PRESIDIO BANK

FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2010 AND 2009

AND FOR THE YEARS THEN ENDED

AND

INDEPENDENT AUDITOR'S REPORT

PERRY-SMITH
THE POWER OF CONFIDENCE

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INDEPENDENT AUDITOR'S REPORT

The Shareholders and
Board of Directors
Presidio Bank

We have audited the accompanying balance sheet of Presidio Bank as of December 31, 2010 and 2009 and the related statements of operations, changes in shareholders' equity and comprehensive income (loss) and cash flows for the 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 audits 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 Presidio Bank as of December 31, 2010 and 2009 and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Perry-Smith LLP

March 11, 2011

PRESIDIO BANK

BALANCE SHEET

December 31, 2010 and 2009

	2010	2009
ASSETS		
Cash and due from banks	$ 31,399,393	$ 21,141,507
Available-for-sale investment securities, at fair value (Note 3)		4,014,920
Held-to-maturity investment securities, at amortized cost (Note 3)	679,901	684,583
Federal Reserve Bank stock, at cost	1,166,650	872,850
Federal Home Loan Bank stock, at cost	1,023,600	1,151,500
Loans, less allowance for loan losses of $4,911,720 in 2010 and $4,926,017 in 2009 (Notes 4, 5,10 and 13)	253,700,572	213,049,599
Premises and equipment, net (Note 6)	1,505,879	999,185
Accrued interest receivable and other assets	2,048,561	2,267,416
	$ 291,524,556	$ 244,181,560
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits:		
Non-interest bearing	$ 58,699,178	$ 47,317,447
Interest bearing (Note 7)	188,667,939	147,075,858
Total deposits	247,367,117	194,393,305
Borrowings (Note 9)	3,000,000	10,000,000
Accrued interest payable and other liabilities	1,769,061	1,568,361
Total liabilities	252,136,178	205,961,666
Commitments and contingencies (Note 10)		
Shareholders' equity (Notes 11 and 12):		
Preferred stock, no par value; 10,000,000 shares authorized:		
Series A, noncumulative, $1,000 per share liquidation preference; 10,800 shares issued and outstanding	10,547,222	10,482,222
Series B, noncumulative, $1,000 per share liquidation preference; 325 shares issued and outstanding	325,000	325,000
Common stock, no par value; 30,000,000 shares authorized; 4,036,099 and 4,000,000 shares issued and outstanding in 2010 and 2009, respectively	41,930,154	41,647,773
Accumulated deficit	(13,413,998)	(14,250,021)
Accumulated other comprehensive income		14,920
Total shareholders' equity	39,388,378	38,219,894
Total liabilities and shareholders' equity	$ 291,524,556	$ 244,181,560

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

PRESIDIO BANK

STATEMENT OF OPERATIONS

For the Years Ended December 31, 2010 and 2009

	2010	2009
Interest and dividend income:		
Interest and fees on loans	$ 12,697,683	$ 9,740,804
Interest on Federal Funds sold		32,975
Interest on due from banks and interest-bearing deposits in other financial institutions	89,645	26,737
Interest on investment securities	47,624	33,329
Dividend income	68,473	57,185
Total interest and dividend income	12,903,425	9,891,030
Interest expense:		
Interest on deposits	1,318,100	1,527,505
Interest on borrowings	198,415	331,970
Total interest expense	1,516,515	1,859,475
Net interest income	11,386,910	8,031,555
Provision for loan losses (Note 5)	893,555	1,950,894
Net interest income after provision for loan losses	10,493,355	6,080,661
Non-interest income:		
Service charges and fees	269,875	181,805
Other non-interest income	27,151	38,926
Total non-interest income	297,026	220,731
Non-interest expenses:		
Salaries and employee benefits (Notes 5 and 14)	6,016,795	5,893,415
Occupancy and equipment (Notes 6 and 10)	1,436,087	946,706
Other (Note 15)	2,436,476	2,592,327
Total non-interest expenses	9,889,358	9,432,448
Net income (loss)	$ 901,023	$ (3,131,056)
Basic and diluted income (loss) per share	$ 0.22	$ (0.78)
Weighted average number of shares outstanding	4,006,861	4,000,000
Weighted average number of diluted shares outstanding	4,006,959	4,000,000

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

PRESIDIO BANK

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS)

For the Years Ended December 31, 2010 and 2009

	Preferred Stock – Series A		Preferred Stock – Series B		Common Stock		Accum-lated Deficit	Accum-ulated Other Compre--hensive Income	Total Share-holders' Equity	Compre-hensive Income (Loss)
	Shares	Amount	Shares	Amount	Shares	Amount				
Balance, January 1, 2009					4,000,000	$ 41,359,278	$ (11,111,743)		$ 30,247,535	
Issuance of Series A Preferred stock, net of discount	10,800	$ 10,475,000							10,475,000	
Issuance of Series B Preferred stock			325	$ 325,000					325,000	
Amortization of discount on Series A Preferred stock		7,222					(7,222)			
Share-based compensation expense						288,495			288,495	
Comprehensive loss:										
Net loss							(3,131,056)		(3,131,056)	$ (3,131,056)
Net change in unrealized gains on available-for-sale investment securities								$ 14,920	14,920	14,920
										$ (3,116,136)
Balance, December 31, 2009	10,800	10,482,222	325	325,000	4,000,000	41,647,773	(14,250,021)	14,920	38,219,894	
Amortization of discount on Series A Preferred stock		65,000					(65,000)			
Restricted stock granted					36,099					
Share-based compensation expense						282,381			282,381	
Comprehensive income:										
Net Income							901,023		901,023	901,023
Net change in unrealized gains on available-for-sale investment securities								(14,920)	(14,920)	(14,920)
										$ 886,103
Balance, December 31, 2010	10,800	$ 10,547,222	325	$ 325,000	4,036,099	$ 41,930,154	$ (13,413,998)	$ -	$ 39,388,378	

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

PRESIDIO BANK

STATEMENT OF CASH FLOWS

For the Years Ended December 31, 2010 and 2009

	2010	2009
Cash flows from operating activities:		
Net income (loss)	$ 901,023	$ (3,131,056)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Provision for loan losses	893,555	1,950,894
Accretion of discounts on investment securities	4,682	
Depreciation and amortization	408,316	284,670
Loss on disposal of equipment	175	
Deferred loan origination (costs) fees, net	(62,357)	65,217
Share-based compensation expense	282,381	288,495
Decrease (increase) in accrued interest receivable and other assets	218,855	(1,202,449)
Increase in accrued interest payable and other liabilities	200,700	273,136
Net cash provided by (used in) operating activities	2,847,330	(1,471,093)
Cash flows from investing activities:		
Maturity (purchase) of available-for-sale investment securities	4,000,000	(4,000,000)
Purchase of held-to-maturity investment securities		(684,583)
(Purchase) redemption of Federal Reserve Bank stock	(293,800)	85,900
Redemption of FHLB stock	127,900	
Net increase in loans	(41,482,171)	(38,030,473)
Purchases of premises and equipment	(915,935)	(339,327)
Proceeds from sale of premises and equipment	750	
Net cash used in investing activities	(38,563,256)	(42,968,483)
Cash flows from financing activities:		
Net increase in demand, interest-bearing and savings deposits	41,420,064	28,704,374
Net increase (decrease) in time deposits	11,553,748	(2,769,390)
Issuance of preferred stock		10,800,000
Repayments of FHLB advances	(7,000,000)	(14,500,000)
Net cash provided by financing activities	45,973,812	22,234,984
Increase (decrease) in cash and cash equivalents	10,257,886	(22,204,592)
Cash and cash equivalents at beginning of year	21,141,507	43,346,099
Cash and cash equivalents at end of year	$ 31,399,393	$ 21,141,507
Supplemental disclosure of cash flow information:		
Cash paid for interest expense	$ 1,558,982	$ 1,885,794

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

1. THE BUSINESS OF PRESIDIO BANK

Presidio Bank (the "Bank") was approved as state-chartered bank on July 24, 2006 and is a member of the Federal Reserve System (the "Fed"). The Bank is subject to regulation by the Fed, the California Department of Financial Institutions (the "DFI"), and the Federal Deposit Insurance Corporation (the "FDIC"). The Bank's deposits are insured by the FDIC up to applicable legal limits.

The Bank is participating in the FDIC's Transaction Account Guarantee Program. Under this program, through December 31, 2012, all noninterest-bearing transaction accounts are fully guaranteed by the FDIC for the entire amount in the account and the Bank is assessed an annual fee of 10 basis points for all deposit amounts exceeding the existing deposit insurance limit of $250,000. Coverage under the Transaction Account Guarantee Program is in addition to and separate from the coverage available under the FDIC's general deposit insurance rules.

The Bank is headquartered in San Francisco, California and also has branch offices in Walnut Creek, San Rafael, Santa Rosa and Palo Alto, California. The Bank provides traditional commercial banking services to its target market throughout Northern California, consisting of small to medium sized businesses, along with the owners and executives of those firms.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General

The accounting and reporting policies of the Bank conform with accounting principles generally accepted in the United States of America and prevailing practices within the banking industry.

Subsequent Events

Management has reviewed all events occurring from December 31, 2010 through March 11, 2011, the date the financial statements were available to be issued and no events occurred during this period requiring accrual or disclosure.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Cash and Cash Equivalents

For the purpose of the statement of cash flows, cash and cash equivalents consist of cash and due from banks.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Federal Reserve Bank Stock and Federal Home Loan Bank Stock

As a member of both the Federal Reserve Bank (the "FRB") and the Federal Home Loan Bank (the "FHLB"), the Bank is required to maintain a minimum level of investment in the capital stocks of the FRB and FHLB. These investments are considered restricted equity securities and are carried at par value. The Bank may request redemption at par value in excess of the amount required to be held. Stock redemptions are made at the discretion of the FRB and FHLB.

Investment Securities

Investment securities are classified into the following categories:

- Available-for-sale securities reported at fair value, with unrealized gains and losses excluded from earnings and reported, net of taxes, as accumulated other comprehensive income (loss) within shareholders' equity.

- Held-to-maturity securities, which management has the positive intent and ability to hold, reported at amortized cost, adjusted for the accretion of discounts and amortization of premiums.

Management determines the appropriate classification of its investments at the time of purchase and may only change the classification in certain limited circumstances. All transfers between categories are accounted for at fair value. There were no transfers between categories during the years ended December 31, 2010 or 2009.

Gains or losses on the sale of investment securities are computed using the specific identification method. Interest earned on investment securities is reported in interest income, net of applicable adjustments for accretion of discounts and amortization of premiums.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investment Securities (Continued)

An investment security is impaired when its carrying value is greater than its fair value. Investment securities that are impaired are evaluated on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation to determine whether such a decline in their fair value is other than temporary. Management utilizes criteria such as the magnitude and duration of the decline and the intent and ability of the Bank to retain its investment in the securities for a period of time sufficient to allow for an anticipated recovery in fair value, in addition to the reasons underlying the decline, to determine whether the loss in value is other than temporary. The term "other than temporary" is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value is determined to be other than temporary, and management does not intend to sell the security or it is more likely than not that the Bank will not be required to sell the security before recovery, only the portion of the impairment loss representing credit exposure is recognized as a charge to earnings, with the balance recognized as a charge to other comprehensive income. If management intends to sell the security or it is more likely than not that the Bank will be required to sell the security before recovering its forecasted cost, the entire impairment loss is recognized as a charge to earnings.

Loans

Loans are stated at principal balances outstanding. Interest is accrued daily based upon outstanding loan balances. However, when in the opinion of management, loans are considered to be impaired and the future collectibility of interest and principal is in serious doubt, loans are placed on nonaccrual status and the accrual of interest income is suspended. Any interest accrued but unpaid is charged against income. Payments received are applied to reduce principal to the extent necessary to ensure collection. Subsequent payments on these loans, or payments received on nonaccrual loans for which the ultimate collectibility of principal is not in doubt, are applied first to earned but unpaid interest and then to principal.

Substantially all loan origination and commitment fees, net of direct loan origination costs, and purchase premiums and discounts on loans are deferred and recognized as an adjustment of yield, to be amortized to interest income over the contractual term of the loan. The unamortized balance of deferred fees and costs is reported as a component of net loans.

The Bank services loans that have been participated to other financial institutions totaling approximately $18,184,000 and $18,622,000 at December 31, 2010 and 2009, respectively.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Allowance for Loan Losses

The allowance for loan losses is an estimate of credit losses inherent in the Bank's loan portfolio that have been incurred as of the balance-sheet date. The allowance is established through a provision for loan losses which is charged to expense. Additions to the allowance are expected to maintain the adequacy of the total allowance after credit losses and loan growth. Credit exposures determined to be uncollectible are charged against the allowance. Cash received on previously charged off amounts is recorded as a recovery to the allowance. The overall allowance consists of two primary components, specific reserves related to impaired loans and general reserves for inherent losses related to loans that are not impaired.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the original agreement. Loans determined to be impaired are individually evaluated for impairment. When a loan is impaired, the Bank measures impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate, except that as a practical expedient, it may measure impairment based on a loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. A loan is collateral dependent if the repayment of the loan is expected to be provided solely by the underlying collateral.

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the Bank for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. Restructured workout loans typically present an elevated level of credit risk as the borrowers are not able to perform according to the original contractual terms. Loans that are reported as TDRs are considered impaired and measured for impairment as described above.

The determination of the general reserve for loans that are not impaired is based on estimates made by management, to include, but not limited to, consideration of historical losses by portfolio segment, internal asset classifications, and qualitative factors to include economic trends in the Bank's service areas, industry experience and trends, geographic concentrations, estimated collateral values, the Bank's underwriting policies, the character of the loan portfolio, and probable losses inherent in the portfolio taken as a whole.

The Bank maintains a separate allowance for each portfolio segment (loan type). These portfolio segments include commercial, construction and land development, commercial real estate and consumer loans. The allowance for loan losses attributable to each portfolio segment, which includes both impaired loans and loans that are not impaired, is combined to determine the Bank's overall allowance, which is included on the balance sheet.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Allowance for Loan Losses (Continued)

The Bank assigns a risk rating to all loans and periodically performs detailed reviews of all such loans over a certain threshold to identify credit risks and to assess the overall collectability of the portfolio. These risk ratings are also subject to examination by independent specialists engaged by the Bank and the Bank's regulators. During these internal reviews, management monitors and analyzes the financial condition of borrowers and guarantors, trends in the industries in which borrowers operate and the fair values of collateral securing these loans. These credit quality indicators are used to assign a risk rating to each individual loan. The risk ratings can be grouped into five major categories, defined as follows:

Pass – A pass loan is a strong, satisfactory or acceptable credit with no existing or known potential weaknesses deserving of management's close attention.

Special Mention – A special mention loan has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or in the Bank's credit position at some future date. Special Mention loans are not adversely classified and do not expose the Bank to sufficient risk to warrant adverse classification.

Substandard – A substandard loan is not adequately protected by the current sound worth and paying capacity of the borrower or the value of the collateral pledged, if any. Loans classified as substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. Well defined weaknesses include a project's lack of marketability, inadequate cash flow or collateral support, failure to complete construction on time or the project's failure to fulfill economic expectations. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

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

Loss – Loans classified as loss are considered uncollectible and charged off immediately.

The general reserve component of the allowance for loan losses also consists of reserve factors that are based on management's assessment of the following for each portfolio segment: (1) inherent credit risk, (2) historical losses and (3) other qualitative factors. These reserve factors are inherently subjective and are driven by the repayment risk associated with each portfolio segment described below.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Allowance for Loan Losses (Continued)

Commercial – Commercial loans generally possess a lower inherent risk of loss than real estate portfolio segments because these loans are generally underwritten to existing cash flows of operating businesses. Debt coverage is provided by business cash flows and economic trends influenced by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans.

Construction and land development – Construction and land development loans generally possess a higher inherent risk of loss than other real estate portfolio segments. A major risk arises from the necessity to complete projects within specified cost and time lines. Trends in the construction industry significantly impact the credit quality of these loans, as demand drives construction activity. In addition, trends in real estate values significantly impact the credit quality of these loans, as property values determine the economic viability of construction projects.

Commercial real estate – Commercial real estate loans generally possess a higher inherent risk of loss than other real estate portfolio segments, except land and construction loans. Adverse economic developments or an overbuilt market impact commercial real estate projects and may result in troubled loans. Trends in vacancy rates of commercial properties impact the credit quality of these loans. High vacancy rates reduce operating revenues and the ability for properties to produce sufficient cash flow to service debt obligations.

Consumer and other – The consumer and other category includes primarily residential real estate and home equity lines of credit. The degree of risk in this portfolio segment depends primarily on the loan amount in relation to collateral value, the interest rate and the borrower's ability to repay in an orderly fashion. These loans generally possess a lower inherent risk of loss than other real estate portfolio segments. Economic trends determined by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Weak economic trends indicate that the borrowers' capacity to repay their obligations may be deteriorating.

Although management believes the allowance to be adequate, ultimate losses may vary from its estimates. At least quarterly, the Board of Directors reviews the adequacy of the allowance, including consideration of the relative risks in the portfolio, current economic conditions and other factors. If the Board of Directors and management determine that changes are warranted based on those reviews, the allowance is adjusted. In addition, the Bank's primary regulators, the FRB and DFI as an integral part of their examination process, review the adequacy of the allowance. These regulatory agencies may require additions to the allowance based on their judgment about information available at the time of their examinations.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Allowance for Credit Losses on Off-Balance-Sheet Credit Exposures

The Bank also maintains a separate allowance for off-balance-sheet commitments. Management estimates anticipated losses using historical data and utilization assumptions. The allowance for off-balance-sheet commitments is included in accrued interest payable and other liabilities on the balance sheet.

Bank Premises and Equipment

Bank premises and equipment are carried at cost. Depreciation is determined using the straight-line method over the estimated useful lives of the related assets. The useful lives of furniture, fixtures and equipment are estimated to be 3 to 7 years. Leasehold improvements are amortized over the lesser of the respective lease term (including renewal periods that are reasonably assured) or their useful lives, which are generally 7 to 10 years.

Certain operating leases contain scheduled and specified rent increases or incentives in the form of tenant improvement allowances or credits. The scheduled rent increases are recognized on a straight-line basis over the lease term as an increase in the amount of rental expense recognized each period. Lease incentives are capitalized at the inception of the lease and amortized on a straight-line basis over the lease term as a reduction of rental expense. Amounts accrued in excess of amounts paid related to the scheduled rent increases are included in accrued interest payable and other liabilities on the balance sheet.

When assets are sold or otherwise disposed of, the cost and related accumulated depreciation or amortization are removed from the accounts, and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is charged to expense as incurred.

Income Taxes

Deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the reported amount of assets and liabilities and their tax basis. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. A valuation allowance is recognized if, based on the weight of available evidence, management believes it is more likely than not that some portion or all of the deferred tax assets will not be realized.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes (Continued)

At December 31, 2010 and 2009, the Bank did not have a reserve for uncertain tax positions. The Bank uses a comprehensive model for recognizing, measuring, presenting and disclosing in the financial statements tax positions taken or expected to be taken on a tax return. A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded. Interest expense and penalties associated with unrecognized tax benefits, if any, are classified as income tax expense in the statement of operations. The Bank has not accrued for any interest or penalties as of December 31, 2010 or December 31, 2009 because it does not have any unrecognized tax benefits.

Earnings (Loss) Per Share

Basic earnings or loss per share, which excludes dilution, is computed by dividing net income or loss by the weighted-average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock, such as stock options, result in the issuance of common stock which share in the earnings of the Bank. The treasury stock method is applied to determine the dilutive effect of stock options in computing diluted earnings per share. However, diluted earnings per share is not presented when a net loss occurs because the conversion of potential common stock is anti-dilutive.

Share-Based Compensation

The Bank has one share-based compensation plan, the Presidio Bank 2006 Stock Option Plan (the "Plan"), which has been approved by its shareholders and permits the grant of stock options and restricted stock for up to 1,200,000 shares of the Bank's common stock, of which 188,101 shares were available for future grant at December 31, 2010. The Plan is designed to attract and retain employees and directors. The amount, frequency, and terms of share-based awards may vary based on competitive practices, the Bank's operating results and government regulations. New shares are issued upon option exercise of stock options and vesting of restricted stock. The Plan does not provide for the settlement of awards in cash. The Plan requires that the option price may not be less than the fair market value of the stock at the date the option is granted, and that the stock must be paid in full at the time the option is exercised. The Bank has issued four types of awards under the plan: Organizer options, which were granted to founders and organizers and were fully vested upon the granting of the award; service-based options, which are granted to employees and Directors and that will generally vest over a five year period; performance-based options, which are granted to employees and Directors and will vest only if the Bank meets or exceeds certain pre-determined financial goals and objectives; and restricted stock, which generally vest quarterly over a two year period.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Share-Based Compensation (Continued)

The Bank accounts for share-based compensation using a fair-value based method that requires that share-based compensation expense be recorded for all stock options and restricted stock that are ultimately expected to vest as the requisite service is rendered.

Management estimates the fair value of each option award as of the date of grant using a Black-Scholes-Merton option pricing formula. Expected volatility is based on historical volatility of similar entities over a preceding period commensurate with the expected term of the option because the Bank's common stock has been publicly traded for a shorter period than the expected term for the options. The "simplified" method described in the Securities and Exchange Commission's Staff Accounting Bulletin No. 110 is used to determine the expected term of the Bank's options due to the lack of sufficient historical data. The risk-free rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant. Expected dividend yield was not considered in the option pricing formula because the Bank has not paid dividends and has no current plans to do so in the future. In addition to these assumptions, management makes estimates regarding pre-vesting forfeitures that will impact total compensation expense recognized under the Plan. Management uses a simplified method to determine the expected term of our stock options due to the lack of sufficient historical data.

The fair value of restricted stock awards is determined using the fair value of the underlying shares on the date of the grant.

Adoption of New Financial Accounting Standards

Transfers of Financial Assets

In June 2009, the Financial Accounting Standards Board ("FASB") issued FASB Accounting Standards Update ("ASU") 2009-16*, Accounting for Transfers of Financial Assets (Statement 166)*, which amends previously issued accounting guidance to enhance accounting and reporting for transfers of financial assets, including securitizations or continuing exposure to the risks related to transferred financial assets. Prior to the issuance of Statement 166, transfers under participation agreements and other partial loan sales fell under the general guidance for transfers of financial assets. Statement 166 introduces a new definition for a participating interest along with the requirement for partial loan sales to meet the definition of a participating interest for sale treatment to occur. If a participation or other partial loan sale does not meet the definition, the portion sold should remain on the books and the proceeds recorded as a secured borrowing until the definition is met. Additionally, existing provisions that require the transferred assets to be isolated from the originating institution (transferor), that the transferor does not maintain effective control through certain agreements to repurchase or redeem the transferred assets and that the purchasing institution (transferee) has the right to pledge or exchange the assets acquired were retained. The new provisions became effective on January 1, 2010 and early adoption was not permitted. The impact of adoption was not material to the financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Adoption of New Financial Accounting Standards (Continued)

Fair Value Measurements

In January 2010, the FASB issued FASB ASU 2010-06*, Improving Disclosures about Fair Value Measurements,* which amends and clarifies existing standards to require additional disclosures regarding fair value measurements. Specifically, the standard requires disclosure of the amounts of significant transfers between Level 1 and Level 2 of the fair value hierarchy and the reasons for these transfers, the reasons for any transfers in or out of Level 3, and information in the reconciliation of recurring Level 3 measurements about purchases, sales, issuances and settlements on a gross basis. This standard clarifies that reporting entities are required to provide fair value measurement disclosures for each class of assets and liabilities—previously separate fair value disclosures were required for each major category of assets and liabilities. This standard also clarifies the requirement to disclose information about both the valuation techniques and inputs used in estimating Level 2 and Level 3 fair value measurements. Except for the requirement to disclose information about purchases, sales, issuances, and settlements in the reconciliation of recurring Level 3 measurements on a gross basis, these disclosures are effective for the year ended December 31, 2010. The requirement to separately disclose purchases, sales, issuances, and settlements of recurring Level 3 measurements becomes effective for the Bank for the year beginning on January 1, 2011. The Bank adopted this new accounting standard as of January 1, 2010 and the impact of adoption was not material to the financial statements.

Disclosures about Credit Quality

In July 2010, the FASB issued FASB ASU 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*. ASU 2010-20 requires more robust and disaggregated disclosures about the credit quality of financing receivables (loans) and allowances for loan losses, including disclosure about credit quality indicators, past due information and modifications of finance receivables. The disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending on and after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. The adoption of this guidance has significantly expanded disclosure requirements related to accounting policies and disclosures related to the allowance for loan losses but did not have an impact on the Bank's financial position, results of operation or cash flows.

3. INVESTMENT SECURITIES

Investment Securities Available-for-Sale

The Bank held no available-for-sale investment securities at December 31, 2010. The amortized cost and estimated fair value of available-for-sale investment securities at December 31, 2009 consisted of the following:

	2009			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
Agency securities	$ 4,000,000	$ 14,920	$ -	$ 4,014,920

Net unrealized holding gains on available-for-sale investment securities totaling $14,920 were recorded as other comprehensive income within shareholders' equity for the year ended December 31, 2009. There were no sales, calls or transfers of available for sale investment securities for the years ended December 31, 2010 and 2009.

Investment Securities Held-to-Maturity

The amortized cost and estimated fair value of held-to-maturity investment securities at December 31, 2010 and 2009 consisted of the following:

	2010			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
Agency securities	$ 679,901	$ 88,394	$ -	$ 768,295

	2009			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
Agency securities	$ 684,583	$ -	$ -	$ 684,583

Held-to-maturity investment securities are recorded at amortized cost, adjusted for the amortization of premiums or accretion of discounts. There were no sales, calls or transfers of held-to-maturity investment securities for the years ended December 31, 2010 and 2009. Held-to-maturity investment securities mature in 2019.

4. LOANS

Outstanding loans are summarized below:

	December 31, 2010	December 31, 2009
Commercial	$ 90,599,766	$ 68,239,975
Construction and land development	13,438,963	18,969,184
Commercial real estate	121,952,468	96,864,631
Consumer and other	32,905,432	34,248,520
	258,896,629	218,322,310
Deferred loan origination fees, net	(284,337)	(346,694)
Allowance for loan losses	(4,911,720)	(4,926,017)
	$ 253,700,572	$ 213,049,599

Salaries and employee benefits totaling $733,494 and $476,644 were deferred as loan origination costs for the years ended December 31, 2010 and 2009, respectively.

5. ALLOWANCE FOR LOAN LOSSES

Changes in the allowance for loan losses for the years ended December 31, 2010 and 2009 were as follows:

	2010	2009
Balance, beginning of year	$ 4,926,017	$ 2,983,000
Provision for loan losses	893,555	1,950,894
Losses charged to the allowance	(907,852)	(7,877)
Balance, end of year	$ 4,911,720	$ 4,926,017

5. ALLOWANCE FOR LOAN LOSSES (Continued)

The following table shows the allocation of the allowance for loan losses at and for the year ended December 31, 2010 by portfolio segment and by impairment methodology:

	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Total
Allowance for Loan Losses					
Ending balance allocated to portfolio segments	$ 2,393,722	$ 409,501	$ 1,585,495	$ 523,002	$ 4,911,720
Ending balance: individually evaluated for impairment	$ -	$ -	$ 314,137	$ -	$ 314,137
Ending balance: collectively evaluated for impairment	$ 2,393,722	$ 409,501	$ 1,271,358	$ 523,002	$ 4,597,583
Loans					
Ending balance	$ 90,599,766	$ 13,438,963	$121,952,468	$ 32,905,432	$258,896,629
Ending balance: individually evaluated for impairment	$ -	$ -	$ 2,393,887	$ -	$ 2,393,887
Ending balance: collectively evaluated for impairment	$ 90,599,766	$ 13,438,963	$119,558,581	$ 32,905,432	$256,502,742

The following table shows the loan portfolio allocated by management's internal risk ratings at December 31, 2010:

	Credit Risk Profile by Internally Assigned Grade				
	Commercial	Construction and Land Development	Commercial Real Estate	Consumer and Other	Total
Grade:					
Pass	$ 83,773,189	$ 10,338,214	$ 115,159,837	$ 32,905,432	$ 242,176,672
Special Mention	4,671,849	3,100,749	1,649,392		9,421,990
Substandard	2,154,728		5,143,239		7,297,967
Doubtful					
Total	$ 90,599,766	$ 13,438,963	$ 121,952,468	$ 32,905,432	$ 258,896,629

The following table shows an aging analysis of the loan portfolio by the time past due at December 31, 2010:

	30-89 Days Past Due	Nonaccrual	Total Past Due	Current	Total
Commercial:					
Commercial				$ 90,599,766	$ 90,599,766
Construction and land development				13,438,963	13,438,963
Commercial real estate		$ 2,393,887	$ 2,393,887	119,558,581	121,952,468
Consumer and other	$ 500,000		500,000	32,405,432	32,905,432
Total	$ 500,000	$ 2,393,887	$ 2,893,887	$256,002,742	$258,896,629

5. ALLOWANCE FOR LOAN LOSSES (Continued)

The recorded investment and unpaid principal balance of impaired loans totaled $2,393,887 and $480,726 at December 31, 2010 and 2009, respectively. The related allowance for loan losses on impaired loans totaled $314,137 and $270,000 at December 31, 2010 and 2009, respectively. The average recorded investment in impaired loans was $2,973,276 and $128,999 for the years ended December 31, 2010 and 2009, respectively. Interest income recognized on impaired loans totaled $182,130 for the year ended December 31, 2010 and there was no interest income recognized on impaired loans for the year ended December 31, 2009. All of the impaired loans at December 31, 2010 were in the commercial real estate loan segment and there were no impaired loans without an allowance recorded.

The Bank does not have commitments to lend additional funds to borrowers with loans whose terms have been modified in troubled debt restructurings.

Nonaccrual loans totaled $2,393,887 and $480,726 at December 31, 2010 and 2009, respectively. There were no accruing loans past due 90 days or more at December 31, 2010 or 2009. Interest forgone on nonaccrual loans totaled $77,962 and $9,729 for the years ended December 31, 2010 and 2009, respectively.

6. PREMISES AND EQUIPMENT

Premises and equipment consisted of the following:

	December 31,	
	2010	2009
Furniture, fixtures and equipment	$ 1,966,081	$ 1,387,203
Leasehold improvements	744,858	414,461
	2,710,939	1,801,664
Less accumulated depreciation and amortization	(1,205,060)	(802,479)
	$ 1,505,879	$ 999,185

Depreciation and amortization included in occupancy and equipment expense totaled $408,316 and $264,113 for the years ended December 31, 2010 and 2009.

7. INTEREST-BEARING DEPOSITS

Interest-bearing deposits consisted of the following:

	December 31, 2010	December 31, 2009
Savings	$ 1,347,852	$ 217,075
Money market	105,258,563	91,834,474
Interest-bearing demand accounts	42,816,883	27,333,416
Time, $100,000 or more	37,648,807	26,309,486
Other time	1,595,834	1,381,407
	$ 188,667,939	$ 147,075,858

Aggregate annual maturities of time deposits are as follows:

Year Ending December 31,	
2011	$ 27,598,335
2012	1,910,030
2013	2,527,550
2014	4,076,098
2015	3,132,628
	$ 39,244,641

Interest expense recognized on interest-bearing deposits for the years ended December 31, 2010 and 2009 consisted of the following:

	December 31, 2010	December 31, 2009
Savings	$ 8,376	$ 783
Money market	631,922	702,458
Interest-bearing demand accounts	295,179	284,747
Time, $100,000 or more	20,913	500,640
Other time	361,710	38,877
	$ 1,318,100	$ 1,527,505

Deposits totaling approximately $31,072,000 or 12.56% of total deposits, were from two major depositors at December 31, 2010. The loss of these deposit relationships could have a material impact on the bank's operations and liquidity. Management attempts to mitigate this risk by working directly with these depositors and by maintaining sufficient liquidity to manage fluctuations in account balances within these larger relationships.

8. INCOME TAXES

Income taxes for the years ended December 31, 2010 and 2009 consisted of the following:

	Federal	State	Total
2010			
Deferred	$ 412,000	$ (110,000)	$ 302,000
Valuation allowance	(412,000)	110,000	(302,000)
Income tax expense	$ -	$ -	$ -

	Federal	State	Total
2009			
Deferred	$ (815,000)	$ (291,000)	$ (1,106,000)
Valuation allowance	815,000	291,000	1,106,000
Income tax expense	$ -	$ -	$ -

The Bank's income tax expense differed from the amount computed by applying the Federal statutory rate of 34% for 2010 and 2009 to the loss before income taxes primarily as a result of the imposition of the valuation allowance against the Bank's deferred tax assets.

8. INCOME TAXES (Continued)

Deferred tax assets (liabilities) at December 31, 2010 and 2009 consisted of the following:

	2010	2009
Deferred tax assets:		
Net operating losses	$ 2,614,000	$ 2,632,000
Organization costs	409,000	448,000
Allowance for loan losses	2,063,000	2,134,000
Share-based compensation	124,000	101,000
Accrued expenses	72,000	77,000
Other	176,000	33,000
Deferred tax assets before valuation allowance	5,458,000	5,425,000
Valuation allowance	(4,852,000)	(5,148,000)
Total deferred tax assets	606,000	277,000
Deferred tax liabilities:		
Depreciation and amortization	(152,000)	(59,000)
FHLB stock dividends	(5,000)	(6,000)
Prepaid expenses	(63,000)	(20,000)
Unrealized gain on available-for-sale securities		(6,000)
Deferred loan costs	(386,000)	(186,000)
Total deferred tax liabilities	(606,000)	(277,000)
Net deferred tax assets	$ -	$ -

The determination of the amount of deferred income tax assets which are more likely than not to be realized is primarily dependent on projections of future earnings, which are subject to uncertainty and estimates that may change given economic conditions and other factors. The realization of deferred income tax assets is assessed and a valuation allowance is recorded if it is "more likely than not" that all or a portion of the deferred tax asset will not be realized. "More likely than not" is defined as greater than a 50% chance. All available evidence, both positive and negative is considered to determine whether, based on the weight of that evidence, a valuation allowance is needed. Based upon management's analysis of available evidence, it is "more likely than not" that none of the Bank's deferred income tax assets as of December 31, 2010 and 2009 will be fully realized and therefore a full valuation allowance was recorded.

At December 31, 2010, the Bank had Federal net operating loss carryforwards (NOLs) of approximately $6,094,000 and State NOLs of approximately $7,573,000. The Federal NOLs begin to expire in 2026 and the State NOLs begin to expire in 2016. The Bank's tax returns filed since inception continue to be open to examination by both federal and California tax authorities.

9. BORROWING ARRANGEMENTS

Lines of Credit

The Bank has unsecured Federal funds lines of credit with two of its correspondent banks under which it can borrow up to an aggregate of $10,000,000. There were no borrowings outstanding under these arrangements at December 31, 2010 or 2009.

FHLB Advances

The Bank has a borrowing arrangement with FHLB under which short-term and long term advances are secured by the Bank's loan portfolio. The Bank's credit limit varies according to the amount and composition of loans pledged as collateral. At December 31, 2010, the amounts pledged and borrowing capacity under such limits were approximately $87,848,000 and $36,928,000, respectively. At December 31, 2009, the amounts pledged and borrowing capacity under such limits were approximately $76,698,000 and $36,583,000, respectively.

At December 31, 2010, borrowings outstanding under these arrangements were as follows:

Interest Rate	Maturity Date	Advance Amount
3.62%	October 31, 2011	3,000,000
		$ 3,000,000

At December 31, 2009, borrowings outstanding under these arrangements were as follows:

Interest Rate	Maturity Date	Advance Amount
3.15%	September 10, 2010	$ 4,000,000
3.62%	October 31, 2011	3,000,000
0.06%	January 4, 2010	3,000,000
		$ 10,000,000

10. COMMITMENTS AND CONTINGENCIES

Operating Leases

The Bank leases its San Francisco headquarters and Walnut Creek, San Rafael and Palo Alto branch offices under non-cancelable operating leases. The leases expire on May 31, 2016, March 31, 2016, February 28, 2013 and January 31, 2020 respectively. The leases include annual rent adjustments of approximately 2.6%, 1.6%, 3% and 3%, respectively, each year during the initial lease terms. The San Francisco lease has two five year renewal options, the Walnut Creek, San Rafael and Palo Alto leases each have one five year renewal option. The Bank Leases its Santa Rosa branch offices on a month-to-month basis.

Approximate future minimum lease payments are as follows:

Year Ending December 31,	Operating Leases
2011	$ 846,499
2012	852,122
2013	765,390
2014	763,640
2015	783,499
Thereafter	1,599,008
	$ 5,610,158

Rental expense included in occupancy and equipment expense totaled $958,071 and $612,997 for years ended December 31, 2010 and 2009, respectively.

Financial Instruments With Off-Balance-Sheet Risk

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business in order to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments consist of the following:

	December 31,	
	2010	2009
Commitments to extend credit	$ 90,347,000	$ 72,560,000
Standby letters of credit	$ 5,211,000	$ 2,334,000

The Bank's exposure to credit loss in the event of nonperformance by the other party for commitments to extend 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 included on the balance sheet.

10. COMMITMENTS AND CONTINGENCIES (Continued)

Financial Instruments With Off-Balance-Sheet Risk (Continued)

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. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, and deeds of trust on residential real estate and income-producing commercial properties.

Standby letters of credit are conditional commitments issued to guarantee the performance of a client to a third party. The credit risk involved in issuing standby letters of credit is essentially the same as that involved in extending loans to clients. The fair value of the liability related to these standby letters of credit, which represents the fees received for issuing the guarantees, was not significant at December 31, 2010. The Bank recognizes these fees as revenue over the term of the commitment or when the commitment is used.

Commercial loan commitments represent approximately 64.64% of total commitments and are generally unsecured or secured by collateral other than real estate and have variable interest rates. Consumer loan commitments represent approximately 11.33% of total commitments and are generally unsecured or secured by collateral other than real estate and have variable interest rates. Real estate loan commitments represent approximately 6.83% of total commitments and are generally secured by property with a loan-to-value ratio not to exceed 75%. The majority of real estate commitments also have variable interest rates. Letters of credit represent 3.12% of total commitments. Home equity lines of credit represent the remaining 14.08% of total commitments and are generally secured by residential real estate and have both variable and fixed interest rates.

Concentrations of Credit Risk

The Bank grants real estate mortgage, real estate construction and commercial loans to customers in San Francisco and surrounding counties. A substantial portion of its portfolio is secured by commercial and residential real estate at December 31, 2010 and 2009.

In management's judgment, a concentration of loans exists in real estate related loans with approximately 64% of the Bank's loans being real estate related. Although management believes the loans within this concentration have no more than the normal risk of collectibility, a substantial decline in the performance of the economy in general or a decline in real estate values in the Bank's primary market area, in particular, could have an adverse impact on the collectibility of these loans. Personal and business income represent the primary source of repayment for a majority of these loans.

10. COMMITMENTS AND CONTINGENCIES (Continued)

Correspondent Banking Agreements

The Bank maintains funds on deposit with other federally insured financial institutions under correspondent banking agreements. Those insured financial institutions have elected to participate in the FDIC sponsored Transaction Account Guarantee Program. Under that program, through December 31, 2012, all noninterest-bearing transaction accounts are fully guaranteed by the FDIC for the entire amount in the account. Coverage under the Transaction Account Guarantee Program is in addition to and separate from the coverage available under the FDIC's general deposit insurance rules.

11. SHARE-BASED COMPENSATION

Stock Option Awards

Stock option activity for the year ended December 31, 2010 is summarized as follows:

	Number of Stock Options Outstanding		Weighted Average Exercise Prices	Weighted Average Remaining Contractual Life
Outstanding at January 1, 2009	969,460	$	9.94	7.9 years
Granted	61,000	$	10.00	
Cancelled or expired	(5,300)	$	9.46	
Outstanding at December 31, 2009	1,025,160	$	9.95	7.2 years
Granted	17,300	$	9.33	
Cancelled or expired	(66,660)	$	9.98	
Outstanding at December 31, 2010	975,800	$	9.93	6.2 years
Exercisable at December 31, 2010	605,400	$	9.97	5.8 years
Additional options expected to vest	254,724	$	9.86	6.7 years

There was no intrinsic value of stock options outstanding, exercisable or expected to vest at December 31, 2010.

11. SHARE-BASED COMPENSATION (Continued)

Stock Option Awards (Continued)

The weighted average exercise price and weighted average remaining contractual term of these awards was as follows at December 31, 2010:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term
Organizer options	180,000	$ 10.00	5.5 years
Service-based options	643,300	$ 9.92	6.4 years
Performance-based options	149,500	$ 9.93	6.3 years

The unrecognized compensation cost related to non-vested service-based options totaled $103,630 as of December 31, 2010. That cost is expected to be amortized on an accelerated basis over a weighted average period of 3.1 years and will be adjusted for subsequent changes in estimated forfeitures. The unrecognized compensation cost related to non-vested performance-based options totaled approximately $214,855 as of December 31, 2010. That cost will be amortized for awards that are expected to vest when and if it becomes probable that the performance measures will be achieved. These performance measures are principally related to asset and deposit size and return on average assets for the twelve months ended June 30, 2011. In management's opinion, it is not probable at the present time that the Bank will achieve these targets by June 30, 2011 and, therefore, no compensation expense has been recorded for the performance-based options for the years ended December 31, 2010 and 2009.

The following stock option information for service-based options is for the years ended December 31, 2010 and 2009:

	2010	2009
Weighted average grant date fair value per share of options granted	$1.00	$0.76
Significant fair value assumptions:		
Expected term in years	6.5 years	6.5 years
Expected annual volatility	22.27%	23.99%
Expected annual dividend yield	0%	0%
Risk-free interest rate	3.6%	3.1%
Total compensation cost (included in operating expenses)	$170,474	$288,495

11. SHARE-BASED COMPENSATION (Continued)

Restricted Stock Awards

The following restricted stock information is for the year ended December 31, 2010.

	2010
Number of shares granted	36,099
Weighted average grant date fair value per share	$6.20

Compensation cost associated with the restricted stocks totaled $111,907 for the year ended December 31, 2010. As of December 31, 2010 the unrecognized compensation cost related to the nonvested restricted stock totaled approximately $111,907. The unrecognized compensation cost at December 31, 2010 is expected to be amortized on a straight-line basis over a weighted average period of one year and will be adjusted for subsequent changes in estimated forfeitures. 18,054 shares of the restricted stock were vested as of December 31, 2010. The fair value of restricted stock that vested during the year ended December 31, 2010 totaled $111,934. There were no restricted stock awards at December 31, 2009.

12. SHAREHOLDERS' EQUITY

Preferred Stock

On November 20, 2009, the Bank entered into a Letter Agreement (the "Purchase Agreement") with the United States Department of the Treasury (the "Treasury"), pursuant to which the Bank issued and sold (i) 10,800 shares of Fixed Rate Non-cumulative Perpetual Preferred Stock, Series A (the "Series A Preferred Stock") for a purchase price of $10,800,000 and (ii) a warrant to purchase 325 shares of Fixed Rate Non-cumulative Perpetual Preferred Stock, Series B stock, (the "Warrant Preferred") for $0.01 per share for an aggregate exercise price of $3.25. The Treasury exercised the warrant immediately upon issuance.

The Series A Preferred Stock qualifies as Tier 1 capital and pays non-cumulative dividends quarterly at a rate of 5% per annum for the first five years, and 9% per annum thereafter. The Warrant Preferred pays non-cumulative dividends at a rate of 9% per annum until redemption. Either series may be redeemed by the Bank after three years; however, the Warrant Preferred may not be redeemed until after all the Series A Preferred Stock has been redeemed. Prior to the end of three years, the Series A Preferred Stock and the Warrant Preferred may be redeemed by the Bank only with proceeds from the sale of qualifying equity securities (a "Qualified Equity Offering").

The Series A Preferred Stock and the Warrant Preferred were issued in a private placement exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended. Neither the Series A Preferred Stock nor the Warrant Preferred will be subject to any contractual restrictions on transfer, except that the Treasury and its transferees shall not effect any transfer of the Series A or Series B Preferred Stock which would require the bank to become subject to the periodic reporting requirements of Section 13 or 15(d) of the Exchange Act.

12. SHAREHOLDERS' EQUITY

Preferred Stock (Continued)

The Series A Preferred and Warrant Preferred shall be non-voting, other than class voting rights on (i) any authorization or issuance of shares ranking senior to the Series A Preferred and Warrant Preferred, (ii) any amendment to the rights of the Series A Preferred and Warrant Preferred, or (iii) any merger, exchange or similar transaction which would adversely affect the rights of the Series A Preferred and Warrant Preferred.

If dividends on the Series A Preferred and Warrant Preferred are not paid in full for six dividend periods, whether or not consecutive, the holders of the Series A Preferred and Warrant Preferred will have the right to elect 2 directors. The right to elect directors will end when full dividends have been paid for all prior dividend periods.

In the Purchase Agreement, the Bank agreed that, until such time as the Treasury ceases to own any of its debt or equity securities acquired pursuant to the Purchase Agreement, the Bank will take all necessary action to ensure that its benefit plans with respect to its senior executive officers comply with Section 111(b) of the Emergency Economic Stabilization Act of 2008 (the "EESA") as implemented by any guidance or regulation under the EESA that has been issued and is in effect as of the date of issuance of the Series A Preferred Stock and the Warrant Preferred, and the Bank agreed to not adopt any benefit plans with respect to, or which cover, its senior executive officers that do not comply with the EESA, and the applicable executives have consented to the foregoing. Furthermore, the Purchase Agreement allows the Treasury to unilaterally amend the terms of the agreement.

With respect to dividends on the Bank's common stock, the Treasury's consent shall be required for any increase in common dividends per share until the third anniversary of the date of its investment, unless prior to such third anniversary the Series A Preferred Stock and the Warrant Preferred are redeemed in whole or the Treasury has transferred all of the Series A Preferred Stock and Warrant Preferred to third parties. After the third anniversary and prior to the tenth anniversary, the Treasury's consent shall be required for any increase in aggregate common dividends per share greater than 3% per annum; provided that no increase in common dividends may be made as a result of any dividend paid in common shares, any stock split or similar transaction. After the tenth anniversary, the Bank is prohibited from paying common dividends or repurchasing any equity securities or trust preferred securities until all equity securities held by the Treasury are redeemed in whole or the Treasury has transferred all of such equity securities to third parties.

Furthermore, for as long as any Series A Preferred Stock or Warrant Preferred is outstanding, no dividends may be declared or paid on junior preferred shares, preferred shares ranking pari passu with the Series A Preferred Stock or Warrant Preferred, or common shares (other than in the case of pari passu preferred shares or dividends on a pro rata basis with the Series A Preferred Stock or Warrant Preferred), nor may the Bank repurchase or redeem any junior preferred shares, preferred shares ranking pari passu with the Series A Preferred Stock or Warrant Preferred, unless the full dividend for the latest completed dividend period has been declared and paid in full.

12. SHAREHOLDERS' EQUITY (Continued)

Preferred Stock (Continued)

The Bank recorded a discount on the Series A Preferred Stock at approximately the liquidation preference of the Warrant Preferred. The discount recorded on the Series A Preferred Stock will be amortized on the level-yield method over five years.

Dividends

Upon declaration by the Board of Directors, all shareholders of record will be entitled to receive dividends. The California Financial Code restricts the total dividend payment of any state banking association in any calendar year to the lesser of (1) the bank's retained earnings or (2) the Bank's net income for its last three fiscal years, less distributions made to shareholders during the same three-year period. At December 31, 2010, no amounts were free of such restrictions.

Regulatory Capital

The Bank is subject to certain regulatory capital requirements administered by the FRB and the FDIC. 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, the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. These quantitative measures are established by regulation and require that minimum amounts and ratios of total and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets be maintained. Capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

The Bank is also subject to additional capital guidelines under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table on the following page. The most recent notification from the FDIC categorized the Bank as well capitalized under these guidelines. There are no conditions or events since that notification that management believes have changed the Bank's category.

Management believes that the Bank met all of its capital adequacy requirements as of December 31, 2010 and 2009.

12. SHAREHOLDERS' EQUITY (Continued)

Regulatory Capital (Continued)

	2010		2009	
	Amount	Ratio	Amount	Ratio
Leverage Ratio				
Presidio Bank	$ 39,388,378	13.8%	$ 38,205,000	16.1%
Minimum requirement for "Well-Capitalized" institution	$ 14,273,124	5.0%	$ 11,865,000	5.0%
Minimum regulatory requirement	$ 11,418,499	4.0%	$ 9,492,000	4.0%
Tier 1 Risk-Based Capital Ratio				
Presidio Bank	$ 39,388,378	14.0%	$ 38,205,000	16.0%
Minimum requirement for "Well-Capitalized" institution	$ 16,849,337	6.0%	$ 14,327,000	6.0%
Minimum regulatory requirement	$ 11,232,891	4.0%	$ 9,551,000	4.0%
Total Risk-Based Capital Ratio				
Presidio Bank	$ 49,921,230	15.3%	$ 41,225,000	17.2%
Minimum requirement for "Well-Capitalized" institution	$ 28,082,228	10.0%	$ 23,968,000	10.0%
Minimum regulatory requirement	$ 22,465,783	8.0%	$ 19,174,000	8.0%

13. RELATED PARTY TRANSACTIONS

During the normal course of business, the Bank enters into transactions with related parties, including Directors, executive officers and affiliates. These transactions include borrowings from the Bank with substantially the same terms, including rates and collateral, as loans to unrelated parties. The following is a summary of the aggregate activity involving related party borrowers during the years ended December 31, 2010 and 2009:

	2010	2009
Beginning balance	$ 1,914,000	$ 1,184,000
Disbursements	5,636,000	4,553,000
Amounts repaid	(5,573,000)	(3,823,000)
Ending balance	$ 1,977,000	$ 1,914,000
Undisbursed commitments to related parties	$ 1,505,000	$ 1,125,000

14. EMPLOYEE BENEFIT PLANS

Profit Sharing Plan

In 2006, the Bank adopted the Presidio Bank 401(k) Profit Sharing Plan and Trust. All employees 21 years of age or older are eligible to participate in the plan. Eligible employees may elect to make tax deferred contributions up to the maximum amount allowed by law. The Bank may make additional contributions to the plan at the discretion of the Board of Directors. Bank contributions vest at a rate of 20% annually for all employees. The Bank made contributions to the Plan totaling approximately $178,000 and $163,000 for the years ended December 31, 2010 and 2009, respectively.

15. OTHER EXPENSES

Other expenses for the years ended December 31, 2010 and 2009 consisted of the following:

	2010	2009
Data processing	$ 649,521	$ 549,014
Regulatory and insurance	467,660	426,257
Professional fees	335,268	404,836
Travel and entertainment	230,128	191,579
Stationary and supplies	164,533	171,414
Correspondent bank charges	141,128	132,106
Telephone	111,311	102,406
Provision for losses on off-balance-sheet commitments		340,000
Other	336,927	274,715
	$ 2,436,476	$ 2,595,327

16. FAIR VALUE MEASUREMENTS

Fair Value of Financial Instruments

The estimated carrying and fair values of the Bank's financial instruments are as follows:

	December 31, 2010		December 31, 2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash and due from banks	$ 31,399,393	$ 31,399,393	$ 21,141,507	$ 21,141,507
Available-for-sale investment Securities			4,014,920	4,014,920
Held-to-maturity investment Securities	679,901	768,295	684,583	684,583
FRB and FHLB stock	2,190,250	2,190,250	2,024,350	2,024,350
Loans, net	253,700,572	256,301,856	213,049,599	218,602,000
Accrued interest receivable	810,684	810,684	701,019	701,019
Financial liabilities:				
Deposits	$ 247,367,117	$ 243,879,182	$ 194,393,305	$ 191,184,000
Borrowings	3,000,000	3,103,014	10,000,000	10,210,000
Accrued interest payable	119,914	119,914	162,381	162,381

These estimates do not reflect any premium or discount that could result from offering the Bank's entire holdings of a particular financial instrument for sale at one time, nor do they attempt to estimate the value of anticipated future business related to the instruments. In addition, the tax ramifications related to the realization of unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of these estimates.

The following methods and assumptions were used to estimate the fair value of financial instruments. For cash and cash equivalents, variable-rate loans and leases, accrued interest receivable and payable, FRB and FHLB stock, demand deposits and short-term borrowings, the carrying amount is estimated to be fair value. For investment securities, fair values are based on quoted market prices, quoted market prices for similar securities and indications of value provided by brokers. The fair values for fixed-rate loans and leases are estimated using discounted cash flow analyses, using interest rates currently being offered at each reporting date for loans with similar terms to borrowers of comparable creditworthiness. Fair values for fixed-rate certificates of deposit are estimated using discounted cash flow analyses using interest rates offered at each reporting date by the Bank for certificates with similar remaining maturities. The fair value of long term borrowings are estimated using discounted cash flow analyses using interest rates offered at each reporting date by FHLB for advances with similar remaining maturities. The fair values of commitments are estimated using the fees currently charged to enter into similar agreements and are not significant and, therefore, not included in the above table.

16. FAIR VALUE MEASUREMENTS (Continued)

Fair Value of Financial Instruments (Continued)

Fair Value Hierarchy

The Bank groups its assets and liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. Valuations within these levels are based upon:

Level 1 – Quoted market prices for identical instruments traded in active exchange markets.

Level 2 – Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable or can be corroborated by observable market data.

Level 3 – Model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect the Bank's estimates of assumptions that market participants would use on pricing the asset or liability. Valuation techniques include management judgment and estimation which may be significant.

Management monitors the availability of observable market data to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period.

Management evaluates the significance of transfers between levels based upon the nature of the financial instrument and size of the transfer relative to total assets, total liabilities or total earnings.

16. FAIR VALUE MEASUREMENTS (Continued)

Fair Value of Financial Instruments (Continued)

Assets Recorded at Fair Value

The following tables present information about the Bank's assets and liabilities measured at fair value on a recurring and nonrecurring basis:

Recurring Basis

The Bank is required on permitted to record the following assets at fair value on a recurring basis under accounting standards,

Description	Fair Value	Level 1	Level 2	Level 3
December 31, 2009				
Available-for-sale investment securities				
Debt securities:				
Mortgage backed securities	$ 4,014,920	$ -	$ 4,014,920	$ -
Total assets measured at fair value on a recurring basis	$ 4,014,920	$ -	$ 4,014,920	$ -

Fair values for available-for-sale investment securities are based on quoted market prices for similar securities. During the year ended December 31, 2009, there were no significant transfers in or out of Levels 1 and 2. There were no assets recorded at fair value on a recurring basis at December 31, 2010.

Non-recurring Basis

The Bank may be required, from time to time, to measure certain assets at fair value on a non-recurring basis. These include assets that are measured at the lower of cost or market value that were recognized at fair value which was below cost at the reporting date.

Description	Fair Value	Level 1	Level 2	Level 3
December 31, 2010				
Impaired loans	$ 2,079,750	$ -	$ -	$ 2,079,750
December 31, 2009				
Impaired loans	$ 210,726	$ -	$ -	$ 210,726

The fair value of impaired loans is based on the fair value of the collateral for all collateral dependent loans and for other impaired loans is estimated using a discounted cash flow model. Impaired loans were categorized as Level 3 with unobservable inputs and assumptions in fair value measurements. Losses on impaired loans totaled $907,842 and $270,000 for the year ended December 31, 2010 and 2009, respectively.