Fresno First Bank

2011

Annual Report

Mission Statement

The mission of Fresno First Bank is to become the Bank of choice for business owners, professionals, entrepreneurs and individuals that value a high touch approach, or "relationship" approach to their banking needs. We will accomplish this by:

- Developing an ownership culture that fosters a working environment which encourages professional and financial growth and entrepreneurial freedom.
- Committing to exceed customer service expectations for quality, responsiveness and professional excellence.
- Generating a superior return for our shareholders while investing in the communities we serve.

Values Statement

Fresno First Bank will be the Bank of choice for successful businesses and individuals who value superior service and a relationship approach to their banking and financing needs. Our group of experienced professional bankers will help clients navigate through complex financial choices which will ultimately assist in stimulating economic growth in our community. Our commitment to an ownership culture will foster an exceptional work environment that generates a fair return for our shareholders.

Core Values

We Value:

- The highest standard of ethical behavior and professional integrity.
- An owner-orientated working environment dedicated to teamwork that encourages respect and dignity, while recognizing and rewarding innovation and exceptional performance.
- Proactive, solutions-orientated recommendations that consistently exceed client expectations.
- The loyalty of our client relationships gained by knowing, understanding and placing their needs first.

FRESNO FIRST BANK

Message from the Chairman

The culture at Fresno First Bank is the foundation of our organization. Our culture empowers the Associates, Management Team and the Board of Directors. As Herb Kelleher, co-founder of Southwest Airlines, said:

"Developing people and culture is more influential than the standard five or ten year strategic plan."

Our outstanding performance has been recognized by Bauer Financial, Inc., an independent bank research firm that analyzes financial institutions through a star-rating system. Bauer Financial has awarded Fresno First Bank a "**Five-Star**" rating for 2011. Also the Findley Reports, which publishes the most comprehensive financial institution analysis, has awarded Fresno First Bank the classification of a "**Super Premier Performance**" rating for 2011, their highest rating. These achievements are a testimony to the dedicated efforts of our people along with the culture we have created. We are focused on commitment to our community along with providing the highest level of service through the development of strong relationships with each and every client.

The Board of Directors believes that market value is one of the most vital factors our culture empowers. Each Associate, Management Team Member and Director has the responsibility to think and take action as owners with a stake in the value of Fresno First Bank. With our culture as our foundation and our entrepreneurial spirit, we will continue to build the market value of Fresno First Bank!

At Fresno First Bank we are committed to continually investing in our people. They are the foundation of our Bank and we believe our Bank is the community bank of the future!

David N. Price
Chairman of the Board

Message from the President & CEO

Over the years you have seen and heard a lot about Fresno First Bank's efforts to build a culture of ownership. We, the Board and Management team, decided to develop this strategy because we believed when you appeal to a higher level of thinking you get a higher level of performance.

We have taken this concept to a higher level by embracing "Open Book Management" and "The Great Game of Business". What has changed through the use of these models? Quite simply, responsibility. Now individuals can feel their own importance and see their contribution to the well-being of the Bank. Now every associate is accountable to our shareholders because they are shareholders.

As they say, "The proof is in the pudding." Since 2007, total assets have grown steadily from just over $60 million to more than $177 million. As our assets grow so does our ability to generate interest income which will increase earnings and shareholder value.

By focusing on building relationships we have been successful at increasing deposits and establishing stable, low cost core deposits. Since 2007, our core deposits have increased from $50 million to more than $158 million, and our rate of growth has been nearly twice the average of our peer banks.

Our loan portfolio has grown from $34 million in December of 2007 to more than $100 million today. By comparison, while our peer banks' total loans outstanding have grown erratically and in some years declined, we have seen consistent double digit growth.

We have now recorded three years of increasing income. In addition, to enhance the overall profitability of the Bank, we have started a number of initiatives (Government Guaranteed Lending, Mortgage Lending and Merchant Services Departments) to increase non-interest income. All departments are in full gear and producing new revenue for the Bank.

At Fresno First Bank, we believe that our positive financial performance is directly related to the ownership culture we are developing. Our Board, Management and Associates continue to focus on creating superior returns and creating long term shareholder value.

Richard "Rick" Whitsell
President & CEO

FRESNO FIRST BANK

Board of Directors

Jack Holt,
Director / President of Holt Lumber Company, Inc.

Dr. Robert Kubo,
Director/Orthodontist, Kubo Orthodontic Group

Lorrie Lorenz,
Director / Principal of Lorenz & Associates

Jared Martin,
Director / Realtor, Keller Williams Realty

David Price,
Chairman of the Board / President and CEO of David N. Price & Associates

Mark Saleh,
Director / President of Wm. B. Saleh & Company

Joel Slonski,
Director / CPA with Slonski & Sailors

Al Smith,
Director / President and CEO of the Greater Fresno Area Chamber of Commerce

Dr. Daniel Suchy,
Director / Retired Physician

Richard Whitsell,
Director / President and CEO of Fresno First Bank

Since the founding of our Bank in 2005, our dedicated Board of Directors has provided leadership and an unwavering commitment to the strength of the Bank and the communities we serve.

At Fresno First Bank we believe that corporate governance begins with a well educated and informed Board, Management and Staff. Our Directors participate in a rigorous education program and actively participate in conferences conducted by the Western Independent Bankers, the National Association of Corporate Directors, the California Bankers Association and various regulatory compliance courses throughout the year. The Bank's Chairman, David Price, is also a member of the WIB Advisory Committee for the Annual Bank Chairman's Forum and a regular participant in the Annual Corporate Governance Conference.

Our Board of Directors and the employees of Fresno First Bank also actively support a number of non-profit organizations throughout the year. These include the American Heart Association, American Red Cross, Community Food Bank, Economic Development Corporation, Habitat for Humanity, H.O.P.E. Animal Foundation, Leukemia & Lymphoma Society, Sierra Foothills Conservancy, Salvation Army and many other local community non-profit organizations.

Fresno First Bank opened for business in December 2005. Now in our seventh year, we are dedicated to the banking needs of businesses, professionals and successful individuals in the Greater Fresno area.

We believe businesses and individuals want the "hands-on, know your customer, relationship" approach, especially when it comes to their money. We've made it our mission to provide a full range of banking services differentiated by an ability to tailor and adjust services quickly to meet needs and opportunities unique to this area.

Achieving that mission is assured because every associate at Fresno First Bank has an ownership stake in the bank. Each has the courage, passion and commitment to create business banking relationships which define a new level of service.

WE SHARE YOUR VALUES

Fresno First Bank has been built on a foundation of core principles that guide everything we do. More than theory, each reflects the real world values of the professionals, businesses and successful individuals we serve.

Passion: *To us, passion is defined as the enthusiasm, energy, courage, ethics and sound judgment that produces positive momentum for our customers. And it's demonstrated daily by everyone at Fresno First Bank.*

Loyalty: *To eliminate the problem of turnover endemic to the bank industry we recruited the best, most experienced professionals and gave each an ownership stake. The result is a banking relationship you can count on for years to come.*

Service: *Fresno First Bank believes 'service' is more than a word. We use it to describe our dedication to taking every opportunity to exceed your expectations of courtesy, professionalism and respect.*

Flexibility: *We understand that businesses can't be successful if they're exactly like their competition. So instead of holding you to rigid criteria, we listen harder and dig deeper to create the best, most adaptable solutions to every need.*

OUR CULTURE

At Fresno First Bank we refer to our team members as "associates" rather than "employees". Why? Because we believe when you appeal to a higher level of thinking, you get a higher level of performance.

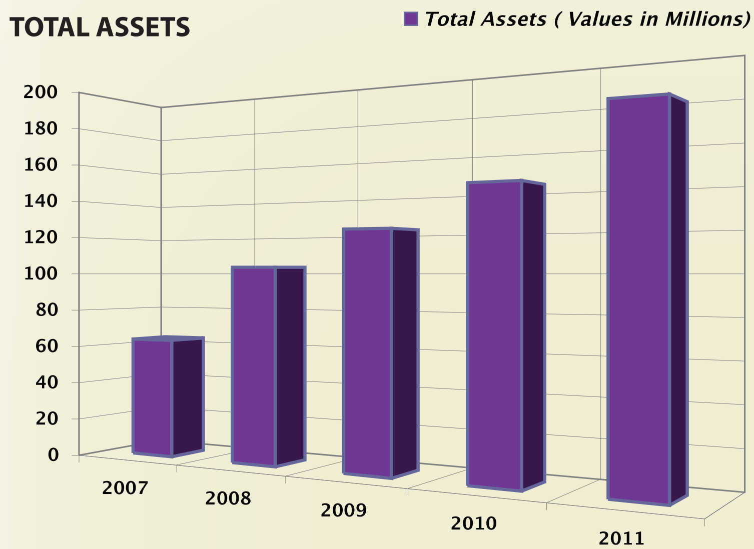
At Fresno First Bank every Associate has an ownership stake in the Bank through our ESOP program and equity compensation plan. In addition, many of our associates regularly invest in Fresno First Bank stock.

In the last three years we have taken these concepts to a higher level by embracing Open-Book Management, employee education and empowerment. So what is Open-Book Management? Better yet, you should understand what "Open-Book" isn't… It's not just sharing numbers. It is more than a promise to be open with employees; it's a process. It's a way to run our company that unleashes the entrepreneur inside every associate; a way to get everyone as informed, involved and engaged as possible to make the company successful.

What has changed through Open-Book Management? Quite simply, responsibility. There is no super-manager who decides how things must be done by everyone else, no finance department guru to watch the performance of every operator and operation to ensure profitability. Those responsibilities are best handled by those who have the most direct impact on them, and who have been taught to make sound business decisions. Now individuals can feel their own importance and contribution to the well-being of the company. Sure we still have a Board of Directors and management team, but now <u>every Associate</u> is accountable to our shareholders because they are shareholders.

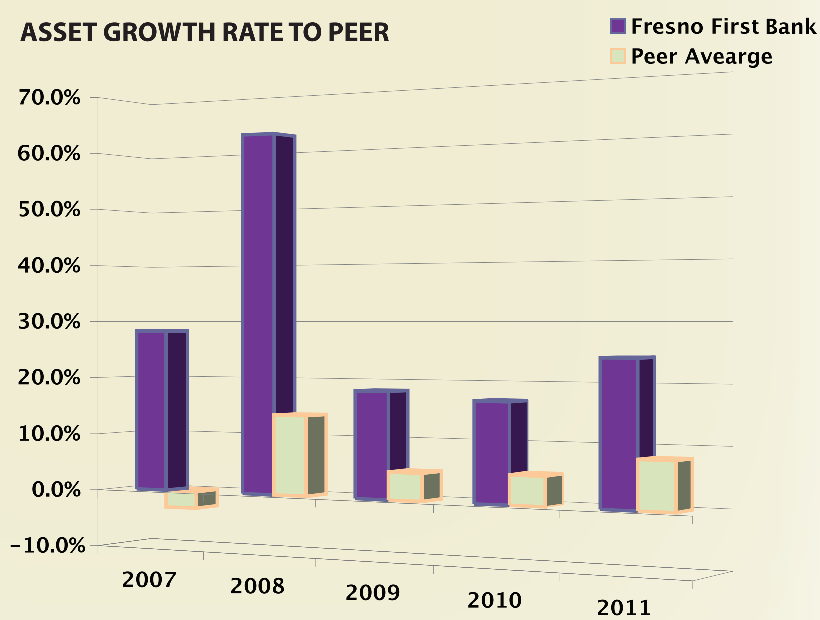
On the following pages you will see highlights of our financial performance over the past several years. We think our culture and our committed Associates, empowered and responsible for performance, have had something to do with our results.

FRESNO FIRST BANK

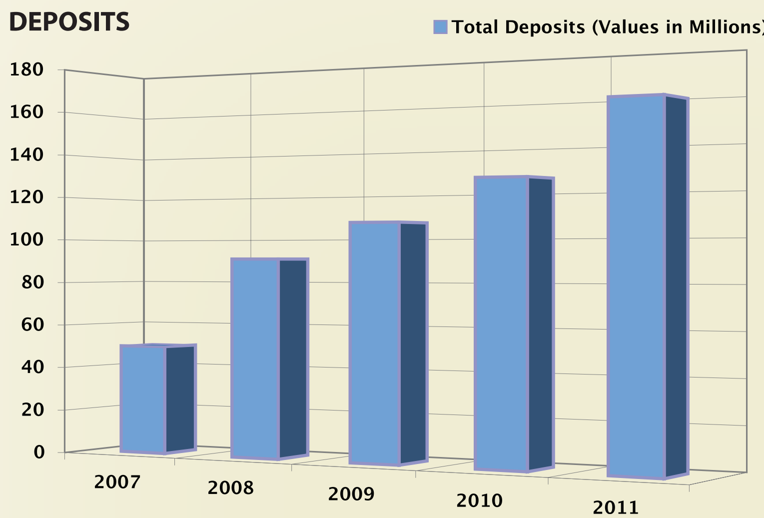


Since 2007, total assets have grown steadily from just over $60 million to more than $177 million at December 31, 2011. As our assets grow so does our ability to generate additional interest income which will increase earnings and shareholder value.

To benchmark our growth compared to similar banks, we use data gathered from regulatory reports filed with the FDIC and provided by SNL Financial. Peer information below consists of data from 31 banks geographically located in markets similar to Fresno First's. These banks range geographically from Bakersfield to Sacramento and from the Central Coast to the Sierra Nevada Mountains. The banks range in size from $91 million to $983 million in total assets with a median size of $185 million. In comparison to the peer group, Fresno First Bank's growth rate has been more than double our peers in each of the last five years. Our ability to grow during one of the worst economic downturns in US history is a testament to our Associates and their ability to offer quality relationship banking that has been well received within our market.

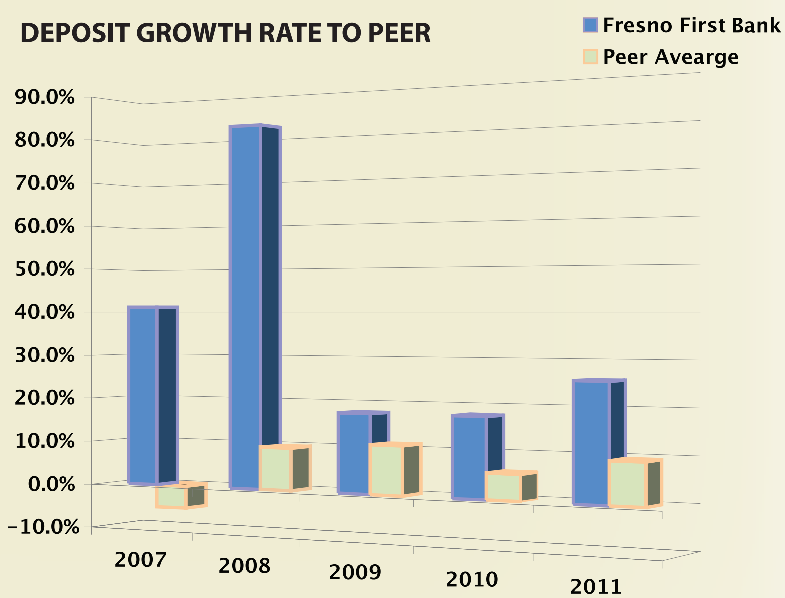


FRESNO FIRST BANK



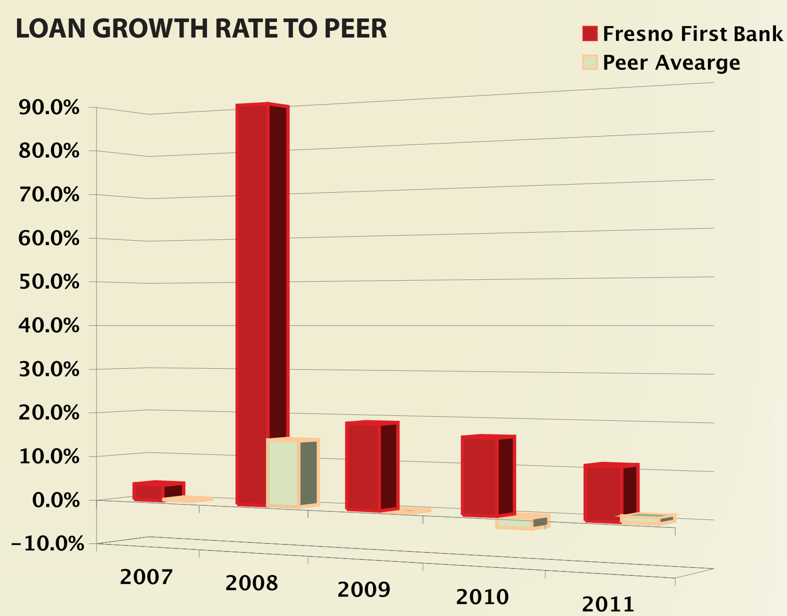
Deposit growth is the catalyst for our growth in assets. Obtaining low cost local core deposits one relationship at a time is what we do every day. Since December 31, 2007, deposits have increased from $50 million to more than $158 million at December 31, 2011.

With more than 30% of our deposits held in zero interest checking accounts, our overall cost of funds is a relatively low .42%. This has allowed our Bank to maintain an interest margin in the top quartile of the industry. Compared to peers we have been able to grow our deposit base at nearly twice the average of peer banks.

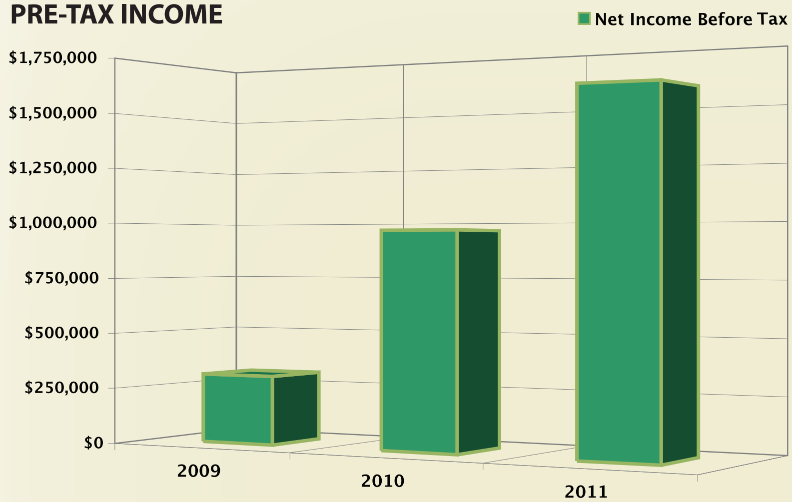


During a time when other banks have ceased to lend and in some cases shrunk their loan portfolios, our loan portfolio has grown from $34 million at December 31, 2007 to more than $100 million today. Our portfolio is well diversified and our credit quality ratios rank Fresno First Bank above peer banks. We pride ourselves in taking a consultative approach with our borrowing customers, tailoring lending solutions to meet client credit needs which will allow their business to flourish.

In comparison to peer banks our growth has far exceeded the average. In three of the last five years our average peer banks total loans outstanding have declined while we have experienced growth each year. During the last four years we have seen "double digit" growth rates.

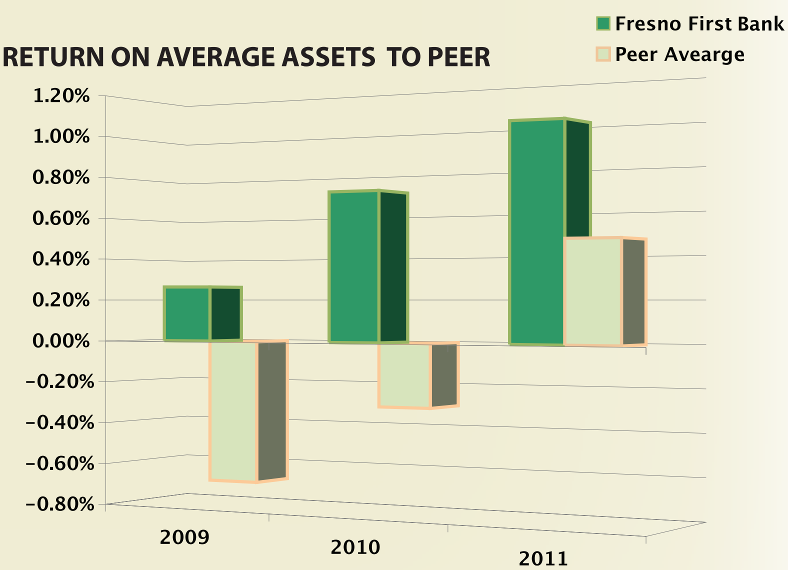


PRE-TAX INCOME



In 2009 we reached profitability and have now recorded three years of increasing profits. The chart at the left displays pre-tax income. In addition to our superior net interest margin we have focused on diversifying the Bank's non-interest income through new initiatives. Over the last two years we have started a government guaranteed lending department, a mortgage department and a merchant services department within the Bank. The goal of these initiatives is to generate non-interest income to enhance the overall profitability of the Bank.

RETURN ON AVERAGE ASSETS TO PEER

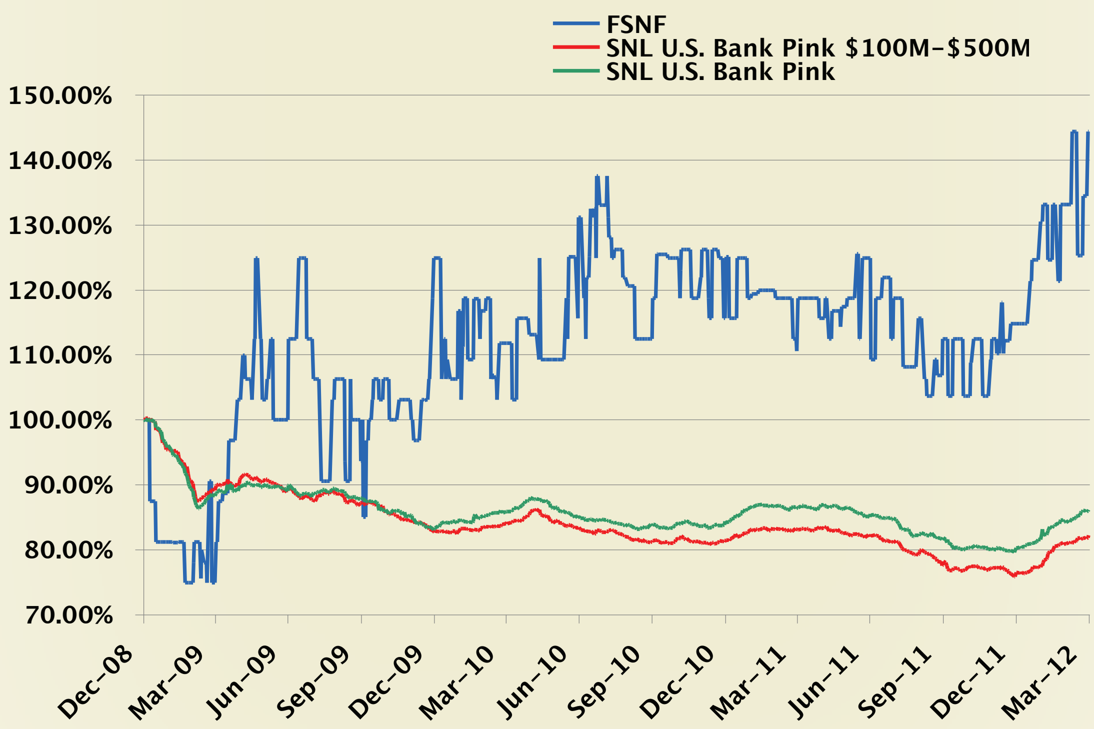


To the right we compare pre-tax return on average assets to the peer bank group. Since 2007 the economic downturn has dramatically affected earnings in the banking industry. As a result, making an apples-to-apples comparison between banks is sometimes difficult. While some banks are in a taxable position, others may be taking tax credits. Because these tax benefits can skew operating performance, we feel pre-tax values present a better apples-to-apples comparison of the value we are creating for our shareholders and make comparison to peer more uniform.

Fresno First Bank's performance compared to industry peers is very positive but Management, the Board and our Associates are seeking even higher financial performance.

Over the last three years many financial stocks have been negatively impacted by the economic downturn. The chart below illustrates the relative performance of Fresno First Bank's stock vs. a broad index of banks of similar size and market.

While past performance is not a guarantee of future results, we would like to think that our positive financial performance has had something to do with our stock's positive performance compared to the market. Our Directors, our Management and our Associates continue to focus on creating long term shareholder value.



Fresno First Bank

Report of Independent Auditors
and Financial Statements

Fresno First Bank

December 31, 2011 and 2010

MOSS-ADAMS LLP

Certified Public Accountants | Business Consultants

Acumen. Agility. Answers.

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MOSS-ADAMS LLP
Certified Public Accountants | Business Consultants

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Shareholders
Fresno First Bank

We have audited the accompanying balance sheets of Fresno First Bank (the Bank) as of December 31, 2011 and 2010, and the related statements of operations, changes in shareholders' equity, and cash flows for the two years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Fresno First Bank as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the two years then ended in conformity with accounting principles generally accepted in the United States of America.

Moss Adams LLP

Stockton, California
March 2, 2012

FRESNO FIRST BANK
BALANCE SHEETS

ASSETS

	DECEMBER 31, 2011	DECEMBER 31, 2010
Cash and due from banks	$ 10,591,802	$ 1,869,053
Federal funds sold	6,070,000	9,185,000
Interest bearing deposits in banks	3,001,970	-
Total cash and cash equivalents	19,663,772	11,054,053
Securities available-for-sale	56,409,131	40,950,119
Loans, net	97,348,521	87,587,993
Federal Home Loan Bank stock, at cost	781,300	636,300
Premises and equipment	600,437	688,622
Interest receivable and other assets	2,892,931	2,190,782
	$ 177,696,092	$ 143,107,869

LIABILITIES AND SHAREHOLDERS' EQUITY

	2011	2010
Deposits	$ 158,774,338	$ 126,106,564
Interest payable and other liabilities	701,084	578,233
Total liabilities	159,475,422	126,684,797
Commitments and contingencies (Notes 4 and 11)		
Shareholders' equity:		
Preferred stock – 5,000,000 shares authorized, $1,000 par value; Series A shares and Series B shares 2,066 issued and outstanding in 2011 and 2010	2,063,278	2,030,611
Common stock – 5,000,000 shares authorized, no par value; 1,766,010 and 1,678,663 shares issued and outstanding in 2011 and 2010, respectively	17,599,944	16,861,096
Additional paid-in capital	1,563,586	1,486,202
Accumulated deficit	(3,405,470)	(4,475,311)
Accumulated other comprehensive income, net	399,332	520,474
Total shareholders' equity	18,220,670	16,423,072
Total liabilities and shareholders' equity	$ 177,696,092	$ 143,107,869

See accompanying notes

	YEARS ENDED DECEMBER 31, 2011	2010
INTEREST INCOME		
Interest and fees on loans	$ 6,260,603	$ 5,692,435
Interest on investment securities	1,094,000	1,113,351
Interest on federal funds sold and other	30,303	22,987
Total interest income	7,384,906	6,828,773
INTEREST EXPENSE		
Interest on savings deposits, NOW, and money market accounts	220,955	262,882
Interest on time deposits	497,229	660,702
Interest on other borrowings	4	-
Total interest expense	718,188	923,584
Net interest income	6,666,718	5,905,189
PROVISION FOR LOAN LOSSES	500,000	1,283,000
Net interest income after provision for loan losses	6,166,718	4,622,189
NON-INTEREST INCOME		
Mortgage fee income	389,321	25,457
Gain on sale of loans	14,827	513,248
Service charges on deposits	319,556	244,728
Loss on sale of other real estate owned	-	(2,982)
Other operating income	64,775	5,474
Total non-interest income	788,479	785,925
NON-INTEREST EXPENSES		
Salaries and employee benefits	2,937,830	2,288,623
Occupancy and equipment expenses	556,974	558,963
Regulatory assessments	279,926	371,008
Data processing fees	347,921	328,898
Professional fees	247,366	181,735
Marketing and business promotion	251,470	145,204
Director fees and stock-based compensation	194,987	91,789
Other expenses	566,551	476,495
	5,383,025	4,442,715
Income before income taxes	1,572,172	965,399
Benefit for income taxes	(344,000)	(555,000)
Net income	$ 1,916,172	$ 1,520,399
Preferred stock dividends and accretion	$ 139,887	$ 139,886
Net income available to common shareholders	$ 1,776,285	$ 1,380,513
Net income per share – basic	$ 1.00	$ 0.78
Net income per share – diluted	$ 1.00	$ 0.78

See accompanying notes

FRESNO FIRST BANK
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Preferred Stock		Common Stock		Additional	Accumulated	Accumulated Other Comprehensive		Total Comprehensive
	Shares	Amount	Shares	Amount	Paid-in Capital	Deficit	Income	Total	Income
Balances, December 31, 2009	2,066	$ 1,997,945	1,674,497	$ 16,819,686	$ 1,390,889	$ (5,855,824)	$ 440,991	$ 14,793,687	
Stock-based compensation	-	-	-	-	95,313	-	-	95,313	
Exercise of stock options	-	-	4,166	41,410	-	-	-	41,410	
Dividend paid on preferred stock	-	-	-	-	-	(107,220)	-	(107,220)	
Accretion of preferred stock	-	32,666	-	-	-	(32,666)	-	-	
Comprehensive income:									
Net income	-	-	-	-	-	1,520,399	-	1,520,399	$ 1,520,399
Other comprehensive income, net of taxes:									
Net unrealized gain on securities available-for-sale, net of tax of $40,945	-	-	-	-	-	-	79,483	79,483	79,483
Total comprehensive income									$ 1,599,882
Balances, December 31, 2010	2,066	2,030,611	1,678,663	16,861,096	1,486,202	(4,475,311)	520,474	16,423,072	
Stock-based compensation	-	-	-	-	77,384	-	-	77,384	
Exercise of stock options	-	-	3,333	33,130	-	-	-	33,130	
Dividend paid on preferred stock	-	-	-	-	-	(107,220)	-	(107,220)	
Accretion of preferred stock	-	32,667	-	-	-	(32,667)	-	-	
Five percent stock dividend	-	-	84,014	705,718	-	(705,718)	-	-	
Cash paid in lieu of fractional shares	-	-	-	-	-	(726)	-	(726)	
Comprehensive income:									
Net income	-	-	-	-	-	1,916,172	-	1,916,172	$ 1,916,172
Other comprehensive income, net of taxes:									
Net unrealized loss on securities available-for-sale, net of tax of $9,380	-	-	-	-	-	-	(121,142)	(121,142)	(121,142)
Total comprehensive income									$ 1,795,030
Balances, December 31, 2011	2,066	$ 2,063,278	1,766,010	$ 17,599,944	$ 1,563,586	$ (3,405,470)	$ 399,332	$ 18,220,670	

See accompanying notes

STATEMENTS OF CASH FLOWS

	YEARS ENDED DECEMBER 31,	
	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 1,916,172	$ 1,520,399
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation and amortization of premises and equipment	182,879	180,682
Amortization and accretion of premiums and discounts on securities available-for-sale, net	253,924	269,956
Provision for loan losses	500,000	1,283,000
Gain on sale of loans	(14,827)	(513,248)
Loss on sale of other real estate owned	-	2,982
Stock-based compensation	77,384	95,313
Increase in deferred taxes	(862,000)	(708,000)
Increase in interest payable and other liabilities	122,851	93,161
Decrease in interest receivable and other assets	150,471	383,632
Net cash from operating activities	2,326,854	2,607,877
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of available-for-sale securities	(49,061,210)	(28,912,750)
Proceeds from maturities of available-for-sale securities	33,236,512	25,513,143
Net increase in loans	(10,245,701)	(12,530,492)
Purchase of Federal Home Loan Bank stock	(145,000)	(194,900)
Proceeds from sale of other real estate owned	-	167,651
Purchases of premises and equipment	(94,694)	(27,407)
Net cash from investing activities	(26,310,093)	(15,984,755)

	YEARS ENDED DECEMBER 31,	
	2011	2010
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in demand deposits and savings accounts	30,091,936	14,358,219
Net increase in time deposits	2,575,838	4,658,326
Cash paid in lieu of fractional shares	(726)	-
Payment of dividends on preferred stock	(107,220)	(107,220)
Common stock issued	33,130	41,410
Net cash from financing activities	32,592,958	18,950,735
NET INCREASE IN CASH AND CASH EQUIVALENTS	8,609,719	5,573,857
CASH AND CASH EQUIVALENTS, beginning of period	11,054,053	5,480,196
CASH AND CASH EQUIVALENTS, end of period	$ 19,663,772	$ 11,054,053
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Interest paid	$ 722,192	$ 955,053
Taxes paid	$ 552,000	$ 69,000

NOTE 1 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of Fresno First Bank (the Bank) conform to generally accepted accounting principles and general practices within the banking industry. A summary of the significant accounting policies applied in the preparation of the accompanying financial statements follows.

Nature of operations – The Bank is incorporated in the state of California and organized as a single operating segment that operates one full-service office in Fresno, California. The Bank's primary source of revenue is providing loans to customers, who are predominately small and middle-market businesses and individuals.

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 and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reported period. Actual results could differ from those estimates.

The allowance for loan losses is the most significant accounting estimate reflected in the Bank's financial statements. The allowance for loan losses includes charges to reduce the recorded balances of loans receivable to their estimated net realizable value, as appropriate. The allowance is based on estimates, and ultimate losses may vary from current estimates. These estimates for losses are based on individual assets and their related cash flow forecasts, sales values, independent appraisals, the volatility of certain real estate markets, and concern for disposing of real estate in distressed markets. Although management of the Bank believes the estimates underlying the calculation of specific allowances are reasonable, there can be no assurances that the Bank could ultimately realize these values. In addition to providing valuation allowances on specific assets where a decline in value has been estimated, the Bank establishes general valuation allowances for losses based on the overall portfolio composition, general market conditions, concentrations, and prior loss experience.

Other significant management judgments and accounting estimates reflected in the Bank's financial statements include:

- Decisions regarding the timing and placement of loans on non-accrual;
- Determination, recognition, and measurement of impaired loans;
- Recognition and measurement of asset servicing rights;
- Determination and evaluation of deferred tax assets and liabilities;
- Determination of the fair value of stock option awards; and
- Determination of the fair value of financial instruments.

NOTE 1 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Concentrations of credit risk – Assets and liabilities that subject the Bank to concentrations of credit risk consist of cash balances at other banks, loans, and deposits. Most of the Bank's customers are located within Fresno County and the surrounding areas. The Bank's primary lending products are discussed in Note 3 to the financial statements. The Bank did not have any significant concentrations in its business with any one customer or industry. The Bank obtains what it believes to be sufficient collateral to secure potential losses on loans. The extent and value of collateral varies based on the details underlying each loan agreement.

As of December 31, 2011 and 2010, the Bank has cash deposits at other financial institutions in excess of FDIC insured limits. However, as the Bank places these deposits with major financial institutions and monitors the financial condition of these institutions, management believes the risk of loss to be minimal. Banking regulations require that banks maintain a percentage of their deposits as reserves in cash or on deposit with the Federal Reserve Bank. The Bank complied with the reserve requirements as of December 31, 2011 and 2010.

Cash and cash equivalents – For purposes of reporting cash flows, cash equivalents include cash, due from banks, interest-bearing deposits in financial institutions with maturities of 90 days or less and federal funds sold. Generally, federal funds are sold for one-day periods and interest-bearing deposits are for periods of ninety days or less.

Securities available-for-sale – Available-for-sale securities consist of U.S. Treasury securities, U.S. Agency securities, obligations of states and political subdivisions, obligations of U.S. Corporations, mortgage-backed securities and other securities not classified as trading securities or held-to-maturity securities. These securities are carried at estimated fair value with unrealized holding gains and losses, net of tax, reported as a separate component of shareholders' equity, accumulated other comprehensive income, until realized. Gains and losses on the sale of available-for-sale securities are determined using the specific identification method. The amortization of premiums and accretion of discounts are recognized as adjustments to interest income using the interest method over the period to call or maturity.

Investments with fair values that are less than amortized cost are considered impaired. Impairment may result from either a decline in the financial condition of the issuing entity or, in the case of fixed interest rate investments, from rising interest rates. At each financial statement date, management assesses each investment to determine if impaired investments are temporarily impaired or if the impairment is other than temporary. This assessment includes a determination of whether the Bank intends to sell the security, or if it is more likely than not that the Bank will be required to sell the security before recovery of its amortized cost basis less any current-period credit losses. For debt securities that are considered other than temporarily impaired and that the Bank does not intend to sell and will not be required to sell prior to recovery of the amortized cost basis, the amount of impairment is separated into the amount that is credit related (credit loss component) and the amount due to all other factors.

The credit loss component is recognized in earnings and is calculated as the difference between the security's amortized cost basis and the present value of its expected future cash flows. The remaining difference between the security's fair value and the present value of the future expected cash flows is deemed to be due to factors that are not credit related and is recognized in other comprehensive income.

NOTE 1 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Loans – Loans are reported at the principal amount outstanding, net of deferred loan fees and costs and the allowance for loan losses. Unearned discounts on installment loans are recognized as income over the terms of the loans. Interest on other loans is calculated by using the simple interest method on the daily balance of the principal amount outstanding.

Loan fees, net of certain direct costs of origination, are deferred and amortized over the contractual term of the loan as an adjustment to the interest yield. During the years ended December 31, 2011 and 2010, salaries and employee benefits expense totaling $49,536 and $66,705, respectively, were deferred as loan origination costs.

Loans on which the accrual of interest has been discontinued are designated as non-accrual loans. Accrual of interest on loans is discontinued either when reasonable doubt exists as to the full and timely collection of interest or principal or when a loan becomes contractually past due by 90 days or more with respect to interest or principal. When a loan is placed on non-accrual status, all interest previously accrued, but not collected, is reversed against current period interest income. Income on such loans is then recognized only to the extent that cash is received and where the future collection of principal is probable. Interest accruals are resumed on such loans only when they are brought fully current with respect to interest and principal and when, in the judgment of management, the loans are estimated to be fully collectible as to both principal and interest.

Allowance for loan losses – The allowance for loan losses is established through a provision for loan losses charged to operations. Loan losses are charged against the allowance for loan losses when management believes that the collectability of the principal is unlikely. Subsequent recoveries of previously charged off amounts, if any, are credited to the allowance.

Management employs a systematic methodology for determining the allowance for loan losses. On a regular basis, management reviews the credit quality of the loan portfolio and considers problem loans, delinquent loans, existing general economic conditions affecting the key lending areas of the Bank, credit quality trends, collateral values, loan volumes and concentrations, seasoning of the loan portfolio, specific industry conditions, recent loss experience, duration of the current business cycle, bank regulatory examination results and findings of the Bank's internal credit examiners. The allowance for loan losses at December 31, 2011 and 2010 reflects management's estimate of probable losses in the portfolio. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific, general, and unallocated components. The specific component relates to loans that are classified as impaired. Impaired loans, as defined, are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent. The general component relates to non-impaired loans and is based on historical loss experience and loss history experienced by the Bank's peers when the Bank did not have losses in a particular loan class, adjusted for qualitative factors impacting the loan portfolio. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

NOTE 1 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Allowance for loan losses (continued) – The Bank considers a loan impaired when it is probable that all amounts of principal and interest due will not be collected according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, current credit worthiness, and the amount of the shortfall in relation to the principal and interest owed.

Federal Home Loan Bank (FHLB) Stock – The Bank is a member of the FHLB system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. FHLB stock is 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.

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 range from three to seven years for computer equipment, equipment, and furniture. 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.

Advertising costs – The Bank expenses the costs of advertising in the period incurred. Advertising expense was $121,449 and $66,000 for the years ended December 31, 2011 and 2010, respectively.

Other real estate owned – Real estate acquired by foreclosure, or deed in lieu of foreclosure is recorded at fair value at the date of foreclosure, establishing a new cost basis by a charge to the allowance for loan losses, if necessary. Fair value is based on current appraisals less estimated selling costs. Any subsequent write-downs are charged against operating expenses and recognized as a valuation allowance. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in other operating expenses.

NOTE 1 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income taxes – The Bank uses the asset and liability method to account for income taxes. Under such method, deferred tax assets and liabilities are recognized for the future tax consequences of differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis (temporary differences). Deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes in the period of enactment.

A valuation allowance against net deferred tax assets is established to the extent that it is more likely than not that the benefits associated with the deferred tax assets will not be fully realized.

In accordance with accounting standards, the Bank has assessed its tax positions and has concluded there are no unrecognized tax benefits at December 31, 2011 and 2010.

The Bank recognizes interest accrued and penalties related to unrecognized tax benefits in tax expense. During the years ended December 31, 2011 and 2010, the Bank recognized no interest and penalties.

The Bank files income tax returns in the U.S. federal jurisdiction and with the state of California. The Bank is subject to U.S. federal or state income tax examinations by tax authorities for years beginning 2007.

Comprehensive income – Changes in unrealized gains and losses on available-for-sale securities are the only component of accumulated other comprehensive income for the Bank.

Fair value measurement – Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Current accounting guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of inputs that may be used to measure fair value:

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

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

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

See Note 14 for more information and disclosures relating to the Bank's fair value measurements.

NOTE 1 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial instruments – In the ordinary course of business, the Bank 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 15. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received.

Earnings per share (EPS) – Basic EPS excludes dilution and is computed by dividing income available to common stockholders 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, such as stock options, 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 treasury stock method is applied to determine the dilutive effect of stock options when computing diluted earnings per share.

Stock-based compensation – The Bank recognizes the cost of employee services received in exchange for awards of stock options, or other equity instruments, based on the grant-date fair value of those awards. This cost is recognized over the period which an employee is required to provide services in exchange for the award, generally the vesting period. See Note 12 for additional information on the Bank's stock option plan.

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

Servicing rights – The Bank sells or transfers loans, including the guaranteed portion of United States Department of Agriculture (USDA) loans (with servicing retained) for cash proceeds equal to the principal amount of loans, as adjusted to yield interest to the investor based upon the current market rates. The Bank records an asset representing the right to service a loan for others when it sells a loan and retains the servicing rights. The carrying value of the loan is allocated between the loan and the servicing rights, based on their relative fair values. The fair value of servicing rights is estimated by discounting estimated future cash flows from servicing using discount rates that approximate current market rates and using estimated prepayment rates.

The servicing rights are initially measured at fair value and amortized in proportion to and over the period of the estimated net servicing income assuming prepayments. Additionally, management assesses the servicing rights for impairment as of each financial reporting date. For purposes of evaluating and measuring impairment, servicing rights are based on a discounted cash flow methodology, current prepayment speeds and market discount rates. Any impairment is measured as the amount by which the carrying value of servicing rights for a stratum exceeds its fair value. The carrying value of servicing rights at December 31, 2011 and 2010 were $50,311 and $56,535, respectively. No impairment charges were recorded for the years ended December 31, 2011 or 2010 related to servicing assets.

NOTE 1 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Reclassifications – Certain reclassifications have been made to the 2010 financial statements to conform to the classifications used in 2011.

Adoption of new accounting standards – In June 2011, the FASB issued ASU No. 2011-05, *Comprehensive Income* (Topic 220) *Presentation of Comprehensive Income*. The ASU improves the comparability, consistency, and transparency of financial reporting and increases the prominence of items reported in other comprehensive income. The amendments to Topic 220, Comprehensive Income, require entities to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. Entities are no longer permitted to present components of other comprehensive income as part of the statement of changes in stockholders' equity. Any adjustments for items that are reclassified from other comprehensive income to net income are to be presented on the face of the entities' financial statement regardless of the method of presentation for comprehensive income. The amendments do not change items to be reported in comprehensive income or when an item of other comprehensive income must be reclassified to net income, nor do the amendments change the option to present the components of other comprehensive income either net of related tax effects or before related tax effects. ASU 2011-05 is effective for fiscal years, and interim periods beginning on or after December 15, 2011. In December 2011, the FASB issued ASU No. 2011-12, *Comprehensive Income* (Topic 220) *Presentation of Comprehensive Income* to effectively defer only those changes in Update 2011-05 that relate to the presentation of reclassification adjustments out of accumulated other comprehensive income. The amendments will be temporary to allow the Board time to redeliberate the presentation requirements for reclassifications out of accumulated other comprehensive income for annual and interim financial statements for public, private, and non-profit entities. The amendments in this ASU are effective at the same time as the amendments in ASU 2011-05 so that entities will not be required to comply with the presentation requirements in ASU 2011-05 that this ASU is deferring. We do not expect this ASU to have an impact on our financial condition or results of operations as it affects presentation only.

In May 2011, the FASB issued ASU No. 2011-04, *Fair Value Measurement* (Topic 820) *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. The ASU improves the comparability of fair value measurements presented and disclosed in accordance with U.S. generally accepted accounting principles ("GAAP") and International Financial Reporting Standards ("IFRS"s) by changing the wording used to describe many of the requirements in U.S GAAP for measuring fair value and disclosure of information. The amendments to this ASU provide explanations on how to measure fair value but do not require any additional fair value measurements and do not establish valuation standards or affect valuation practices outside of financial reporting. The amendments clarify existing fair value measurements and disclosure requirements to include application of the highest and best use and valuation premises concepts; measuring fair value of an instrument classified in a reporting entity's shareholders' equity; and disclosure requirements regarding quantitative information about unobservable inputs categorized within Level 3 of the fair value hierarchy. In addition, clarification is provided for measuring the fair value of financial instruments that are managed in a portfolio and the application of premiums and discounts in a fair value measurement. For non-public entities, ASU 2011-04 is effective for annual periods beginning after December 15, 2011. We do not expect this ASU to have a significant impact on our financial condition or results of operations.

NOTE 1 –SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Adoption of new accounting standards (continued) – In April 2011, the FASB issued ASU No. 2011-02, *Receivables* (Topic 310): *A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring*. The ASU clarifies which loan modifications constitute troubled debt restructurings. It is intended to assist creditors in determining whether a modification of the terms of a receivable meets the criteria to be considered a troubled debt restructuring ("TDR"), both for purposes of recording an impairment loss and for disclosure of a TDR. In evaluating whether a restructuring constitutes a TDR, a creditor must separately conclude that both of the following exist: (a) the restructuring constitutes a concession; and (b) the debtor is experiencing financial difficulties. The amendments to ASU Topic 310, Receivables, clarify the guidance on a creditor's evaluation of whether it has granted a concession and whether a debtor is experiencing financial difficulties. ASU No. 2011-02 is effective for interim and annual periods beginning on or after June 15, 2011, and applies retrospectively to restructurings occurring on or after the beginning of the fiscal year of adoption. We have adopted this ASU and provided the applicable disclosure in Note 3 herein.

NOTE 2 – INVESTMENT SECURITIES

The amortized cost and estimated fair values of securities available-for-sale are as follows:

	2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale:				
U.S. government and agency securities	$ 43,692,819	$ 627,822	$ (16,151)	$ 44,304,490
Mortgage-backed securities	8,463,114	279,936	(104)	8,742,946
State and municipal agencies	1,097,560	-	(2,314)	1,095,246
Corporate debt securities	2,478,803	-	(212,354)	2,266,449
	$ 55,732,296	$ 907,758	$ (230,923)	$ 56,409,131

	2010			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale:				
U.S. government and agency securities	$ 29,755,275	$ 564,513	$ (52,096)	$ 30,267,692
Mortgage-backed securities	7,959,512	323,520	(72,346)	8,210,686
Corporate debt securities	2,446,735	32,669	(7,663)	2,471,741
	$ 40,161,522	$ 920,702	$ (132,105)	$ 40,950,119

The amortized cost and estimated fair value of all investment securities as of December 31, 2011 by expected maturities are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 132,900	$ 133,335
Due after one year to five years	3,221,472	3,106,483
Due from five to ten years	11,522,452	11,657,885
Due after ten years	40,855,472	41,511,428
	$ 55,732,296	$ 56,409,131

NOTE 2 – INVESTMENT SECURITIES (CONTINUED)

The gross unrealized loss and related estimated fair value of investment securities that have been in a continuous loss position for less than twelve months and over twelve months are as follows:

	2011					
	Less than 12 months		Over Twelve Months		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. government and agency securities	$ 10,771,367	$ (16,151)	$ -	$ -	$ 10,771,367	$ (16,151)
Mortgage-backed securities	46,521	(104)	-	-	46,521	(104)
State and municipal agencies	1,095,245	(2,314)	-	-	1,095,245	(2,314)
Corporate debt securities	2,266,449	(212,354)	-	-	2,266,449	(212,354)
	$ 14,179,582	$ (230,923)	$ -	$ -	$ 14,179,582	$ (230,923)

	2010					
	Less than 12 months		Over Twelve Months		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. government and agency securities	$ 4,997,410	$ (50,644)	$ 626,371	$ (1,452)	$ 5,623,781	$ (52,096)
Mortgage-backed securities	1,165,201	(72,346)	-	-	1,165,201	(72,346)
Corporate debt securities	447,750	(7,663)	-	-	447,750	(7,663)
	$ 6,610,361	$ (130,653)	$ 626,371	$ (1,452)	$ 7,236,732	$ (132,105)

Certain investment securities shown in the previous table currently have fair values less than amortized cost and therefore contain unrealized losses. The Bank considers a number of factors including, but not limited to: (a) the length of time and the extent to which the fair value has been less than the amortized cost, (b) the financial condition and near-term prospects of the issuer, (c) the intent and ability of the Bank to retain its investment for a period of time sufficient to allow for an anticipated recovery in value, (d) whether the debtor is current on interest and principal payments, and (e) general market conditions and the industry- or sector-specific outlook. Management has evaluated all securities at December 31, 2011 and 2010, and has determined that no securities are other than temporarily impaired.

NOTE 2 – INVESTMENT SECURITIES (CONTINUED)

The Bank does not have the intent to sell the investments that are impaired, and it is more likely than not that the Bank will not be required to sell those investments before recovery of the amortized cost basis. The Bank has evaluated these securities and has determined that the decline in value is temporary and is related to the change in market interest rates since purchase. The decline in value is not related to any issuer- or industry-specific event. These temporary unrealized losses relate principally to current interest rates for similar types of securities. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. At December 31, 2011, there were twenty investment securities with unrealized losses. The Bank anticipates full recovery of amortized cost with respect to these securities at maturity or sooner in the event of a more favorable market interest rate environment.

During 2011 and 2010, the Bank did not sell investment securities.

Investment securities carried at approximately $2,055,000 and $4,586,000 at December 31, 2011 and 2010, respectively, were pledged to secure public deposits or other purposes as permitted or required by law.

NOTE 3 – LOANS

Major classifications of loans are as follows:

	DECEMBER 31,	
	2011	2010
Commercial and industrial	$ 31,624,476	$ 25,770,488
Commercial real estate	36,021,259	36,525,936
Land and construction	8,389,230	7,087,852
Residential real estate	14,360,561	13,606,512
Agriculture	9,560,586	6,442,728
Consumer	436,656	833,683
	100,392,768	90,267,199
Allowance for loan losses	(2,792,619)	(2,379,121)
Deferred loan fees and costs, net	(251,628)	(300,085)
	$ 97,348,521	$ 87,587,993

NOTE 3 – LOANS (CONTINUED)

The Bank's loan portfolio consists primarily of loans to borrowers within Fresno County, 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.

All of the Bank's loans are underwritten after evaluating the borrower's character and, for commercial and business loans, managerial and operational experience. Underwriting standards are designed to promote relationship banking rather than transactional banking.

Commercial and industrial loans are primarily made to commercial and business entities for working capital, equipment purchases, growth and expansion, and any other permissible purposes. The Bank's management examines current and projected cash flows to determine the ability of the borrower to repay its obligations as agreed. Commercial loans are primarily made based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets such as equipment, accounts receivable or inventory and may incorporate personal guarantees or personal assets as collateral; however, some loans may be made on an unsecured basis.

Commercial real estate loans are primarily made to owner-users of the property or investors with current tenants in the property. The Bank does not originate speculative commercial real estate loans where cash flow and repayment is dependent on the eventual lease or sale of the subject property without identified prospects. Commercial real estate loans are subject to underwriting standards and processes similar to commercial loans. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally largely dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. The properties securing the Bank's commercial real estate portfolio are diverse in terms of type and industries operating within the properties. This diversity helps reduce the Bank's exposure to adverse economic events that affect any single market or industry. Management monitors and evaluates commercial real estate loans based on collateral type, geography, industry, and risk grade criteria.

Land and construction loans are primarily made to borrowers who are using the property for their own purposes. The Bank does not make speculative land loans where repayment will be from the eventual sale of the property to unknown parties. Land loans are made with amortizing repayment terms to borrowers with proven, historic cash flow sufficient to repay the loan. Collateral values are based on the current "as is" market value of the property. Construction loans are made based on the borrower's historic and projected cash flow. The Bank does not engage in speculative construction loans where repayment will come from the sale or lease of the property to unknown parties.

NOTE 3 – LOANS (CONTINUED)

Residential real estate loans are made to individuals for the purchase or refinance of residential 1-to-4 family properties, or for other consumer purposes. Residential real estate loans are underwritten based upon income, credit history, and collateral. The Bank does not generate residential real estate loans for sale. To monitor and manage residential loan risk, policies and procedures are developed and modified, as needed. Underwriting standards for home loans are heavily influenced by statutory requirements, which include, but are not limited to, a determination and verification of borrower's ability to repay the loan, maximum loan-to-value percentage, collection remedies, and documentation requirements.

Agricultural loans are primarily made to producers of agricultural products. Agricultural loans are subject to underwriting standards and processes similar to commercial loans. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate and/or agricultural commodities. Agricultural real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally largely dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Agricultural crop loans may be more adversely affected by conditions in the weather or in the general economy. The properties securing the Bank's agricultural portfolio are diverse in terms of type of crop. This diversity helps reduce the Bank's exposure to adverse economic events that affect any single commodity. Management monitors and evaluates agricultural real estate loans based on collateral, crop type, geography, and risk grade criteria.

Consumer loans are made to individuals for personal, household, and family expenditures and consist of term loans and lines of credit. The Bank does not offer credit card plans. Consumer loans are subject to underwriting standards and processes similar to residential real estate loans and are based primarily on income, credit history and collateral; however, some consumer loans are unsecured. To monitor and manage consumer loan risk, policies and procedures are developed and modified, as needed. This activity coupled with relatively small loan amounts that are spread across many individual borrowers minimizes risk.

The Bank utilizes an independent third party loan review consultant to review and validate the credit risk program on a periodic basis. Results of these reviews are presented to management and the Bank's Board of Directors. The loan review process complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel, as well as the Bank's policies and procedures.

NOTE 3 – LOANS (CONTINUED)

Information related to impaired loans as of December 31, 2011 and for the year ended consisted of the following:

	Commercial and Industrial	Commercial Real Estate	Land and Construction	Residential Real Estate	Agriculture	Consumer	Total
Recorded Investment in impaired loans:							
With no specific allowance recorded	$ -	$ -	$ -	$ 90,323	$ -	$ -	$ 90,323
With a specific allowance recorded	-	2,026,462	2,561,418	294,848	-	-	4,882,728
Total recorded investment in impaired loans	$ -	$ 2,026,462	$ 2,561,418	$ 385,171	$ -	$ -	$ 4,973,051
Unpaid principal balance of impaired loans:							
With no specific allowance recorded	$ -	$ -	$ -	$ 90,323	$ -	$ -	$ 90,323
With a specific allowance recorded	-	2,026,462	2,561,418	294,848	-	-	4,882,728
Total unpaid principal balance of impaired loans	$ -	$ 2,026,462	$ 2,561,418	$ 385,171	$ -	$ -	$ 4,973,051
Specific allowance	$ -	$ 434,597	$ 47,494	$ 75,248	$ -	$ -	$ 557,339
Average recorded investment in impaired loans during the year	-	2,351,021	1,286,563	392,273	237,826	-	4,267,683
Interest income recognized on impaired loans during the year	-	42,252	140,110	11,023	23,988	-	217,373

Information related to impaired loans as of December 31, 2010 and for the year ended consisted of the following:

	Commercial and Industrial	Commercial Real Estate	Land and Construction	Residential Real Estate	Agriculture	Consumer	Total
Recorded Investment in impaired loans:							
With no specific allowance recorded	$ -	$ -	$ -	$ -	$ -	$ -	$ -
With a specific allowance recorded	-	2,556,102	627,076	1,168,940	476,719	-	4,828,837
Total recorded investment in impaired loans	$ -	$ 2,556,102	$ 627,076	$ 1,168,940	$ 476,719	$ -	$ 4,828,837
Unpaid principal balance of impaired loans:							
With no specific allowance recorded	$ -	$ -	$ -	$ -	$ -	$ -	$ -
With a specific allowance recorded	-	2,556,102	627,076	1,168,940	476,719	-	4,828,837
Total unpaid principal balance of impaired loans	$ -	$ 2,556,102	$ 627,076	$ 1,168,940	$ 476,719	$ -	$ 4,828,837
Specific allowance	$ -	$ 96,905	$ 1,411	$ 80,038	$ 19,501	$ -	$ 197,855
Average recorded investment in impaired loans during the year	-	639,025	444,455	1,093,785	477,702	-	2,654,967
Interest income recognized on impaired loans during the year	-	46,547	11,916	70,955	24,232	-	153,650

NOTE 3 – LOANS (CONTINUED)

The Bank has established a loan risk rating system to measure and monitor the quality of the loan portfolio. All loans are assigned a risk rating from the inception of the loan until the loan is paid off. The primary loan grades are as follows:

Loans rated Pass – These are loans to borrowers with satisfactory financial support, repayment capacity and credit strength. Borrowers in this category demonstrate fundamentally sound financial positions, repayment capacity, credit history and management expertise. Loans in this category must have an identifiable and stable source of repayment and meet the Bank's policy regarding debt service coverage ratios. These borrowers are capable of sustaining normal economic, market or operational setbacks without significant financial impacts. Financial ratios and trends are acceptable. Negative external industry factors are generally not present. The loan may be secured, unsecured or supported by non-real estate collateral for which the value is more difficult to determine and/or marketability is more uncertain. These loans carry a normal degree of risk. The borrowers have the capacity to perform according to terms; any deviation from historic performance is limited and temporary.

Loans rated Special Mention – These are loans that have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the Bank's credit position at some future date. Special Mention assets are not adversely classified and do not expose the Bank to sufficient risk to warrant adverse classification. These loans exhibit a more weakened condition than Pass loans but not to the degree where they would be considered substandard. These loans show definite signs of deterioration or weakness, and the likelihood of correction is somewhat questionable. Weaknesses might include significant earnings decline, collection of accounts receivable is slowing, delayed accounts payable, greater dependency on-line usage, covenants not being met, and/or waived for short periods.

Loans rated Substandard – These are loans that are inadequately protected by the current sound worth and paying capacity of the borrower or by the collateral pledged, if any. These loans have a well-defined weakness, or weaknesses that jeopardize the liquidation of the loan. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Loans rated Doubtful – These are loans that have all the weaknesses inherent in a loan classified as substandard with the added characteristic that the weaknesses makes the collection or liquidation in full, on the basis of currently known facts, conditions, and values, highly questionable and improbable. These loans have a high probability of loss due to significant deterioration in financial condition of the borrower and collateral value pledged, if any. The borrower is unable to demonstrate the ability to strengthen their financial condition within a reasonable time; therefore, close supervision is required and the loan is placed on non-accrual. The risk of loss is measured by an impairment analysis; any loss exposure determined through this analysis is to be charged-off.

NOTE 3 – LOANS (CONTINUED)

The following table summarizes the loan portfolio by credit quality and product and/or collateral type as of December 31, 2011:

	Pass	Special Mention	Substandard	Doubtful	Total
Grade:					
Commercial and industrial	$ 28,842,637	$ 194,000	$ 2,587,839	$ -	$ 31,624,476
Commercial real estate	29,761,942	3,448,964	2,810,353	-	36,021,259
Land and construction	5,797,670	-	2,591,560	-	8,389,230
Residential real estate	13,627,890	-	732,671	-	14,360,561
Agriculture	9,560,586	-	-	-	9,560,586
Consumer	436,656	-	-	-	436,656
	$ 88,027,381	$ 3,642,964	$ 8,722,423	$ -	$ 100,392,768

The following table summarizes the loan portfolio by credit quality and product and/or collateral type as of December 31, 2010:

	Pass	Special Mention	Substandard	Doubtful	Total
Grade:					
Commercial and industrial	$ 20,952,607	$ 2,847,807	$ 1,970,074	$ -	$ 25,770,488
Commercial real estate	32,137,144	-	4,388,792	-	36,525,936
Land and construction	4,421,908	1,996,418	669,526	-	7,087,852
Residential real estate	12,085,034	-	1,521,478	-	13,606,512
Agriculture	5,966,009	-	476,719	-	6,442,728
Consumer	833,683	-	-	-	833,683
	$ 76,396,385	$ 4,844,225	$ 9,026,589	$ -	$ 90,267,199

NOTE 3 – LOANS (CONTINUED)

The following table is an aging analysis of loans, segregated by class of loans, as of December 31, 2011:

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Recorded Investment > 90 Days and Accruing
Commercial and industrial	$ 43,740	$ -	$ -	$ 43,740	$ 31,580,736	$ 31,624,476	$ -
Commercial real estate	-	795,299	-	795,299	35,225,960	36,021,259	-
Land and construction	30,142	-	-	30,142	8,359,088	8,389,230	-
Residential real estate	-	-	-	-	14,360,561	14,360,561	-
Agriculture	-	-	-	-	9,560,586	9,560,586	-
Consumer	-	-	-	-	436,656	436,656	-
Total	$ 73,882	$ 795,299	$ -	$ 869,181	$ 99,523,587	$ 100,392,768	$ -

The following table is an aging analysis of loans, segregated by class of loans, as of December 31, 2010:

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Recorded Investment > 90 Days and Accruing
Commercial and industrial	$ -	$ -	$ -	$ -	$ 25,770,488	$ 25,770,488	$ -
Commercial real estate	-	-	-	-	36,525,936	36,525,936	-
Land and construction	-	-	-	-	7,087,852	7,087,852	-
Residential real estate	-	-	-	-	13,606,512	13,606,512	-
Agriculture	-	-	-	-	6,442,728	6,442,728	-
Consumer	-	-	-	-	833,683	833,683	-
Total	$ -	$ -	$ -	$ -	$ 90,267,199	$ 90,267,199	$ -

NOTE 3 – LOANS (CONTINUED)

The following table summarizes loans to customers whose loan terms were modified in troubled debt restructurings:

	Year ended December 31, 2011		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings			
Commercial and industrial	-	$ -	$ -
Commercial real estate	-	-	-
Land and construction	2	2,105,388	2,105,388
Residential real estate	-	-	-
Agriculture	-	-	-
Consumer	-	-	-
	2	$ 2,105,388	$ 2,105,388

	Year ended December 31, 2010		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings			
Commercial and industrial	-	$ -	$ -
Commercial real estate	2	2,587,094	2,587,094
Land and construction	-	-	-
Residential real estate	1	122,275	105,999
Agriculture	-	-	-
Consumer	-	-	-
	3	$ 2,709,369	$ 2,693,093

The loans outlined above are considered troubled debt restructuring because the Bank granted a concession to a borrower experiencing financial difficulties that it would not otherwise consider. During 2011, there were two loans to one borrower that were modified and considered troubled debt restructurings because specific interest rate concessions were granted to the borrower. During 2010, there were three loans modified and considered troubled debt restructurings because specific interest rate concessions were granted to the borrowers.

NOTE 3 – LOANS (CONTINUED)

Year-end non-accrual loans, segregated by class, are as follows:

	DECEMBER 31, 2011	DECEMBER 31, 2010
Commercial and industrial	$ -	$ -
Commercial real estate	795,299	-
Land and construction	-	-
Residential real estate	90,323	105,999
Agriculture	-	-
Consumer	-	-
	$ 885,622	$ 105,999

NOTE 3 – LOANS (CONTINUED)

The following table summarizes the Bank's allowance for loan losses for the year ended December 31, 2011 by loan product and collateral type:

	Commercial and Industrial	Commercial Real Estate	Land and Construction	Residential Real Estate	Agriculture	Consumer	Unallocated	Total
Allowance for loan losses:								
Beginning balance	$ 615,005	$ 830,346	$ 296,611	$ 281,281	$ 59,983	$ 13,393	$ 282,502	$ 2,379,121
Charge-offs	(86,902)	-	-	-	-	-	-	(86,902)
Recoveries	400	-	-	-	-	-	-	400
Provision	614,046	(58,940)	(120,957)	(38,583)	11,276	(11,785)	104,943	500,000
Ending balance	$ 1,142,549	$ 771,406	$ 175,654	$ 242,698	$ 71,259	$ 1,608	$ 387,445	$ 2,792,619
Period-end amount allocated to:								
Loans individually evaluated for impairment	$ -	$ 434,597	$ 47,494	$ 75,248	$ -	$ -	$ -	$ 557,339
Loans collectively evaluated for impairment	1,142,549	336,809	128,160	167,450	71,259	1,608	387,445	2,235,280
Ending balance	$ 1,142,549	$ 771,406	$ 175,654	$ 242,698	$ 71,259	$ 1,608	$ 387,445	$ 2,792,619
Loans:								
Individually evaluated for impairment	$ -	$ 2,026,462	$ 2,561,418	$ 385,171	$ -	$ -		$ 4,973,051
Collectively evaluated for impairment	31,624,476	33,994,797	5,827,812	13,975,390	9,560,586	436,656		95,419,717
Ending balance	$ 31,624,476	$ 36,021,259	$ 8,389,230	$ 14,360,561	$ 9,560,586	$ 436,656		$ 100,392,768

NOTE 3 – LOANS (CONTINUED)

The following table summarizes the Bank's allowance for loan losses for the year ended December 31, 2010 by loan product and collateral type:

	Commercial and Industrial	Commercial Real Estate	Land and Construction	Residential Real Estate	Agriculture	Consumer	Unallocated	Total
Allowance for loan losses:								
Beginning balance	$ 525,636	$ 191,089	$ 431,057	$ 182,085	$ 84,136	$ 25,138	$ 6,647	$ 1,445,788
Charge-offs	(413,576)	-	(6,500)	-	-	-	-	(420,076)
Recoveries	32,121	-	38,288	-	-	-	-	70,409
Provision	470,824	639,257	(166,234)	99,196	(24,153)	(11,745)	275,855	1,283,000
Ending balance	$ 615,005	$ 830,346	$ 296,611	$ 281,281	$ 59,983	$ 13,393	$ 282,502	$ 2,379,121
Period-end amount allocated to:								
Loans individually evaluated for impairment	$ -	$ 96,905	$ 1,411	$ 80,038	$ 19,501	$ -	$ -	$ 197,855
Loans collectively evaluated for impairment	615,005	733,441	295,200	201,243	40,482	13,393	282,502	2,181,266
Ending balance	$ 615,005	$ 830,346	$ 296,611	$ 281,281	$ 59,983	$ 13,393	$ 282,502	$ 2,379,121
Loans:								
Individually evaluated for impairment	$ -	$ 2,556,102	$ 627,076	$ 1,168,940	$ 476,719	$ -		$ 4,828,837
Collectively evaluated for impairment	25,770,488	33,969,834	6,460,776	12,437,572	5,966,009	833,683		85,438,362
Ending balance	$ 25,770,488	$ 36,525,936	$ 7,087,852	$ 13,606,512	$ 6,442,728	$ 833,683		$ 90,267,199

NOTE 4 – PREMISES AND EQUIPMENT

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

	DECEMBER 31,	
	2011	2010
Leasehold improvements	$ 1,123,897	$ 1,123,897
Furniture, fixtures, and equipment	469,958	467,489
Computer equipment	555,726	463,501
	2,149,581	2,054,887
Less accumulated depreciation and amortization	(1,549,144)	(1,366,265)
	$ 600,437	$ 688,622

The Bank has entered into a ten-year lease for its main banking office and administrative offices. The Bank is responsible for common area maintenance, taxes, and insurance to the extent they exceed the base year amounts. The lease expires on January 31, 2016.

At December 31, 2011, the future lease rental payable under noncancellable operating lease commitments for the Banks' main office and administrative offices were as follows:

2012	$ 303,676
2013	303,676
2014	312,028
2015	321,388
2016	26,848
Thereafter	-
	$ 1,267,616

The minimum rental payments shown above are given for the existing lease obligations and are not a forecast of future rental expense. Total rental expense was approximately $301,000 and $310,000 for the years ended December 31, 2011 and 2010, respectively.

NOTE 5 – DEPOSITS

Customer deposits were as follows:

	DECEMBER 31, 2011	DECEMBER 31, 2010
Non-interest-bearing demand	$ 48,155,031	$ 31,597,639
Savings, NOW, and money market accounts	62,427,469	48,892,925
Time deposits under $100,000	15,484,463	18,394,407
Time deposits $100,000 and over	32,707,375	27,221,593
	$ 158,774,338	$ 126,106,564

At December 31, 2011, the scheduled maturities of time deposits are as follows:

2012	$ 41,578,391
2013	4,049,353
2014	1,022,167
2015	1,309,853
2016 and beyond	232,074
	$ 48,191,838

NOTE 6 – BORROWING ARRANGEMENTS

The Bank may borrow up to $10,000,000 overnight on an unsecured basis from three correspondent banks. The Bank may also borrow up to approximately $24,571,000 from the Federal Home Loan Bank of San Francisco, subject to providing collateral and fulfilling other conditions of the credit facility. The Bank has pledged investment securities of approximately $2,055,000 for the credit facility at Federal Home Loan Bank. The Bank may also borrow from the Federal Reserve Bank of San Francisco, subject to fulfilling other conditions of the credit facility and providing collateral. As of December 2011 and 2010, no amounts were outstanding under these arrangements.

NOTE 7 – EMPLOYEE BENEFITS

The Bank sponsors an employee stock ownership plan (ESOP) for eligible employees. Eligibility begins after an employee has attained the age of 21 and completed one year of service, as defined in the ESOP documents. Under the ESOP, the Bank contributes a discretionary amount to the ESOP for the purchase of the Bank's stock, to be held in trust for each participant to later be distributed in accordance with the ESOP. For the years ended December 31, 2011 and 2010, contributions to the ESOP were $150,000 and $99,996, respectively.

The Bank sponsors a 401(k) plan for the benefit of its employees. The Bank can match employee contributions and make additional contributions as determined by the Board of Directors annually. The Bank made no contributions for the years ended December 31, 2011 and 2010.

NOTE 8 – INCOME TAXES

The benefit for income taxes for the years ended December 31, consists of the following:

	2011	2010
Current		
Federal	$ 358,000	$ -
State	151,000	112,000
	509,000	112,000
Deferred		
Federal	(729,000)	(411,000)
State	(124,000)	(256,000)
	(853,000)	(667,000)
	$ (344,000)	$ (555,000)

Deferred taxes are a result of differences between income tax accounting and generally accepted accounting principles with respect to income and expense recognition.

NOTE 8 – INCOME TAXES (CONTINUED)

The following is a summary of the components of the net deferred tax asset accounts recognized in the accompanying statements of financial condition at December 31:

	2011	2010
Deferred tax assets:		
Pre-operating expenses	$ 154,000	$ 171,000
Depreciation differences	170,000	159,000
Allowance for loan losses due to tax limitations	1,008,000	820,000
Stock-based compensation	274,000	286,000
Operating loss carryforwards	383,000	748,000
Other	135,000	142,000
	2,124,000	2,326,000
Deferred tax liabilities:		
Accrual to cash	(104,000)	(155,000)
Unrealized gains on available-for-sale securities	(278,000)	(324,000)
Other	(62,000)	(91,000)
	(444,000)	(570,000)
Valuation allowance	(66,000)	(995,000)
Net deferred income tax asset	$ 1,614,000	$ 761,000

As of December 31, 2011 and 2010, a valuation allowance equal to the amount of realizable deferred tax assets was recorded based on the determination that the Bank is more likely than not unable to utilize the deferred tax assets. The Bank reduced the valuation allowance by approximately $929,000 and $1,063,000 in 2011 and 2010, respectively. The Bank has net operating losses carryforwards of approximately $5,357,000 for California franchise tax purposes. California net operating loss carryforwards, to the extent not used, will begin to expire in 2019.

The Bank is subject to federal income tax and franchise tax of the state of California. Income tax returns for the years ended December 31, 2011, 2010, and 2009 are open to audit by the federal authorities and income tax returns for the years ended December 31, 2011, 2010, 2009, 2008, and 2007 are open to audit by state authorities. Unrecognized tax benefits are not expected to significantly increase or decrease within the next twelve months.

NOTE 9 – RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Bank has granted loans to certain directors and their related interests with which they are associated. The balance of these loans outstanding was approximately $1,479,000 and $1,356,000 at December 31, 2011 and 2010, respectively.

Deposits from certain directors, officers, and their related interests with which they are associated held by the Bank at December 31, 2011 and 2010 amounted to approximately $2,853,000 and $1,999,000, respectively.

NOTE 10 – EARNINGS PER SHARE (EPS)

Earnings per share for the years ended December 31, were computed as follows:

	2011	2010
Basic earnings per share:		
Net income	$ 1,916,172	$ 1,520,399
Accretion of preferred stock	(32,667)	(32,666)
Dividends paid on preferred stock	(107,220)	(107,220)
Net income available to common shareholders	$ 1,776,285	$ 1,380,513
Weighted average common shares outstanding	1,771,534	1,760,158
Basic earnings per share	$ 1.00	$ 0.78
Diluted earnings per share:		
Net income	$ 1,916,172	$ 1,520,399
Accretion of preferred stock	(32,667)	(32,666)
Dividends paid on preferred stock	(107,220)	(107,220)
Net income available to common shareholders	$ 1,776,285	$ 1,380,513
Weighted average common shares outstanding	1,771,534	1,760,158
Effect of dilutive options	609	1,055
Adjusted weighted average common shares outstanding	1,772,143	1,761,213
Diluted earnings per share	$ 1.00	$ 0.78

At December 31, 2011 and 2010, there were 433,049 and 439,957 stock options, respectively, that could potentially dilute earnings per share in the future that were not included in the computation of diluted earnings per share because to do so would have been antidilutive. All income per share amounts have been retroactively adjusted for the effect of stock dividends.

NOTE 11– 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 and standby letters of 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, 2011 and 2010, the Bank had the following outstanding financial commitments whose contractual amount represents credit risk:

	2011	2010
Commitments to extend credit	$ 21,380,000	$ 18,491,000
Letters of credit	-	-
	$ 21,380,000	$ 18,491,000

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 and standby letters of credit are secured by real estate.

NOTE 12– STOCK OPTION PLAN

The Bank's 2005 Equity Based Compensation Plan was approved by its shareholders in February 2006. Under the terms of the 2005 Equity Based Compensation Plan (the Plan), officers and key employees may be granted both nonqualified, incentive stock options and restricted stock awards and directors, who are not also an officer or employee, may only be granted nonqualified stock options and restricted stock awards. The Plan provides for a maximum number of shares that may be awarded to eligible employees and directors not to exceed 495,000 shares. Stock options are granted at a price not less than 100% of the fair market value of the stock on the date of grant. Stock options expire no later than ten years from the date of the grant and all equity based awards generally vest over three years. The Plan provides for accelerated vesting if there is a change of control, as defined in the Plan. The Bank recognized stock based compensation cost of $77,384 and $95,313 in 2011 and 2010, respectively. The Bank recognized tax expense related to stock based compensation of $11,859 and $32,789 in 2011 and 2010, respectively.

NOTE 12– STOCK OPTION PLAN (CONTINUED)

The following table shows weighted average assumptions used in valuing stock options granted for the years ended December 31:

	2011	2010
Expected volatility	36.43%	25.00%
Expected term	6.5 years	5.2 years
Expected dividends	None	None
Risk free rate	1.98%	1.65%
Grant date fair value	$ 2.62	$ 2.50

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 longer trading history. The expected term represents the estimated average period of time that the options remain outstanding. Since the Bank does not have sufficient historical data on the exercise of stock options, the expected term is based on the "simplified" method that measures the expected term as the average of the vesting period and the contractual term. The risk free rate of return reflects the grant date interest rate offered for U.S. Treasury bonds over the expected term of the options.

A summary of the status of stock options that have been granted by the Bank as of December 31, 2011 and changes during the year ending thereon is presented below:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at beginning of year	440,962	$ 10.86		
Granted	1,000	$ 10.05		
Exercised	(3,333)	$ 7.50		
Forfeited or expired	(5,000)	$ 9.50		
Outstanding at end of year	433,629	$ 10.64	5.4 years	None
Options exercisable	380,348	$ 10.77	4.8 years	None

As of December 31, 2011, there was approximately $107,000 of total unrecognized compensation cost related to the outstanding stock options that will be recognized over a weighted average period of 1.6 years.

NOTE 13 – REGULATORY MATTERS

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet these 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 classifications are also subject to qualitative judgments by the regulators about components, risk-weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 2011, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2011, 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). To be categorized as well capitalized, the Bank must maintain minimum ratios as set forth in the table below. The following table also sets forth the Bank's actual capital amounts and ratios (dollar amounts in thousands):

	Actual		For capital adequacy purposes		To be well-capitalized under prompt corrective action provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2011:						
Total Capital (to Risk-Weighted Assets)	$ 18,797	19.5%	$ 7,695	≥ 8.0%	$ 9,619	≥ 10.0%
Tier I Capital (to Risk-Weighted Assets)	$ 17,574	18.3%	$ 3,848	≥ 4.0%	$ 5,771	≥ 6.0%
Tier I Capital (to Average Assets)	$ 17,574	10.2%	$ 6,909	≥ 4.0%	$ 8,636	≥ 5.0%
December 31, 2010:						
Total Capital (to Risk-Weighted Assets)	$ 17,011	19.6%	$ 6,959	≥ 8.0%	$ 8,699	≥ 10.0%
Tier I Capital (to Risk-Weighted Assets)	$ 15,903	18.3%	$ 3,480	≥ 4.0%	$ 5,220	≥ 6.0%
Tier I Capital (to Average Assets)	$ 15,903	11.1%	$ 5,750	≥ 4.0%	$ 7,187	≥ 5.0%

NOTE 13 – REGULATORY MATTERS (CONTINUED)

The California Financial Code provides that a bank may not make a cash distribution to its shareholders in excess of the lessor of the bank's undivided profits or the bank's net income for its last three fiscal years less any distributions made to shareholders during the same period without the approval in advance of the Commissioner of the California Department of Financial Institutions. Pursuant to the terms of the Bank's participation in the Troubled Assets Relief Program (TARP) Capital Purchase Program (see Note 16), the Bank's ability to declare or pay dividends on any of their shares is limited by the U.S. Treasury. See Note 10 for payment of dividends on the preferred stock related to the Bank's participation in the TARP Capital Purchase Program.

NOTE 14 – FAIR VALUE MEASUREMENT

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

Securities – The fair values of securities available-for-sale are determined by obtaining quoted prices on nationally recognized securities 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 specific securities but rather by relying on the securities' relationship to other benchmark securities (Level 2).

Collateral-Dependent Impaired Loans – The Bank does not record loans at fair value on a recurring basis. However, from time to time, fair value adjustments are recorded on these loans to reflect: (1) partial write-downs, through charge-offs or specific reserve allowances, that are based on the current appraised or market-quoted value of the underlying collateral or (2) the full charge-off of the loan carrying value. In some cases, the properties for which market quotes or appraisal values have been obtained are located in areas where comparable sales data is limited, outdated, or unavailable. Fair value estimates for collateral-dependent impaired loans are obtained from real estate brokers or other third-party consultants (Level 3).

NOTE 14 – FAIR VALUE MEASUREMENT (CONTINUED)

The following tables summarize the Bank's assets that were measured at fair value on a recurring and non-recurring basis at December 31, 2011:

Description of Assets	December 31, 2011	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Securities available-for-sale (recurring)				
U.S. government and agency securities	$ 44,304,490	$ -	$ 44,304,490	$ -
Mortgage-backed securities	8,742,946	-	8,742,946	-
State and municipal agencies	1,095,246	-	1,095,246	-
Corporate debt securities	2,266,449	-	2,266,449	-
Impaired loans (non-recurring)	745,875	-	-	745,875
Total	$ 57,155,006	$ -	$ 56,409,131	$ 745,875

The following tables summarize the Bank's assets that were measured at fair value on a recurring and non-recurring basis at December 31, 2010:

Description of Assets	December 31, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Securities available-for-sale (recurring)				
U.S. government and agency securities	$ 30,267,692	$ 1,419,296	$ 28,848,396	$ -
Mortgage-backed securities	8,210,686	-	8,210,686	-
Corporate debt securities	2,471,741	447,750	2,023,991	-
Impaired loans (non-recurring)	332,128	-	-	332,128
Total	$ 41,282,247	$ 1,867,046	$ 39,083,073	$ 332,128

NOTE 15 – FAIR VALUE OF FINANCIAL INSTRUMENTS

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

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

The following methods and assumptions were used by the Bank in estimating fair values of financial instruments:

Financial assets – The carrying amounts of cash, short-term investments, due from customers on acceptances, and bank acceptances outstanding are considered to approximate fair value. Short-term investments include federal funds sold, securities purchased under agreements to resell, and interest bearing deposits with banks. The fair values of investment securities, including available for sale and held to maturity, are generally based on quoted market prices. The fair value of variable loans that reprice frequently and that have experienced no significant change in credit risk are based on carrying values. The fair values for all other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers with similar credit quality. Loans are generally expected to be held to maturity and any unrealized gains or losses are not expected to be realized. Fair value for Federal Home Loan Bank stock and interest receivable approximates its carrying value.

Financial liabilities – The carrying amounts of deposit liabilities payable on demands, commercial paper, and other borrowed funds are considered to approximate fair value. For fixed maturity deposits, fair value is estimated by discounting estimated future cash flows using currently offered rates for deposits of similar remaining maturities. The fair value of interest payable approximates its carrying amount.

NOTE 15 – FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Off-balance sheet financial instruments – The fair value of commitments to extend credit and standby letters of credit is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the credit standing of the counterparties.

The estimated fair value of financial instruments at December 31, is summarized as follows (in thousands):

	2011		2010	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash and cash equivalents	$ 19,664	$ 19,664	$ 11,054	$ 11,054
Securities available-for-sale	56,409	56,409	40,950	40,950
Loans, net	97,349	101,533	87,588	90,599
Federal Home Loan Bank stock	781	781	636	636
Interest receivable	724	724	589	589
Financial liabilities:				
Deposits	158,774	159,218	126,107	126,726
Interest payable	35	35	39	39
Off-balance-sheet liabilities:				
Commitments to extend credit and letters of credit	-	214	-	185

NOTE 16 – PREFERRED STOCK

On January 23, 2009, the Bank, in connection with the Troubled Assets Relief Program (TARP) Capital Purchase Program, entered into a Purchase Agreement with the United States Department of the Treasury (the Treasury), pursuant to which the Bank issued 1,968 shares of the Bank's Preferred Stock as Fixed Rate Non-cumulative Perpetual Preferred Stock, Series A (the Series A Preferred Stock) and 98 shares of Fixed Rate Non-cumulative Perpetual Warrant Preferred Stock, Series B (the Series B Preferred Stock) for an aggregate purchase price of $1,968,000 in cash.

Both Series A and Series B Preferred stock qualify as Tier 1 Capital. Series A Preferred Stock pay non-cumulative dividends at a rate of 5% per annum for the first five years and 9% per annum thereafter. Series B Preferred Stock pay non-cumulative dividends at a rate of 9% per annum. Series A Preferred Stock can be redeemed after three years for $1,968,000, and Series B can be redeemed for $98,000 after Series A Preferred Stock has been redeemed.

NOTE 17 – SUBSEQUENT EVENTS

The Bank has evaluated the effects of subsequent events that have occurred after the period ending December 31, 2011 and through March 2, 2012, which is the date the financial statements were issued.

FRESNO FIRST BANK

Corporate Information

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Notice of Annual Meeting

Tuesday, July 10, 2012 at 5:30 pm
Fort Washington Country Club
10272 N. Millbrook
Fresno, CA 93730

Independent Auditors

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