

SUTTER COMMUNITY BANK

**Independent Auditor's Report
and
Financial Statements**

**For the year ended December 31, 2007 and
For the period from June 19, 2006
(Date operations commenced) through
December 31, 2006**

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Sutter Community Bank

We have audited the accompanying balance sheets of Sutter Community Bank (the Bank) as of December 31, 2007 and 2006, and the related statements of operations, changes in shareholders' equity, and cash flows for the year ended December 31, 2007 and the period from June 19, 2006 (date operations commenced) through December 31, 2006. 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 audit.

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 Sutter Community Bank as of December 31, 2007 and 2006, and the results of its operations and its cash flows for the year ended December 31, 2007 and the period from June 19, 2006 (date operations commenced) through December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

Moss Adams LLP

Stockton, California
March 28, 2008

SUTTER COMMUNITY BANK

SUTTER COMMUNITY BANK
BALANCE SHEETS

ASSETS

	DECEMBER 31,	
	2007	2006
Cash and due from banks	\$ 1,209,062	\$ 2,185,703
Federal funds sold	10,530,000	5,060,000
	<u>11,739,062</u>	<u>7,245,703</u>
Cash and cash equivalents	11,739,062	7,245,703
Loans, net	32,720,255	17,179,325
Premises and equipment, net	435,841	597,068
Interest receivable and other assets	809,630	186,539
	<u>\$ 45,704,788</u>	<u>\$ 25,208,635</u>

LIABILITIES AND SHAREHOLDERS' EQUITY

Deposits	\$ 37,869,184	\$ 17,216,952
Interest payable and other liabilities	528,405	217,574
	<u>38,397,589</u>	<u>17,434,526</u>
Total liabilities	38,397,589	17,434,526
Commitments and contingencies (Notes 9 and 11)		
Shareholders' equity		
Preferred stock, no par value, 5,000,000 shares authorized; no shares issued or outstanding	-	-
Common stock, no par value, 5,000,000 shares authorized; 951,678 shares issued and outstanding at December 31, 2007 and 2006	9,478,418	9,478,418
Additional paid-in capital	236,281	-
Accumulated deficit	(2,407,500)	(1,704,309)
	<u>7,307,199</u>	<u>7,774,109</u>
Total shareholders' equity	7,307,199	7,774,109
	<u>\$ 45,704,788</u>	<u>\$ 25,208,635</u>

SUTTER COMMUNITY BANK
STATEMENTS OF OPERATIONS
FOR THE YEAR ENDED DECEMBER 31, 2007 AND
FOR THE PERIOD FROM JUNE 19, 2006 (DATE OPERATIONS COMMENCED)
THROUGH DECEMBER 31, 2006

	2007	2006
INTEREST INCOME		
Interest and fees on loans	\$ 2,350,060	\$ 474,503
Interest on federal funds sold	344,840	268,193
	<u>2,694,900</u>	<u>742,696</u>
INTEREST EXPENSE		
Interest expense on deposits	1,018,406	178,075
Interest expense on borrowings	-	933
	<u>1,018,406</u>	<u>179,008</u>
Net interest income	1,676,494	563,688
PROVISION FOR LOAN LOSSES	218,200	217,530
Net interest income after provision for loan losses	<u>1,458,294</u>	<u>346,158</u>
NON-INTEREST INCOME		
Gain on sale of loans	327,740	-
Service charges on deposits	59,141	9,338
Other operating income	32,225	7,835
	<u>419,106</u>	<u>17,173</u>
NON-INTEREST EXPENSES		
Salaries and employee benefits	1,544,818	705,497
Professional fees	148,061	161,783
Occupancy expense	290,147	149,906
Data processing fees	262,497	139,019
Advertising and promotion	151,767	104,589
Supplies expense	33,748	29,164
Transportation and communication expense	21,939	21,971
Insurance expense	50,998	15,151
Other operating expenses	75,816	15,214
	<u>2,579,791</u>	<u>1,342,294</u>
LOSS BEFORE INCOME TAXES	(702,391)	(978,963)
Provision for income taxes	800	-
NET LOSS	<u>\$ (703,191)</u>	<u>\$ (978,963)</u>
NET LOSS PER SHARE – BASIC AND DILUTED	<u>\$ (0.74)</u>	<u>\$ (1.03)</u>
WEIGHTED AVERAGE SHARES OUTSTANDING	<u>951,678</u>	<u>951,678</u>

SUTTER COMMUNITY BANK
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE YEAR ENDED DECEMBER 31, 2007 AND
FOR THE PERIOD FROM JUNE 19, 2006 (DATE OPERATIONS COMMENCED)
THROUGH DECEMBER 31, 2006

	Common Stock		Additional Paid-In Capital	Accumulated Deficit	Total
	Shares	Amount			
Net loss incurred during organizational period	-	\$ -	\$ -	\$ (725,346)	\$ (725,346)
Issuance of common stock, net of stock offering expenses of \$38,362	951,678	9,478,418	-	-	9,478,418
Net loss	-	-	-	(978,963)	(978,963)
Balances at December 31, 2006	951,678	9,478,418	-	(1,704,309)	7,774,109
Stock based compensation	-	-	236,281	-	236,281
Net loss	-	-	-	(703,191)	(703,191)
Balances at December 31, 2007	951,678	\$ 9,478,418	\$ 236,281	\$ (2,407,500)	\$ 7,307,199

SUTTER COMMUNITY BANK
STATEMENTS OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2007 AND
FOR THE PERIOD FROM JUNE 19, 2006 (DATE OPERATIONS COMMENCED)
THROUGH DECEMBER 31, 2006

	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$ (703,191)	\$ (978,963)
Adjustments to reconcile net loss to net cash from operating activities:		
Depreciation and amortization of premises and equipment	203,663	108,296
Stock based compensation	236,281	-
Provision for loan losses	218,200	217,530
Proceeds from sale of loans	3,783,996	-
Gain on sale of loans	327,740	-
Increase in interest payable and other liabilities	310,831	147,032
Increase in interest receivable and other assets	(400,376)	(150,481)
Net cash from operating activities	3,977,144	(656,586)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net increase in loans	(19,870,866)	(17,396,855)
Purchase of equity stock	(222,715)	(400)
Purchase of premises and equipment	(42,436)	(424,148)
Net cash from investing activities	(20,136,017)	(17,821,403)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in demand deposits and savings accounts	8,032,546	10,768,326
Net increase in time deposits	12,619,686	6,448,626
Repayment of loan from organizers	-	(400,000)
Repayment of other borrowings	-	(700,000)
Net cash from financing activities	20,652,232	16,116,952
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	4,493,359	(2,361,037)
CASH AND CASH EQUIVALENTS, beginning of period	7,245,703	9,606,740
CASH AND CASH EQUIVALENTS, end of year	\$ 11,739,062	\$ 7,245,703
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest	\$ 731,193	\$ 68,253
Income taxes	\$ 800	\$ -

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of Sutter Community 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.

On December 15, 2005, the California Commissioner of Financial Institutions approved the Bank's application for organization. The Bank also received conditional approval of an application that it filed for insurance of bank deposit accounts with the Federal Deposit Insurance Corporation (FDIC). The state chartered bank was incorporated under the laws of the state of California on December 19, 2005, and opened for business on June 19, 2006. The Bank offers traditional commercial banking products and services to businesses and individuals through one branch located in Sutter County.

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. The Bank provides for estimated losses on loans receivable and real estate when any significant and permanent decline in value occurs. 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 identified, 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;
- Determination and evaluation of asset servicing rights; and
- Determination and evaluation of deferred tax assets and liabilities.

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and cash equivalents – Cash and cash equivalents include cash on hand, amounts due from banks, money market funds, and federal funds sold. Generally, federal funds are sold for one-day periods. The Bank maintains the minimum required amount of funds on deposit with other federally insured financial institutions under correspondent banking agreements. Generally, banks are required to maintain non-interest bearing cash reserves equal to a percentage of certain deposits. At times throughout the year, balances can exceed FDIC insurance limits. For the year ended December 31, 2007, no reserve balance was required.

Loans and allowance for loan losses – 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 year ended December 31, 2007 and the period from June 19, 2006 (date operations commenced) through December 31, 2006, salaries, employee benefits, and other expenses totaling \$119,238 and \$44,501, 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.

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

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Loans and allowance for loan losses – (continued)

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 adjusted for qualitative factors. 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.

The Bank considers a loan impaired when it is probable that all amounts of principal and interest due, according to the contractual terms of the loan agreement, will not be collected, which is the same criteria used for the transfer of loans to non-accrual status. Interest income is recognized on impaired loans in the same manner as non-accrual loans. 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, and the amount of the shortfall in relation to the principal and interest owed.

Premises and equipment – Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are provided for in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives using the straight-line method. The estimated lives used in determining depreciation are:

Equipment	2 – 5 years
Furniture and fixtures	2 – 5 years
Leasehold improvements	3 – 4 years

Leasehold improvements are amortized over the lesser of the useful life of the asset or the term of the lease. The straight-line method of depreciation is followed for all assets for financial reporting purposes, but accelerated methods are used for tax purposes. Deferred income taxes have been provided for the resulting temporary differences.

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.

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income taxes –(continued)

A valuation allowance 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.

The Bank adopted the provisions of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, on January 1, 2007. The Bank had no unrecognized tax benefits that would require an adjustment to the January 1, 2007 beginning balance of retained earnings. The Bank had no unrecognized tax benefits at January 1, 2007 and at December 31, 2007.

The Bank recognizes interest accrued and penalties related to unrecognized tax benefits in tax expense. During the year ended December 31, 2007 and the period from June 19, 2006 (date operations commenced) through December 31, 2006, 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 2006.

Net loss per common share – Net loss per common share is calculated using the weighted average number of common shares outstanding during the period.

Net loss incurred during organization – During the organizational period, the Bank incurred the following expenses:

Salaries and benefits	\$ 369,593
Consulting and professional fees	236,653
Rent and occupancy expense	102,760
Other, net	16,340
	\$ 725,346
Net loss incurred during organization	\$ 725,346

Interest earned on the funds provided by organizers and the proceeds from the sale of common stock totaling \$71,916 was used to offset the loss incurred during organization. Net loss incurred during organization totaling \$725,346 was charged to the accumulated deficit at the date the Bank commenced operations. Cash flows from pre-opening activities were as follows:

Net loss incurred during organization	\$ (725,346)
Stock issuance proceeds, net of offering costs	9,478,418
Purchase of leasehold improvements, furniture, and equipment	(281,216)
Other assets	(35,658)
Accrued expenses	70,542
Loan from organizers	400,000
Bank borrowings	700,000
	\$ 9,606,740
Cash and cash equivalents at date operations commenced	\$ 9,606,740

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 contain 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.

Advertising costs – The Bank expenses marketing costs as they are incurred. Advertising expense was \$73,885 and \$49,951 for the year ended December 31, 2007 and the period from June 19, 2006 (date operations commenced) through December 31, 2006, respectively.

Servicing Rights – Servicing rights retained are measured by allocating the carrying value of the loans between the assets sold and the interest retained, based on the relative fair value at the date of sale. Fair value is estimated using the present value of the future loan servicing fees from the right to service loans for others. In estimating fair value, management makes a number of estimates including loan prepayment speeds. The loan prepayment speeds assumption is significantly impacted by interest rates. In general, during periods of falling interest rates, loans prepay faster and the value of the servicing asset declines. Conversely, during periods of rising rates, the value of servicing rights generally increases due to slower rates of prepayment. Management uses historical prepayment rates for similar loan types in estimating prepayment speeds. Servicing rights retained are capitalized and included in the servicing asset at their allocated carrying value and amortized in proportion to, and over the period of, estimated future net servicing revenues.

Stock-based compensation – The Bank adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 123(R), *Share Based Payments*, a revision to the previously issued guidance on accounting for stock options and other forms of equity-based compensation. SFAS No. 123(R) requires companies to recognize in the income statement the grant-date fair value of stock options and other equity-based forms of compensation issued to employees and directors over the requisite service period (generally the vesting period).

The fair value of each option grant is estimated as of the grant date using an option-pricing model with the assumptions noted in the following table. The Bank utilizes a Black-Scholes pricing model for valuating its stock option grants. The assumptions used in this model include an estimate of expected volatility, based on the historical volatility of the price of similar bank stocks. The Bank estimates the number of options expected to be forfeited based on industry average forfeiture rates. The risk-free interest rates are equal to the U.S. Treasury yield at the time of the grant and commensurate with the expected term of the grant. The following are the weighted average assumptions used to estimate the value of stock options granted during 2007:

Dividend yield	0.00%
Expected volatility	17.75%
Risk-free interest rate	4.80%
Expected option term	6.5 years
Stock based compensation recorded	\$ 236,281

As the Bank has limited history of option data to evaluate, the Bank's expected option life and expected stock price volatility has been determined based on the combined evaluation of peer group data and employee data (age, expected retirement, etc.).

NOTE 2 – CASH AND DUE FROM BANKS

Cash and due from banks includes balances with the Federal Reserve and other correspondent banks. The Bank is required to maintain specified reserves by the Federal Reserve Bank. The average reserve requirements are based on a percentage of the Bank's deposit liabilities. At December 31, 2007, no reserve was required. At December 31, 2007, the Bank had cash deposits at other financial institutions in excess of the FDIC insured limits. However, as the Bank places these deposits with major financial institutions, management believes the risk of loss to be minimal.

NOTE 3 – LOANS

Major classifications of loans are as follows:

	DECEMBER 31,	
	2007	2006
Commercial	\$ 8,673,943	\$ 3,389,324
Commercial real estate	9,850,116	5,315,312
Construction and land development	3,613,607	2,760,962
Residential real estate	1,224,633	768,947
Agricultural production, land, and equipment	9,518,501	4,789,767
Consumer and other	441,324	386,243
	33,322,124	17,410,555
Allowance for loan losses	(434,217)	(217,530)
Deferred loan fees and costs, net	(167,652)	(13,700)
	\$ 32,720,255	\$ 17,179,325

SUTTER COMMUNITY BANK
NOTES TO FINANCIAL STATEMENTS

NOTE 3 – LOANS (CONTINUED)

The Bank's customers are primarily located in Sutter County. Approximately 27% of the Bank's loans are for general commercial uses including professional, retail, and small business. Approximately 30% of the Bank's loans are commercial real estate loans. Additionally, 11% of the Bank's loans are for real estate construction for residential and commercial real estate. The remaining 32% are in residential real estate, agriculture, and consumer loans. Generally, real estate loans are collateralized by real property while commercial and other loans are collateralized by funds on deposit, business, or personal assets. Repayment is generally expected from the proceeds of the sales of property for real estate construction loans and from cash flows of the borrower for other loans.

Changes in the allowance for loan losses are as follows:

	DECEMBER 31,	
	2007	2006
Balance, beginning of period	\$ 217,530	\$ -
Provision for loan losses	218,200	217,530
Loans charged off	(1,513)	-
Recoveries of loans previously charged off	-	-
Balance, end of period	<u>\$ 434,217</u>	<u>\$ 217,530</u>

The total recorded investment in impaired loans at December 31, 2007 was \$1,900,000. The average recorded investment in impaired loans was \$130,137 during 2007. Specific reserves related to impaired loans at December 31, 2007 totaled approximately \$81,000. No interest income was recognized on impaired loans, while considered impaired during 2007. There were no loans impaired at December 31, 2006 and no loans were considered impaired during the period from June 19, 2006 (date operations commenced) through December 31, 2006.

The total recorded investment in non-accrual loans was \$1,900,000 at December 31, 2007. There were no non-accrual loans at December 31, 2006. In addition, there were no loans past due greater than 90 days and still accruing interest at December 31, 2007 or 2006.

NOTE 4 – PREMISES AND EQUIPMENT

Premises and equipment consists of the following:

	DECEMBER 31,	
	2007	2006
Furniture, fixtures, and equipment	\$ 250,699	\$ 218,506
Computer software	229,311	223,285
Leasehold improvements	267,790	263,573
	747,800	705,364
Less accumulated depreciation and amortization	(311,959)	(108,296)
	\$ 435,841	\$ 597,068

Depreciation and amortization expense totaled \$203,663 and \$108,296 for the year ended December 31, 2007 and the period from June 19, 2006 (date operations commenced) through December 31, 2006, respectively.

NOTE 5 – INTEREST RECEIVABLE AND OTHER ASSETS

Interest receivable and other assets were as follows:

	DECEMBER 31,	
	2007	2006
Accrued interest and fees – loans	\$ 327,202	\$ 134,347
Servicing assets	199,932	-
Pacific Coast Bankers' Bank stock	170,000	-
Federal Home Loan Bank stock	51,100	400
Prepaid expenses and other assets	61,396	51,792
	\$ 809,630	\$ 186,539

SUTTER COMMUNITY BANK
NOTES TO FINANCIAL STATEMENTS

NOTE 6 – DEPOSITS

Customer deposits were as follows:

	DECEMBER 31,	
	2007	2006
Demand, non-interest bearing	\$ 4,981,221	\$ 3,701,756
Money market	7,898,369	4,188,043
NOW	4,614,765	1,378,873
Savings	1,306,517	1,499,654
Time – less than \$100,000	7,459,983	3,066,337
Time – greater than \$100,000	11,608,329	3,382,289
	<u>\$ 37,869,184</u>	<u>\$ 17,216,952</u>

Certificates of deposit issued and their remaining maturities are as follows:

Year ending December 31,

2008	\$ 17,582,137
2009	628,414
2010	521,565
2011	44,204
2012 and beyond	291,992
	<u>\$ 19,068,312</u>

Interest expense, net of early withdrawal penalty, recognized on interest-bearing deposits for the years ended December 31, 2007 and the period from June 19, 2006 (date operations commenced) through December 31, 2006, consisted of the following:

	2007	2006
Interest-bearing checking	\$ 65,156	\$ 1,252
Savings and club	11,326	2,998
Money market	205,619	34,354
Time deposits less than \$100,000	306,821	68,349
Time deposits greater than \$100,000	429,484	71,122
Total interest expense on deposits	<u>\$ 1,018,406</u>	<u>\$ 178,075</u>

NOTE 7 – INCOME TAXES

The provision for income taxes for the year ended December 31, 2007 and the period from June 19, 2006 (date operations commenced) through December 31, 2006 consisted of \$800 and \$0 state tax, respectively.

Deferred tax assets at December 31, 2007 and 2006, consisted of the following:

	DECEMBER 31,	
	2007	2006
Deferred tax assets:		
Net operating losses	\$ 335,000	403,000
Accrual to cash	135,000	-
Accumulated depreciation	18,000	5,000
Allowance for loan loss	160,000	71,000
Non-qualified stock options	59,000	-
	707,000	479,000
Deferred tax liabilities:		
Organization and start-up costs	(32,000)	(11,000)
Accrual to cash	-	(48,000)
Deferred loan fees	(32,000)	(18,000)
	(64,000)	(77,000)
Valuation allowance	(643,000)	(402,000)
Net deferred income tax asset	\$ -	\$ -

NOTE 7 – INCOME TAXES (CONTINUED)

As of December 31, 2007, 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. At December 31, 2007 and 2006, the Bank has federal net operating loss carryforwards totaling approximately \$818,000 and \$774,000, respectively. Additionally, at December 31, 2007 and 2006, the Bank has state net operating loss carryforwards totaling approximately \$793,000 and \$763,000, respectively. These net operating loss carryforwards will begin to expire in 2026 for federal income tax purposes and in 2016 for state income tax purposes if not previously utilized. Utilization of the net operating loss may be subject to substantial annual limitation due to ownership change limitations provided by the Internal Revenue Code and similar state provisions. Such an annual limitation could result in the expiration of net operating loss carryforwards before utilization.

The valuation allowance was increased by \$241,000 during the year ended December 31, 2007.

NOTE 8 – FINANCIAL INSTRUMENTS

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

The Bank's exposure to credit loss, in the event of non-performance by the other party to the financial instrument for 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 and conditional obligations as it does for on-balance-sheet instruments.

	<u>Contract Amount</u>
Financial instruments whose contract amounts represent credit risk:	
Undisbursed loan commitments	\$ 5,761,443
Overdraft protection	<u>319,323</u>
	<u>\$ 6,080,766</u>

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 many 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. Collateral held varies but may include accounts receivable, inventory, property, plant, and equipment, and income-producing commercial properties.

NOTE 8 – FINANCIAL INSTRUMENTS (CONTINUED)

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers.

NOTE 9 – SERVICING ASSETS

The Bank sold the guaranteed portion of certain Small Business Administration (SBA) and United States Department of Agriculture (USDA) loans during 2007 and retained the servicing rights associated with the guaranteed portion of those loans. Asset servicing rights retained are measured by allocating the carrying value of the loans between the assets sold and the interest retained, based on the relative fair value at the date of sale. Fair value is estimated using the present value of the future loan servicing fees from the right to service loans for others. The Bank utilizes the amortization method to account for the subsequent measurement of the servicing assets. The servicing assets are amortized in proportion to, and over the period of, estimated net servicing income. Additionally, the Bank assesses its servicing assets for impairment as of each financial reporting date.

During the year ended December 31, 2007, the Bank earned approximately \$16,000 in contractually specified servicing fees. Servicing fees and the amortization of the servicing asset are reported as a component of interest and fee income from loans.

Changes in the balance of the servicing asset were as follows:

Balance, January 1, 2007	\$	-
Additions for new asset servicing rights capitalized		206,788
Amortization of servicing rights		<u>(6,856)</u>
Balance, December 31, 2007	<u>\$</u>	<u>199,932</u>
Balance of loans serviced for others	\$	3,872,404
Servicing rights as a percentage of serviced loans		5.16%
Constant prepayment rate		10.08%
Discount rate		10.00%
Weighted average life in years		9.54

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NOTE 10 – RELATED-PARTY TRANSACTIONS

The Bank, in the normal course of business, makes loans to and receives deposits from its directors, officers, principal shareholders, and their associates. In management’s opinion, these transactions are on substantially the same terms as comparable transactions with other customers of the Bank.

The Bank’s related party loan activity for the year ended December 31, 2007 and the period from June 19, 2006 (date operations commenced) through December 31, 2006 is summarized below:

	<u>2007</u>	<u>2006</u>
Aggregate amount outstanding, beginning of year	\$ 181,671	\$ -
New loans or advances during the period	3,948,367	181,671
Repayments during the period	<u>(419,142)</u>	<u>-</u>
Aggregate amount outstanding, end of year	<u>\$ 3,710,896</u>	<u>\$ 181,671</u>
Loan commitments	<u>\$ 4,094,500</u>	<u>\$ 376,000</u>

Related party deposits amounted to \$3,305,510 and \$2,401,564 as of December 31, 2007 and 2006, respectively.

NOTE 11 – COMMITMENTS AND CONTINGENCIES

The Bank is obligated for rental payments under certain operating lease agreements, some of which contain renewal options and escalation clauses that provide for increased rentals. Total rental expenses for the year ended December 31, 2007 and the period from June 19, 2006 (date operations commenced) through December 31, 2006, was \$87,600 and \$43,800, respectively.

As of December 31, 2007, the future minimum rental payments under non-cancellable operating leases are as follows:

Year ending December 31,

2008	\$ 97,200
2009	<u>49,200</u>
	<u>\$ 146,400</u>

The Bank has an unsecured federal funds line totaling \$6 million with its correspondent bank, Pacific Coast Bankers’ Bank, The Independent Bankers’ Bank and Union Bank of California. There were no amounts outstanding under these facilities at December 31, 2007 or 2006.

NOTE 12 – REGULATORY MATTERS

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

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, 2007, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2007, the most recent notification from the FDIC categorized the Bank as well-capitalized under the regulatory framework for prompt corrective action. To be categorized as well-capitalized, the Bank must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the following table. There are no conditions or events since that notification that management believes have changed the Bank's category.

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NOTES TO FINANCIAL STATEMENTS

NOTE 12 – REGULATORY MATTERS (CONTINUED)

The Bank's actual capital amounts and ratios are presented in the following table.

	Actual		For capital adequacy purposes		To be well-capitalized under prompt corrective action provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(dollars in thousands)						
As of December 31, 2007:						
Total Capital (to Risk-Weighted Assets)	\$ 7,748	20.4%	\$ 3,043	≥8.0%	\$ 3,804	≥10.0%
Tier I Capital (to Risk-Weighted Assets)	\$ 7,308	19.2%	\$ 1,521	≥4.0%	\$ 2,282	≥6.0%
Tier I Capital (to Average Assets)	\$ 7,308	17.3%	\$ 1,693	≥4.0%	\$ 2,116	≥5.0%
As of December 31, 2006:						
Total Capital (to Risk-Weighted Assets)	\$ 7,992	34.6%	\$ 1,849	≥8.0%	\$ 2,311	≥10.0%
Tier I Capital (to Risk-Weighted Assets)	\$ 7,774	33.6%	\$ 924	≥4.0%	\$ 1,387	≥ 6.0%
Tier I Capital (to Average Assets)	\$ 7,774	38.4%	\$ 809	≥4.0%	\$ 1,011	≥ 5.0%

The California Financial Code restricts the total dividend payment of any state banking association in any calendar year to the lesser of the Bank's retained earnings or 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, 2007, no amounts were available for dividend distributions.

NOTE 13 – STOCK OPTION PLAN

During 2006, the Bank's shareholders approved a fixed stock option plan (the Plan) under which incentive and non-qualified stock options may be granted to key employees, directors, and others, respectively, to purchase up to 285,503 shares of the authorized and un-issued common stock of the Bank at a price equal to the fair market value on the date of grant. The Plan provides that the incentive options are exercisable in equal increments over a three-year period from the date of grant or over any other schedule approved by the Board of Directors. All incentive and non-qualified stock options expire no later than ten years from the date of grant. The Plan received regulatory approval on February 13, 2007, at which time the Bank began granting stock options.

NOTE 13 – STOCK OPTION PLAN (CONTINUED)

A summary of the status of the Bank's fixed stock option plan and changes during the year ended December 31, 2007 is presented below.

	2007	
	Shares	Weighted-Average Exercise Price
Outstanding at beginning of year	-	\$ -
Granted	258,066	\$ 10.00
Exercised	-	\$ -
Forfeited	-	\$ -
	<u>258,066</u>	<u>\$ 10.00</u>
Outstanding at end of year	<u>258,066</u>	<u>\$ 10.00</u>
Options exercisable at year end	<u>-</u>	<u>\$ -</u>
Weighted-average fair value of options granted during the year		\$ 10.00
		2007
Weighted-average fair value of options granted during the period		\$ 3.23
Intrinsic value of options exercised		\$ -
Options exercisable at year end:		-
Weighted-average exercise price		\$ -
Intrinsic value		\$ -
Weighted-average remaining contractual life		-
Options outstanding at year end:		258,066
Weighted-average exercise price		\$ 10.00
Intrinsic value		\$ -
Weighted-average remaining contractual life		9.12 years