based capital reporting requirements. A qualifying community banking organization is defined as having less than \$10 billion in total assets, a leverage ratio greater than 9%, off-balance sheet exposures of 25% or less of total assets, trading assets and liabilities of 5% or less of total assets and is not an advanced approaches institution. Meeting these qualifications, the Bank has elected to opt-in to the CBLR framework.

As of December 31, 2023, the most recent notification from the FDIC 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 FDIC requires the Bank to maintain its Tier 1 Capital to average assets at 8% during the first three years of operations.

To be categorized as well capitalized under the CBLR capital framework, the Bank must maintain the minimum ratio as set forth in the table below. The following table also sets forth the Bank's actual capital amount and ratio (dollar amounts in thousands) as of December 31, 2023:

	Actual		To be Well-Capitalized Under Prompt Corrective Action Regulations (CBLR Framework)	
	Amount	Ratio	Amount	Ratio
As of December 31, 2023				
Tier 1 Capital to average total assets	\$ 19,388	45.3%	\$ 3,849	9.0%

The California Financial Code also provides that a bank may not make a cash distribution to its shareholders 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 by the bank's shareholders during the same period.