CENTRAL VALLEY COMMUNITY BANCORP
Form 10-K
March 29, 2017
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K
x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2016
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission file number: 000-31977
CENTRAL VALLEY COMMUNITY BANCORP
(Exact name of registrant as specified in its charter)

CALIFORNIA	77-0539125
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
7100 N. Financial Dr., Suite 101, Fresno, CA	93720
(Address of principal executive offices)	(Zip Code)

559-298-1775
(Registrant's telephone number, including area code)
[None]
(Former name, former address and former fiscal year, if changed since last report)
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on which Registered
Common Stock, no par value	NASDAQ Capital Market [EXCHANGE]

Securities registered pursuant to Section 12(g) of the Act: None
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No x
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes o No x
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o	Smaller reporting company o
(Do not check if a smaller reporting company)	

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

As of June 30, 2016, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was $123,746,000 based on the price at which the stock was last sold on June 30, 2016.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, No Par Value	Outstanding at March 13, 2017	
[Common Stock, No par value]	12,195,460	shares

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive proxy statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A in connection with the 2017 Annual Meeting of Shareholders to be held on May 18, 2017 are incorporated by reference into Part III of this Report. The proxy statement will be filed with the Securities and Exchange Commission not later than 120 days after the Registrant's fiscal year ended December 31, 2016

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PART I

ITEM 1 - DESCRIPTION OF BUSINESS

General

Central Valley Community Bancorp (the Company) was incorporated on February 7, 2000 as a California corporation, for the purpose of becoming the holding company for Central Valley Community Bank (the Bank), formerly known as Clovis Community Bank, a California state chartered bank, through a corporate reorganization. In the reorganization, the Bank became the wholly-owned subsidiary of the Company, and the shareholders of the Bank became the shareholders of the Company. The Company made a decision in the first half of 2002 to change the name of its one subsidiary, Clovis Community Bank, to Central Valley Community Bank. The Company is registered as a bank holding company under the Bank Holding Company Act of 1956, as amended (the BHC Act), and is subject to supervision and regulation by the Board of Governors of the Federal Reserve System (the Board of Governors).

At December 31, 2016, we had one banking subsidiary, the Bank. The Bank is a multi-community bank that offers a full range of commercial banking services to small and medium size businesses, and their owners, managers and employees in the central valley area of California. We serve eight contiguous counties in California's central valley including Fresno County, El Dorado County, Madera County, Merced County, Sacramento County, San Joaquin County, Stanislaus County, and Tulare County, and their surrounding areas through the Bank. We do not currently conduct any operations other than through the Bank. Unless the context otherwise requires, references to us refer to the Company and the Bank on a consolidated basis. At December 31, 2016, we had consolidated total assets of approximately $1,443,323,000. See Items 7 and 8, Management's Discussion and Analysis of Financial Condition and Results of Operations, and Financial Statements.

Effective October 1, 2016, the Company and Sierra Vista Bank (SVB) completed a merger under which Sierra Vista Bank, with three full-service offices, located in Folsom and Fair Oaks (Sacramento County) and Cameron Park (El Dorado County), merged with and into the Bank. The Bank is regulated by the California Department of Business Oversight and its primary Federal regulator is the FDIC.

As of March 1, 2017, we had a total of 319 employees and 287 full time equivalent employees, including the employees of the Bank.

The Bank

The Bank was organized in 1979 and commenced business as a California state chartered bank in 1980. The deposits of the Bank are insured by the Federal Deposit Insurance Corporation (the FDIC) up to applicable limits. The Bank is not a member of the Federal Reserve System.

The Bank operates 22 full-service banking offices in Cameron Park, Clovis, Exeter, Fair Oaks, Folsom, Fresno, Kerman, Lodi, Madera, Merced, Modesto, Oakhurst, Prather, Sacramento, Stockton, Tracy, and Visalia. The Bank conducts a commercial banking business, which includes accepting demand, savings and time deposits and making commercial, real estate and consumer loans. It also provides domestic and international wire transfer services and provides safe deposit boxes and other customary banking services. The Bank also has offered Internet banking since 2000. Internet banking consists of inquiry, account status, bill paying, account transfers, and cash management. The Bank does not offer trust services or international banking services and does not currently plan to do so in the near future. The Bank has a Real Estate Division, an Agribusiness Center, and an SBA Lending Division in Fresno. All real estate related transactions are conducted and processed through the Real Estate Division, including interim construction loans for single family residences and commercial buildings. We offer permanent single family residential loans through our mortgage broker services. Our total market share of deposits in Fresno, Madera, and Tulare counties was 4.82% in 2016 compared to 4.76% in 2015 based on FDIC deposit market share information published as of June 30, 2016. Our total market share in the other counties we operate in (El Dorado, Merced, San Joaquin, Sacramento, and Stanislaus), was less than 1.00% in 2016. At December 31, 2016, we had total loans of

$756,628,000. Total commercial and industrial loans outstanding were $88,652,000, total agricultural land and production loans outstanding were $25,509,000, total real estate construction and other land loans outstanding were $69,200,000; total other real estate loans outstanding were $481,596,000, total equity loans and lines of credit were $64,494,000 and total consumer installment loans outstanding were $25,910,000. Our loans are collateralized by real estate, listed securities, savings and time deposits, automobiles, inventory, accounts receivable, machinery and equipment.

In 2005, the Company acquired the Bank of Madera County (BMC) and its two branches in Madera and Oakhurst, California.

In 2008, the Company acquired Service 1st and its banking subsidiary, S1 Bank, adding three branches located in Tracy, Stockton and Lodi, California.

In 2009, we opened a new full service office in Merced, California and relocated our Oakhurst office to a new smaller facility in a more desirable location.

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In 2010, the Company expanded the existing Modesto loan production office opened in 2007, to a larger full-service branch.
In 2013, the Company acquired Visalia Community Bank, adding four branches located in Exeter and Visalia, California.
In 2016, the Company acquired Sierra Vista Bank, adding three branches located in Folsom, Fair Oaks and Cameron Park, California.
As opposed to acquisition, opening new branches provides the Company with opportunities to expand its loan and deposit base; however, based on past experience, management expects these new offices may initially have a negative impact on earnings until the volume of business grows to cover fixed overhead expenses. The Bank anticipates opening new branches in the future. In February 2017, the Bank established the Real Estate and Agribusiness Center Branch in Fresno, California. The Bank's private banking office in Gold River, California will be closed in late April, 2017 and will open a full-service branch in Roseville, California the same weekend in April, 2017. After extensive analysis combined with the rising popularity of online and mobile banking trends, the Company chose to consolidate the Sunnyside office into our Fresno Downtown office in April 2016.
The Company terminated its interest in Central Valley Community Insurance Services, LLC (CVCIS) at the beginning of the third quarter of 2015. The Bank's interest in CVCIS was originally established in 2006 for the purpose of providing health, commercial property and casualty insurance products and services primarily to business customers. The operating results of CVCIS were not significant to the Company's operations. The termination of this entity did not have a material impact on the Company's financial statements.
Since August of 1995 the Bank has been a party to an agreement with Investment Centers of America, pursuant to which Investment Centers of America provides Bank customers with access to investment services. In connection with entering into this agreement, the Bank adopted a policy intended to comply with FDIC Regulation Section 337.4, which outlines the guidelines under which an insured non-member bank may be affiliated with a company that directly engages in the sale, distribution, or underwriting of stocks, bonds, debentures, notes, or other securities.
No individual or single group of related accounts is considered material in relation to the Bank's assets or deposits, or in relation to the overall business of the Company. However, at December 31, 2016 approximately 81.4% of our loan portfolio held for investment consisted of loans secured by real estate, including construction loans, equity loans and lines of credit and commercial loans secured by real estate and 15.1% consisted of commercial loans. See Item 7 — Management's Discussion and Analysis of Financial Condition and Results of Operations. In addition, our business activities currently are mainly concentrated in Fresno, El Dorado, Madera, Merced, Sacramento, San Joaquin, Stanislaus, and Tulare Counties in California. Consequently, our results of operations and financial condition are dependent upon the general trends in this part of the California economy and, in particular, the residential and commercial real estate markets. Further, our concentration of operations in this area of California exposes us to greater risk than other banking companies with a wider geographic base in the event of catastrophes, such as earthquakes, fires, droughts, and floods in this region, or as a result of energy shortages in California.
Our deposits are attracted from individual and commercial customers. A material portion of our deposits have not been obtained from a single person or a few persons, the loss of any one or more of which would not have a material adverse effect on our business.

Competition

The banking business in California generally, and our primary service area specifically, is highly competitive with respect to both loans and deposits, and is dominated by a relatively small number of major banks with many offices operating over a wide geographic area. Among the advantages such major banks have over us is their ability to finance wide-ranging advertising campaigns and to allocate their investment assets, including loans, to regions of higher yield and demand. Major banks offer certain services such as international banking and trust services which we do not offer directly but which we usually can offer indirectly through correspondent institutions. To compete effectively, we rely substantially on local promotional activity, personal contacts by our officers, directors and employees, referrals by our shareholders, extended hours, personalized service and our reputation in the communities we serve.

In Fresno and Madera Counties, in addition to our 10 full-service branch locations serving the Bank's primary service areas, as of June 30, 2016 there were 144 operating banking and credit union offices in our primary service area, which consists of the cities of Clovis, Fresno, Kerman, Oakhurst, Madera, and Prather, California. Prather does not contain any banking offices other than our office. The June 2016 FDIC Summary of Deposits report indicated the Company had 4.88% of the total deposits held by all depositories in Fresno County and 8.08% in Madera County. In San Joaquin County, in addition to our three full service branch locations, as of June 30, 2016 there were 101 operating banking and credit union offices. The FDIC Summary of Deposits as of June 2016 report indicated the Company had 1.57% of total deposits held by all depositories in San Joaquin County. In Merced County, in addition to our one branch, as of June 30, 2016 there were 30 operating banking and credit union offices in our primary service area. In Sacramento County, in addition to our three branches, as of June 30, 2016 there were 223 operating banking and credit union offices in our primary service area. In Stanislaus County, in addition to our one branch, there were 88 operating banking and credit union offices in our primary service area. In Tulare County, in addition to our four branches there were 54 operating banking and credit union offices in our primary service area. In El Dorado County, in addition to our one branch, there were 39 operating banking and credit union offices in our primary service area. Business activity in our primary service area is oriented toward light industry, small business and agriculture.

By virtue of their greater total capitalization, larger banks have substantially higher lending limits than we do. Legal lending limits to an individual customer are limited to a percentage of our total capital. As of December 31, 2016, the Bank's legal lending limits to individual customers were $19,561,000 for unsecured loans and $32,601,000 for unsecured and secured loans combined. As of December 31, 2016 the Bank's lending commitments in excess of $6.5 million to 21 borrowers are summarized in the table below.

	Loans	Loan Commitments		
(Dollars in thousands)	Outstanding	Secured	Unsecured	Total
Loans	$ 197,716	$170,085	$ 58,020	$228,105
Number of loans		60	26	86

For borrowers desiring loans in excess of the Bank's lending limits, the Bank seeks to make such loans on a participation basis with other financial institutions. Banks also compete with money market funds and other money market instruments, which are not subject to interest rate ceilings. In recent years, increased competition has also developed from specialized finance and non-finance companies that offer wholesale finance, credit card, and other consumer finance services, including on-line banking services and personal finance software. Competition for deposit and loan products remains strong, from both banking and non-banking firms, and affects the rates of those products as well as the terms on which they are offered to customers.

Technological innovation continues to contribute to greater competition in domestic and international financial services markets. Technological innovation has, for example, made it possible for non-depository institutions to offer customers automated transfer payment services that previously have been traditional banking products. In addition, customers now expect a choice of several delivery systems and channels, including telephone, mail, home computer, ATMs, remote deposit, mobile banking applications, self-service branches, and in-store branches.

Mergers between financial institutions have placed additional pressure on banks to streamline their operations, reduce expenses, and increase revenues to remain competitive. In addition, competition has intensified due to federal and state interstate banking laws, which permit banking organizations to expand geographically with fewer restrictions than in the past. Such laws allow banks to merge with other banks across state lines, thereby enabling banks to establish or expand banking operations in our market. The competitive environment also is significantly impacted by federal and state legislation, which may make it easier for non-bank financial institutions to compete with us.

Supervision and Regulation

GENERAL

The banking and financial services businesses in which we engage are extensively regulated under both federal and state law. Such regulation is intended, among other things, to protect depositors whose deposits are insured by the FDIC and the banking system as a whole. The monetary and fiscal policies of the federal government and the policies of regulatory agencies, particularly the Board of Governors, also influence the commercial banking business. The Board of Governors implements national monetary policies (with objectives such as curbing inflation and combating recession) by its open-market operations in United States Government securities, by adjusting the required level of reserves for financial intermediaries subject to its reserve requirements and by varying the discount rates applicable to borrowings by depository institutions. The actions of the Board of Governors in these areas influence the growth of bank loans, investments and deposits and also affect interest rates charged on loans and paid on deposits. Indirectly such actions may also affect the ability of non-bank financial institutions to compete with the Bank. The nature and impact of any future changes in monetary policies cannot be predicted.

The laws, regulations, and policies affecting financial services businesses are continuously under review by Congress and state legislatures, and federal and state regulatory agencies. From time to time, legislation is enacted which has the effect of increasing the cost of doing business, limiting or expanding permissible activities or affecting the competitive balance between banks and other financial intermediaries. Proposals to change the laws and regulations governing the operations and taxation of banks, bank holding companies and other financial intermediaries are frequently made in Congress, in the California legislature and before various bank regulatory and other professional agencies. Changes in the laws, regulations or policies that affect us cannot necessarily be predicted, but they may have a material effect on our business and earnings.

BANK HOLDING COMPANY REGULATION

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The Company, as a bank holding company, is subject to regulation under the BHC Act, and is subject to the supervision and examination of the Board of Governors. Pursuant to the BHC Act, we are required to obtain the prior approval of the Board of Governors before we may acquire all or substantially all of the assets of any bank, or ownership or control of voting shares of any bank if, after giving effect to such acquisition, we would own or control, directly or indirectly, more than five percent of such bank.

Under the BHC Act, we may not engage in any business other than managing or controlling banks or furnishing services to our subsidiaries that the Board of Governors deems to be so closely related to banking as to be a proper incident to banking. Bank holding companies that qualify and elect to be treated as “financial holding companies” may engage in a broad range of additional activities that are (i) financial in nature or incidental to such financial activities or (ii) complementary to a financial activity and do not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally. These activities include securities underwriting and dealing, insurance underwriting and making merchant banking investments. We have not elected to be treated as a financial holding company and currently have no plans to make a financial holding company election.

We are also prohibited, with certain exceptions, from acquiring direct or indirect ownership or control of more than five percent of the voting shares of any company unless the company is engaged in banking activities or the Board of Governors determines that the activity is so closely related to banking to be a proper incident to banking. The Board of Governors’ approval must be obtained before the shares of any such company can be acquired and, in certain cases, before any approved company can open new offices.

The BHC Act and regulations of the Board of Governors also impose certain constraints on the redemption or purchase by a bank holding company of its own shares of stock.

Our earnings and activities are affected by legislation, by actions of regulators, and by local legislative and administrative bodies and decisions of courts in the jurisdictions in which both the Company and the Bank conduct business. For example, these include limitations on the ability of the Bank to pay dividends to the Company and the ability of the Company to pay dividends to its shareholders. It is the policy of the Board of Governors that bank holding companies should pay cash dividends on common stock only out of income available over the past year and only if prospective earnings retention is consistent with the organization’s expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividends that undermines the bank holding company’s ability to serve as a source of strength to its banking subsidiaries. Various federal and state statutory provisions limit the amount of dividends that subsidiary banks can pay to their holding companies without regulatory approval. In addition to these explicit limitations, the federal regulatory agencies are authorized to prohibit a banking subsidiary or bank holding company from engaging in an unsafe or unsound banking practice. Depending upon the circumstances, the agencies could take the position that paying a dividend would constitute an unsafe or unsound banking practice.

In addition, banking subsidiaries of bank holding companies are subject to certain restrictions imposed by federal law in dealings with their holding companies and other affiliates. Transactions between affiliates are subject to Sections 23A and 23B of the Federal Reserve Act. Regulation W codifies interpretive guidance with respect to affiliate transactions. Subject to certain exceptions set forth in the Federal Reserve Act and Regulation W, a bank can make a loan or extend credit to an affiliate, purchase or invest in the securities of an affiliate, purchase assets from an affiliate, accept securities of an affiliate as collateral security for a loan or extension of credit to any person or company, issue a guarantee, or accept letters of credit on behalf of an affiliate only if the aggregate amount of the above transactions of such subsidiary does not exceed 10 percent of such subsidiary’s capital stock and surplus on a per affiliate basis or 20 percent of such subsidiary’s capital stock and surplus on an aggregate affiliate basis. Such transactions must be on terms and conditions that are consistent with safe and sound banking practices and on terms that are not more favorable than those provided to a non-affiliate. A bank and its subsidiaries generally may not purchase a “low-quality asset,” as that term is defined in the Federal Reserve Act, from an affiliate. Such restrictions also generally prevent a holding company and its other affiliates from borrowing from a banking subsidiary of the holding company unless the loans are secured by collateral.

A holding company and its banking subsidiaries are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit, sale or lease of property or provision of services. For example, with certain exceptions a bank may not condition an extension of credit on a customer obtaining other services provided by it, a holding company or any of its other bank affiliates, or on a promise by the customer not to obtain other services from a competitor.

The Board of Governors has cease and desist powers over parent bank holding companies and non-banking subsidiaries where actions of a parent bank holding company or its non-financial institution subsidiaries represent an unsafe or unsound practice or violation of law. The Board of Governors has the authority to regulate debt obligations (other than commercial paper) issued by bank holding companies by imposing interest ceilings and reserve requirements on such debt obligations.

We are also a bank holding company within the meaning of Section 3700 of the California Financial Code. As such, we and our subsidiaries are subject to examination by the California Department of Business Oversight (DBO). Further, we are required by the Board of Governors to maintain certain capital levels. See “Capital Standards.”

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REGULATION OF THE BANK

Banks are extensively regulated under both federal and state law. The Bank, as a California state-chartered bank, is subject to primary supervision, regulation and periodic examination by the DBO and the FDIC. The Bank is not a member of the Federal Reserve System, but is nevertheless subject to certain regulations of the Board of Governors. If, as a result of an examination of a bank, the FDIC should determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity, or other aspects of the Bank's operations are unsatisfactory or that the Bank or its management is violating or has violated any law or regulation, various remedies are available to the FDIC. Such remedies include the power to enjoin "unsafe or unsound" practices, to require affirmative action to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in capital, to restrict the growth of the Bank, to assess civil monetary penalties, to remove officers and directors, and ultimately to terminate the Bank's deposit insurance, which for a California chartered bank would result in a revocation of the Bank's charter. The DBO has many of the same remedial powers.
The Bank is a member of the FDIC, which currently insures customer deposits in each member bank to a maximum of $250,000 per depositor. For this protection, the Bank is subject to the rules and regulations of the FDIC, and, as is the case with all insured banks, may be required to pay a semi-annual statutory assessment. All of a depositors' accounts at an insured depository institution, including all non-interest bearing transactions accounts, will be insured by the FDIC up to the standard maximum deposit insurance amount of ($250,000) for each deposit insurance ownership category.
Various requirements and restrictions under the laws of the State of California and the United States affect the operations of the Bank. State and federal statutes and regulations relate to many aspects of the Bank's operations, including standards for safety and soundness, reserves against deposits, interest rates payable on deposits, loans, investments, mergers and acquisitions, borrowings, dividends, locations of branch offices, fair lending requirements, Community Reinvestment Act activities, and loans to affiliates.
Depositor Preference. In the event of the "liquidation or other resolution" of an insured depository institution, the claims of depositors of the institution, including the claims of the FDIC as subrogee of insured depositors, and certain claims for administrative expenses of the FDIC as a receiver, will have priority over other general unsecured claims against the institution. If an insured depository institution fails, insured and uninsured depositors along with the FDIC, will have priority in payment ahead of unsecured, non-deposit creditors including the parent bank holding company with respect to any extensions of credit they have made to such insured depository institution.
Brokered Deposit Restrictions. Well-capitalized institutions are not subject to limitations on brokered deposits, while an adequately capitalized institution is able to accept, renew or roll over brokered deposits only with a waiver from the FDIC and subject to certain restrictions on the yield paid on such deposits. Undercapitalized institutions are generally not permitted to accept, renew, or roll over brokered deposits. The Bank is eligible to accept brokered deposits without limitations.
Loans to Directors, Executive Officers and Principal Shareholders. The authority of the Bank to extend credit to its directors, executive officers and principal shareholders, including their immediate family members and corporations and other entities that they control, is subject to substantial restrictions and requirements under Sections 22(g) and 22(h) of the Federal Reserve Act and Regulation O promulgated thereunder, as well as the Sarbanes- Oxley Act of 2002. These statutes and regulations impose specific limits on the amount of loans the Bank may make to directors and other insiders, and specified approval procedures must be followed in making loans that exceed certain amounts. In addition, all loans the Bank makes to directors and other insiders must satisfy the following requirements:

- the loans must be made on substantially the same terms, including interest rates and collateral, as prevailing at the time for comparable transactions with persons not affiliated with the Bank;
- the Bank must follow credit underwriting procedures at least as stringent as those applicable to comparable transactions with persons who are not affiliated with the Bank; and
- the loans must not involve a greater than normal risk of non-payment or include other features not favorable to the Bank.

Furthermore, the Bank must periodically report all loans made to directors and other insiders to the bank regulators, and these loans are closely scrutinized by the regulators for compliance with Sections 22(g) and 22(h) of the Federal

Reserve Act and Regulation O. Each loan to directors or other insiders must be pre-approved by the Bank board of directors with the interested director abstaining from voting.

PAYMENT OF DIVIDENDS

THE COMPANY

Our shareholders are entitled to receive dividends when and as declared by our Board of Directors, out of funds legally available, subject to the dividends preference, if any, on preferred shares that may be outstanding, and also subject to the restrictions of the California Corporations Code.

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The principal source of cash revenue to the Company is dividends received from the Bank. The Bank's ability to make dividend payments to the Company is subject to state and federal regulatory restrictions.

THE BANK

Dividends payable by the Bank to the Company are restricted under California law to the lesser of the Bank's retained earnings, or the Bank's net income for the latest three fiscal years, less dividends paid during that period, or, with the approval of the DBO, to the greater of the retained earnings of the Bank, the net income of the Bank for its last fiscal year or the net income of the Bank for its current fiscal year.
In addition to the regulations concerning minimum uniform capital adequacy requirements described below, the FDIC has established guidelines regarding the maintenance of an adequate allowance for credit losses. Therefore, the future payment of cash dividends by the Bank will generally depend, in addition to regulatory constraints, upon the Bank's earnings during any fiscal period, the assessment of the Board of Directors of the capital requirements of the Bank and other factors, including the maintenance of an adequate allowance for credit losses.

CAPITAL STANDARDS

Banks and bank holding companies are subject to various capital requirements administered by state and federal banking agencies. Capital adequacy guidelines involve quantitative measures of assets, liabilities and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weighting and other factors.
The Board of Governors, the FDIC and other federal banking agencies have issued risk-based capital adequacy guidelines intended to provide a measure of capital adequacy that reflects the degree of risk associated with a banking organization's operations for both transactions reported on the balance sheet as assets, and transactions, such as letters of credit and recourse arrangements, which are reported as off-balance-sheet items. Under these guidelines, nominal dollar amounts of assets and credit equivalent amounts of off-balance-sheet items are multiplied by one of several risk adjustment percentages, which range from 0% for assets with low credit risk, such as certain U.S. government securities, to 100% for assets with relatively higher credit risk, such as business loans.
Prior to January 1, 2015, the guidelines included a minimum required ratio of qualifying Tier 1 capital plus Tier 2 capital to total risk weighted assets of 8% or total risk-based capital ratio, and a minimum required ratio of Tier 1 capital to total risk weighted assets of 4% or Tier 1 risk-based capital ratio. The guidelines also provided for a minimum ratio of Tier 1 capital to average assets, or "leverage ratio," of 3% for institutions having the highest regulatory rating, and 4% for all other institutions.
Tier 1 capital was generally defined as the sum of core capital elements, less goodwill and other intangible assets, accumulated other comprehensive income, disallowed deferred tax assets, and certain other deductions. The following items were defined as core capital elements: (i) common shareholders' equity; (ii) qualifying non-cumulative perpetual preferred stock and related surplus (and, in the case of holding companies, senior perpetual preferred stock issued to the U.S. Treasury Department pursuant to the Troubled Asset Relief Program); (iii) minority interest in the equity accounts of consolidated subsidiaries; and (iv) "restricted" core capital elements (which include qualifying trust preferred securities) up to 25% of all core capital elements. Tier 2 capital included the following supplemental capital elements: (i) allowance for loan and lease losses (but not more than 1.25% of an institution's risk-weighted assets); (ii) perpetual preferred stock and related surplus not qualifying as core capital; (iii) hybrid capital instruments, perpetual debt and mandatory convertible debt instruments; and (iv) term subordinated debt and intermediate-term preferred stock and related surplus. The maximum amount of Tier 2 capital was capped at 100% of Tier 1 capital.
As of December 31, 2016, the Company and the Bank's regulatory capital ratios all exceeded regulatory requirements. See Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operation.
In July 2013, the federal bank regulators approved final rules, or the capital rules, implementing the Basel Committee's December 2010 final capital framework for strengthening international capital standards, known as Basel III, and various provisions of Dodd-Frank. The capital rules substantially revise the risk-based capital requirements applicable

to bank holding companies and banks compared to the previous risk-based capital rules. The capital rules revise the components of capital and address other issues affecting the numerator in regulatory capital ratio calculations. Subject to a phase-in period for various provisions, the capital rules became effective for the Company and Bank beginning on January 1, 2015.

The Basel III capital rules: (i) introduce a new capital measure called “common equity tier 1” and related regulatory capital ratio of common equity Tier 1 to risk-weighted assets: (ii) specify that Tier 1 capital consists of common equity Tier 1 and “Additional Tier 1 capital” instruments meeting certain revised requirements; (iii) mandate that most deductions/adjustments to regulatory capital measures be made to common equity Tier 1 and not to the other components of capital; and (iv) expand the scope of the deductions from and adjustments to capital as compared to existing regulations. Under the Basel III capital rules, for most banking organizations, the most common form of Additional Tier 1 capital is noncumulative perpetual preferred stock and the most common form of Tier 2 capital is subordinated debt and a portion of the allowance for loan and lease losses, which in each case, are subject to the Basel III capital rules' specific requirements. Under the Basel III capital rules, the following are the initial minimum capital ratios applicable to the Company and Bank as of January 1, 2015:

* 4.5% Common equity Tier 1 to risk-weighted assets;
* 6.0% Tier 1 capital (common equity Tier 1 plus Additional Tier 1 capital) to risk-weighted assets;
* 8.0% total capital (Tier 1 capital plus Tier 2 capital) to risk-weighted assets; and
* 4.0% Tier 1 leverage ratio

The Basel III capital rules also introduce a new "capital conversation buffer" for banking organizations to maintain a common equity Tier 1 ratio more than 2.5% above these minimum risk-weighted asset ratios. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of common equity Tier 1 to risk-weighted assets above the minimum but below the capital conservation buffer will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall. The implementation of the capital conservation buffer was phased in beginning on January 1, 2016 at 0.625% and will be phased in over a four-year period (increasing by that amount on each subsequent January 1, until it reaches 2.5% on January 1, 2019). Thus, when fully phased-in on January 1, 2019, the Company and Bank will be required to maintain this additional capital conservation buffer of 2.5% of common equity Tier 1 resulting in the following minimum capital ratios:

* 4.5% Common equity Tier 1 to risk-weighted assets, plus the capital conversation buffer, or a minimum ratio of common equity Tier 1 to risk weighted assets of at least 7%;
* 6.0% Tier 1 capital to risk-weighted assets, plus the capital conservation buffer, or a minimum Tier 1 capital ratio of at least 8.5%;
* 8.0% Total capital to risk-weighted assets, plus the capital conservation buffer, or a minimum total capital ratio of at least 10.5%; and
* 4.0% Tier 1 leverage ratio

The Basel III capital rules provide for a number of deductions from and adjustments to common equity Tier 1. These include, for example, the requirement that: (i) mortgage servicing rights; (ii) deferred tax assets arising from temporary differences that could not be realized through net operating loss carrybacks, and (iii) significant investments in non-consolidated financial entities be deducted from common equity Tier 1 to the extent that any one such category exceeds 10% of common equity Tier 1 or all such items, in the aggregate, exceed 15% of common equity Tier 1. Implementation of the deductions and other adjustments to common equity Tier 1 began on January 1, 2015 and will be phased-in over a four-year period (beginning at 40% on January 1, 2015 and an additional 20% per year thereafter). In addition, the Company and Bank made a one-time election as permitted under the Basel III capital rules to continue the current capital standards under which the effects of accumulated other comprehensive income or loss ("AOCI") items included in shareholders' equity (for example, unrealized gains or losses on securities held in the available-for-sale portfolio) under U.S. GAAP are excluded for the purposes of determining regulatory capital ratios. The Company and Bank made this election in order to avoid significant variations in the level of capital depending upon the impact of interest rate fluctuations on the fair value of its available-for-sale securities portfolio.

The capital rules also increase the required capital for certain categories of assets, including higher-risk construction real estate loans, certain past-due or nonaccrual loans, and certain exposures related to securitizations. The capital rules adopt the same risk weightings for residential mortgages that existed under previous risk-based capital rules. Based on existing capital levels at December 31, 2016 and 2015, the Company and Bank meet all capital adequacy requirements under the Basel III capital rules on a fully phased-in basis. See Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operation.

A bank that does not achieve and maintain the required capital levels may be issued a capital directive by the FDIC to ensure the maintenance of required capital levels. As discussed above, the Company and the Bank are required to maintain certain levels of capital. The regulatory capital guidelines as well as the actual capitalization, exclusive of the capital conservation buffer, for the Bank and the Company on a consolidated basis as of December 31, 2016 are as follows:

	Requirement	Actual

	Adequately Capitalized	For the Bank to be Well Capitalized	Bank	Company
Total risk-based capital ratio	8.00%	10.00 %	13.57%	13.72 %
Tier 1 risk-based capital ratio	6.00%	8.00 %	12.59%	12.74 %
Common equity Tier 1 ratio	4.50%	6.50 %	12.59%	12.48 %
Tier 1 leverage capital ratio	4.00%	5.00 %	8.64 %	8.75 %

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VOLCKER RULE

The final rules adopted on December 10, 2013, to implement a part of the Dodd-Frank Act commonly referred to as the “Volcker Rule”, would prohibit insured depository institutions and companies affiliated with insured depository institutions (“banking entities”) from engaging in short-term proprietary trading of certain securities, derivatives, commodity futures and options on these instruments, for their own account. The final rules also impose limits on banking entities’ investments in, and other relationships with, hedge funds or private equity funds. These rules became effective on April 1, 2014. Certain collateralized debt obligations (“CDOs”), securities backed by trust preferred securities which were initially defined as covered funds subject to the investment prohibitions, have been exempted to address the concern that many community banks holding such CDOs securities may have been required to recognize significant losses on those securities.

Like the Dodd-Frank Act, the final rules provide exemptions for certain activities, including market making, underwriting, hedging, trading in government obligations, insurance company activities, and organizing and offering hedge funds or private equity funds. The final rules also clarify that certain activities are not prohibited, including acting as agent, broker, or custodian.

The compliance requirements under the final rules vary based on the size of the banking entity and the scope of activities conducted. Banking entities with significant trading operations will be required to establish a detailed compliance program and their CEOs will be required to attest that the program is reasonably designed to achieve compliance with the final rule. Independent testing and analysis of an institution’s compliance program will also be required. The final rules reduce the burden on smaller, less-complex institutions by limiting their compliance and reporting requirements. Additionally, a banking entity that does not engage in covered trading activities will not need to establish a compliance program. The Company and the Bank held no investment positions at December 31, 2016 that were subject to the final rule. Therefore, while these new rules may require us to conduct certain internal analysis and reporting, we believe that they will not require any material changes in our operations or business.

USA PATRIOT ACT

On October 26, 2001, President Bush signed the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT) Act of 2001. The USA PATRIOT Act also made significant changes to the Bank Secrecy Act. Under the USA PATRIOT Act, financial institutions are subject to prohibitions against specified financial transactions and account relationships as well as enhanced due diligence and of identifying customers when establishing new relationships and standards in their dealings with foreign financial institutions and foreign customers. For example, the enhanced due diligence policies, procedures, and controls generally require financial institutions to take reasonable steps:

* To conduct enhanced scrutiny of account relationships to guard against money laundering and report any suspicious transaction;
* To ascertain the identity of the nominal and beneficial owners of, and the source of funds deposited into, each account as needed to guard against money laundering and report any suspicious transactions;
* To ascertain for any foreign bank, the shares of which are not publicly traded, the identity of the owners of the foreign bank, and the nature and extent of the ownership interest of each such owner; and
* To ascertain whether any foreign bank provides correspondent accounts to other foreign banks and, if so, the identity of those foreign banks and related due diligence information.

Under the USA PATRIOT Act, financial institutions are to establish anti-money laundering programs to enhance their Bank Secrecy Act program. The USA PATRIOT Act sets forth minimum standards for these programs, including:

* The development of internal policies, procedures, and controls;
* The designation of a compliance officer;
* An ongoing employee training program; and

* An independent audit function to test the programs.
Bank management believes that the Bank is currently in compliance with the US PATRIOT Act.

OFFICE OF FOREIGN ASSETS CONTROL REGULATION

The U.S. Treasury Department's Office of Foreign Assets Control ("OFAC"), administers and enforces economic and trade sanctions against targeted foreign countries and regimes under authority of various laws, including designated foreign countries, nationals and others. OFAC publishes lists of specially designated targets and countries. The Company and the Bank are responsible for, among other things, blocking accounts of and transactions with such targets and countries, prohibiting unlicensed trade and financial transactions with them and reporting blocked transactions after their occurrence. Failure to comply with these

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sanctions could have serious legal and reputational consequences, including causing applicable bank regulatory authorities not to approve merger or acquisition transactions when regulatory approval is required or to prohibit such transactions even if approval is not required.

SAFEGUARDING OF CUSTOMER INFORMATION AND PRIVACY

The Federal Reserve and other bank regulatory agencies have adopted guidelines for safeguarding confidential, personal customer information. These guidelines require financial institutions to create, implement and maintain a comprehensive written information security program designed to ensure the security and confidentiality of customer information, protect against any anticipated threats or hazards to the security or integrity of such information and protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer. The Bank has adopted a customer information security program to comply with such requirements.

Financial institutions are also required to implement policies and procedures regarding the disclosure of nonpublic personal information about consumers to non-affiliated third parties. In general, financial institutions must provide explanations to consumers on policies and procedures regarding the disclosure of such nonpublic personal information and, except as otherwise required by law, prohibits disclosing such information. The Bank has implemented privacy policies addressing these restrictions which are distributed regularly to all existing and new customers of the Bank.

COMMUNITY REINVESTMENT ACT

The Community Reinvestment Act (CRA) is intended to encourage insured depository institutions, while operating safely and soundly, to help meet the credit needs of their communities. The CRA specifically directs the federal bank regulatory agencies, in examining insured depository institutions, to assess their record of helping to meet the credit needs of their entire community, including low-and moderate-income neighborhoods, consistent with safe and sound banking practices. The CRA further requires the agencies to take a financial institution’s record of meeting its community credit needs into account when evaluating applications for, among other things, domestic branches, consummating mergers or acquisitions or holding company formations. The federal banking agencies have adopted regulations which measure a bank’s compliance with its CRA obligations on a performance based evaluation system. This system bases CRA ratings on an institution’s actual lending service and investment performance rather than the extent to which the institution conducts needs assessments, documents community outreach or complies with other procedural requirements . The ratings range from “outstanding” to a low of “substantial noncompliance.” The Bank had a CRA rating of “satisfactory” as of its most recent regulatory examination.

CONSUMER PROTECTION LAWS AND REGULATIONS

The bank regulatory agencies are focusing greater attention on compliance with consumer protection laws and their implementing regulations. Examination and enforcement have become more intense in nature, and insured institutions have been advised to monitor carefully compliance with such laws and regulations. The Bank is subject to many federal consumer protection statutes and regulations, some of which are discussed below.

The Equal Credit Opportunity Act (ECOA) generally prohibits discrimination in any credit transaction, whether for consumer or business purposes, on the basis of race, color, religion, national origin, sex, marital status, age, receipt of income from public assistance programs, or good faith exercise of any rights under the Consumer Credit Protection Act.

The Truth in Lending Act (TILA) is designed to ensure that credit terms are disclosed in a meaningful way so that consumers may compare credit terms more readily and knowledgeably. As a result of the TILA, all creditors must use the same credit terminology to express rates and payments, including the annual percentage rate, the finance charge, the amount financed, the total of payments and the payment schedule, among other things.

The Fair Housing Act (FH Act) regulates many practices, including making it unlawful for any lender to discriminate in its housing-related lending activities against any person because of race, color, religion, national origin, sex, handicap or familial status. A number of lending practices have been found by the courts to be, or may be considered, illegal under the FH Act, including some that are not specifically mentioned in the FH Act itself.

The Home Mortgage Disclosure Act (HMDA) grew out of public concern over credit shortages in certain urban neighborhoods and provides public information that will help show whether financial institutions are serving the housing credit needs of the neighborhoods and communities in which they are located. The HMDA also includes a “fair lending” aspect that requires the collection and disclosure of data about applicant and borrower characteristics as a way of identifying possible discriminatory lending patterns and enforcing anti-discrimination statutes.

Finally, the Real Estate Settlement Procedures Act (RESPA) requires lenders to provide borrowers with disclosures regarding the nature and cost of real estate settlements. Also, RESPA prohibits certain abusive practices, such as kickbacks,

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and places limitations on the amount of escrow accounts. Penalties under the above laws may include fines, reimbursements and other civil money penalties.

Due to heightened regulatory concern related to compliance with the CRA, TILA, FH Act, ECOA, HMDA and RESPA generally, the Bank may incur additional compliance costs or be required to expend additional funds for investments in its local community.

CONSUMER FINANCIAL PROTECTION BUREAU

Dodd-Frank created a new, independent federal agency, the Consumer Financial Protection Bureau (CFPB), which was granted broad rulemaking, supervisory and enforcement powers under various federal consumer financial protection laws. The CFPB is also authorized to engage in consumer financial education, track consumer complaints, request data and promote the availability of financial services to underserved consumers and communities. Although all institutions are subject to rules adopted by the CFPB and examination by the CFPB in conjunction with examinations by the institution’s primary federal regulator, the CFPB has primary examination and enforcement authority over institutions with assets of $10 billion or more. The FDIC has primary responsibility for examination of the Bank and enforcement with respect to federal consumer protection laws so long as the Bank has total consolidated assets of less than $10 billion, and state authorities are responsible for monitoring our compliance with all state consumer laws. The CFPB also has the authority to require reports from institutions with less than $10 billion in assets, such as the Bank, to support the CFPB in implementing federal consumer protection laws, supporting examination activities, and assessing and detecting risks to consumers and financial markets.

The consumer protection provisions of Dodd-Frank and the examination, supervision and enforcement of those laws and implementing regulations by the CFPB have created a more intense and complex environment for consumer finance regulation. The CFPB has significant authority to implement and enforce federal consumer finance laws, including the Truth in Lending Act, the Equal Credit Opportunity Act and new requirements for financial services products provided for in Dodd-Frank, as well as the authority to identify and prohibit unfair, deceptive or abusive acts and practices. The review of products and practices to prevent such acts and practices is a continuing focus of the CFPB, and of banking regulators more broadly. The ultimate impact of this heightened scrutiny is uncertain but could result in changes to pricing, practices, products and procedures. It could also result in increased costs related to regulatory oversight, supervision and examination, additional remediation efforts and possible penalties. In addition, Dodd-Frank provides the CFPB with broad supervisory, examination and enforcement authority over various consumer financial products and services, including the ability to require reimbursements and other payments to customers for alleged legal violations and to impose significant penalties, as well as injunctive relief that prohibits lenders from engaging in allegedly unlawful practices. The CFPB also has the authority to obtain cease and desist orders providing for affirmative relief or monetary penalties. Dodd-Frank does not prevent states from adopting stricter consumer protection standards. State regulation of financial products and potential enforcement actions could also adversely affect our business, financial condition or results of operations.

DEPOSIT INSURANCE

The FDIC is an independent federal agency that insures deposits up to prescribed statutory limits of federally insured banks and savings institutions and safeguards the safety and soundness of the banking and savings industries. The FDIC insures the Bank’s customer deposits through the Deposit Insurance Fund (the “DIF”) up to prescribed limits for each depositor. Pursuant to Dodd-Frank, the maximum deposit insurance amount was increased to $250,000. The amount of FDIC assessments paid by each DIF member institution is based on its relative risk of default as measured by regulatory capital ratios and other supervisory factors.

The Bank is subject to deposit insurance assessments to maintain the DIF. In October 2010, the FDIC adopted a revised restoration plan to ensure that the DIF’s designated reserve ratio (“DRR”) reaches 1.35% of insured deposits by September 30, 2020, the deadline mandated by Dodd-Frank. However, financial institutions like the Bank with assets of less than $10 billion are exempted from the cost of this increase. The restoration plan proposed an increase in the

DRR to 2% of estimated insured deposits as a long-term goal for the fund. The FDIC also proposed future assessment rate reductions in lieu of dividends when the DRR reaches 1.5% or greater.

We are generally unable to control the amount of premiums that we are required to pay for FDIC insurance. If there are additional bank or financial institution failures or if the FDIC otherwise determines, we may be required to pay even higher FDIC premiums than the recently increased levels. These announced increases and any future increases in FDIC insurance premiums may have a material and adverse effect on our earnings and could have a material adverse effect on the value of or market for our common stock.

In addition to DIF assessments, banks must pay quarterly assessments that are applied to the retirement of Financing Corporation ("FICO") bonds issued in the 1980's to assist in the recovery of the savings and loan industry. The FICO assessment amount fluctuates quarterly, but was 0.00140% of average total assets less average tangible equity for the third quarter of 2016. As of the date of this report, the Company had not received the FICO assessment for the fourth quarter of 2016. Those assessments will continue until the Financing Corporation bonds mature in 2019.

The FDIC may terminate a depository institution’s deposit insurance upon a finding that the institution’s financial condition is unsafe or unsound or that the institution has engaged in unsafe or unsound practices that pose a risk to the DIF or that may prejudice the interest of the bank’s depositors. The termination of deposit insurance for a bank would also result in the revocation of the bank’s charter by the DBO.

CALIFORNIA FINANCIAL INFORMATION PRIVACY ACT/FAIR CREDIT REPORTING ACT

In 1970, the Federal Fair Credit Reporting Act (the FCRA) was enacted to insure the confidentiality, accuracy, relevancy and proper utilization of consumer credit report information. Under the framework of the FCRA, the United States has developed a highly advanced and efficient credit reporting system. The information contained in that broad system is used by financial institutions, retailers and other creditors of every size in making a wide variety of decisions regarding financial transactions. Employers and law enforcement agencies have also made wide use of the information collected and maintained in databases made possible by the FCRA. The FCRA affirmatively preempts state law in a number of areas, including the ability of entities affiliated by common ownership to share and exchange information freely, and the requirements on credit bureaus to reinvestigate the contents of reports in response to consumer complaints, among others.

The California Financial Information Privacy Act, which was enacted in 2003, requires a financial institution to provide specific information to a consumer related to the sharing of that consumer’s nonpublic personal information. The Act allows a consumer to direct the financial institution not to share his or her nonpublic personal information with affiliated or nonaffiliated companies with which a financial institution has contracted to provide financial products and services, and requires that permission from each such consumer be acquired by a financial institution prior to sharing such information.

The FACT Act, (Fair and Accurate Credit Transaction Act) became law in 2003, effectively extending and amending provisions of the Fair Credit Reporting Act (FCRA). The FACT Act created many new responsibilities for consumer reporting agencies and users of consumer reports. It contains many new consumer disclosure requirements as well as provisions to address identity theft.

CHECK 21 ACT

On December 22, 2003, the Board of Governors amended Regulation CC and its commentary to implement the Check Clearing for the 21st Century Act (Check 21 Act). The Check 21 Act became effective on October 28, 2004.

To facilitate check truncation and electronic check exchange, the Check 21 Act authorizes a new negotiable instrument called a “substitute check” and provides that a properly prepared substitute check is the legal equivalent of the original check for all purposes. A substitute check is a paper reproduction of the original check that can be processed just like the original check. The Check 21 Act does not require any bank to create substitute checks or to accept checks electronically. The amendments: 1) set forth the requirements of the Check 21 Act that applies to banks; 2) provide a model disclosure and model notices relating to substitute checks; and 3) set forth bank endorsement and identification requirements for substitute checks.

The Bank has been imaging its customers’ checks since 2000. Check 21 Act has had limited impact on the Bank.

Other

Other legislation which has been or may be proposed to the United States Congress and the California Legislature and regulations which may be proposed by the Board of Governors, FDIC and the DBO may affect our business. It cannot be predicted whether any pending or proposed legislation or regulations will be adopted or the effect such legislation or regulations may have upon our business.

ADDITIONAL INFORMATION

Copies of the annual report on Form 10-K for the year ended December 31, 2016 may be obtained without charge upon written request to Dave Kinross, Chief Financial Officer, at the Company's administrative offices, 7100 N. Financial Dr., Suite 101, Fresno, CA 93720. The Form 10-K is available on our website: www.cvcb.com.
Inquiries regarding Central Valley Community Bancorp's accounting, internal controls or auditing concerns should be directed to Steven D. McDonald, chairman of the Board of Directors' Audit Committee, at steve.mcdonald@cvcb.com or anonymously at www.ethicspoint.com or EthicsPoint, Inc. at 1-866-294-9588.
General inquiries about Central Valley Community Bancorp or Central Valley Community Bank should be directed to LeAnn Ruiz, Assistant Corporate Secretary at 1-800-298-1775.

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ITEM 1A - RISK FACTORS

An investment in our common stock is subject to risks inherent to our business. The material risks and uncertainties that Management believes may affect our business are described below. Before making an investment decision, you should carefully consider the risks and uncertainties described below together with all of the other information included or incorporated by reference in this Annual Report. The risks and uncertainties described below are not the only ones facing our business. Additional risks and uncertainties that Management is not aware of or focused on or that Management currently deems immaterial may also impair our business operations. This Annual Report is qualified in its entirety by these risk factors.

If any of the following risks actually occur, our financial condition and results of operations could be materially and adversely affected. If this were to happen, the value of our common stock could decline significantly, and you could lose all or part of your investment.

Worsening economic conditions could adversely affect our business.
The economic conditions in the United States in general and within California and in our operating markets suffered from the economic downturn of 2007 through 2010. The availability of credit and consumer spending, real estate values, and consumer confidence have all been adversely affected by the economic downturn. Unemployment nationwide, in California, and in our operating markets increased significantly through this economic downturn. Although unemployment statistics have returned to more normal historical levels, there is no certainty that these levels will continue in the future. The volatility of the capital markets and the credit, capital and liquidity problems confronting the U.S. financial system have not been resolved despite massive government expenditures and legislative efforts to stabilize the U.S. financial system. While economic conditions have improved, the sustainability of the economic recovery remains uncertain.
The Bank conducts banking operations principally in California's Central Valley. As a result, our financial condition, results of operations and cash flows are subject to changes in the economic conditions in California's Central Valley. Our business results are dependent in large part upon the business activity, population, income levels, deposits and real estate activity in the Central Valley, and adverse economic conditions could have a material adverse effect upon us. In addition, the Central Valley remains largely dependent on agriculture. A downturn in agriculture and agricultural related business could indirectly and adversely affect our results of operations and financial condition.
We can provide no assurance that economic conditions in the United States in general and in the State of California and within our operating markets will not further deteriorate or that such deterioration will not materially and adversely affect us. A further deterioration in economic conditions locally, regionally or nationally could result in a further economic downturn in the Central Valley with the following consequences, any of which could further adversely affect our business:

- loan delinquencies and defaults may increase;
- problem assets and foreclosures may increase;
- demand for our products and services may decline;
- low cost or noninterest bearing deposits may decrease;
- collateral for loans may decline in value, in turn reducing customers' borrowing power, and reducing the value of assets and collateral as sources of repayment of existing loans;
- foreclosed assets may not be able to be sold;
- volatile securities market conditions could adversely affect valuations of investment portfolio assets; and
- reputational risk may increase due to public sentiment regarding the banking industry.

Governmental monetary policies and intervention to stabilize the U.S. financial system may affect our business and are beyond our control.
The business of banking is affected significantly by the fiscal and monetary policies of the Federal government and its agencies. Such policies are beyond our control. We are particularly affected by the policies established by the Federal

Reserve Board in relation to the supply of money and credit in the United States. The instruments of monetary policy available to the Federal Reserve Board can be used in varying degrees and combinations to directly affect the availability of bank loans and deposits, as well as the interest rates charged on loans and paid on deposits, and this can and does have a material effect on our business.

Tightening of credit markets and liquidity risk could adversely affect our business, financial condition and results of operations.
A tightening of the credit markets or any inability to obtain adequate funds for continued loan growth at an acceptable cost could adversely affect our asset growth and liquidity position and, therefore, our earnings capability. In addition to core deposit growth, maturity of investment securities and loan and lease payments, we also rely on alternative funding sources including unsecured borrowing lines with correspondent banks, secured borrowing lines with the Federal Home Loan Bank of

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San Francisco and the Federal Reserve Bank of San Francisco, and public time certificates of deposits. Our ability to access these sources could be impaired by deterioration in our financial condition as well as factors that are not specific to us, such as a disruption in the financial markets or negative views and expectations for the financial services industry or serious dislocation in the general credit markets. In the event such a disruption should occur, our ability to access these sources could be adversely affected, both as to price and availability, which would limit or potentially raise the cost of the funds available to us.

We have a concentration risk in real estate related loans.
At December 31, 2016, $615 million, or 81.40% of our total loan and lease portfolio, consisted of real estate related loans. Substantially all of our real property collateral is located in our operating markets in the Central Valley in California. In the past decade, deteriorating economic conditions in California and in our operating markets adversely affected commercial and residential real estate values; a return of such conditions could harm the performance of the Company's real estate related loans, as could a continuing substantial decline in commercial and residential real estate values in our primary market areas as a result of natural disasters such as earthquakes, fires, drought, and floods. Such a decline in values could have an adverse impact on us by limiting repayment of defaulted loans through sale of commercial and residential real estate collateral and by a likely increase in the number of defaulted loans to the extent that the financial condition of our borrowers is adversely affected by such a decline in values. The adverse effects of the foregoing matters upon our real estate portfolio could necessitate a material increase in the provision for loan and lease losses.
In addition, banking regulators now give commercial real estate loans extremely close scrutiny due to risks relating to the cyclical nature of the real estate market, and related risks for lenders with high concentrations of such loans. The regulators have required banks with relatively high levels of commercial real estate loans to implement enhanced underwriting standards, internal controls, risk management policies and portfolio stress testing, which has resulted in higher allowances for possible loan losses. Any increase in our allowance for loan losses would adversely affect our net income, and any requirement that we maintain higher capital levels could adversely impact our business, results of operations and financial condition

If our allowance for credit losses is not sufficient to cover actual loan losses, our earnings could decrease.
Our loan customers may not repay their loans according to the terms of these loans, and the collateral securing the payment of these loans may be insufficient to assure repayment. We may experience significant credit losses that could have a material adverse effect on our operating results. We make various assumptions and judgments about the collectability of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of our loans. In determining the size of the allowance, we rely on our experience and our evaluation of economic conditions. If our assumptions prove to be incorrect, our current allowance may not be sufficient to cover future loan losses and adjustments may be necessary to allow for different economic conditions or adverse developments in our loan portfolio. Significant additions to our allowance would materially decrease our net income.
In addition, federal and state regulators periodically review our allowance for credit losses and may require us to increase our provision for credit losses or recognize further loan charge-offs, based on judgments different than those we make. Any increase in our allowance or charge-offs as required by these regulatory agencies could have a negative effect on us.

Non-performing assets take significant time to resolve and adversely affect our results of operations and financial condition.
At December 31, 2016, our non-performing loans and leases were 0.29% of total loans and leases compared to 0.40% at December 31, 2015, and 2.45% at December 31, 2014, and our non-performing assets (which include foreclosed real estate) were 0.18% of total assets compared to 0.19% at December 31, 2015. The allowance for credit losses as a percentage of non-performing loans and leases was 427.80% as of December 31, 2016 compared to 398.26% at December 31, 2015. Non-performing assets adversely affect our net income in various ways. We generally do not

record interest income on non-performing loans or other real estate owned, thereby adversely affecting our income and increasing our loan administration costs. When we take collateral in foreclosures and similar proceedings, we are required to mark the related asset to the then fair value of the collateral, which may ultimately result in a loss. An increase in the level of non-performing assets increases our risk profile and may impact the capital levels our regulators believe are appropriate in light of the ensuing risk profile, which could result in a request to reduce our level of non-performing assets. When we reduce problem assets through loan sales, workouts, restructurings and otherwise, decreases in the value of the underlying collateral, or in these borrowers' performance or financial condition, whether or not due to economic and market conditions beyond our control, could adversely affect our business, results of operations and financial condition. In addition, the resolution of non-performing assets requires significant commitments of time from management and our directors, which can be detrimental to the performance of their other responsibilities. There can be no assurance that we will not experience future increases in non-performing assets or that the disposition of such non-performing assets will not adversely affect our profitability.

Our focus on lending to small to mid-sized community-based businesses may increase our credit risk.
Commercial real estate and commercial business loans generally are considered riskier than single-family residential loans because they have larger balances to a single borrower or group of related borrowers. Commercial real estate and

commercial business loans involve risks because the borrowers' ability to repay the loans typically depends primarily on the successful operation of the businesses or the properties securing the loans. Most of the Bank's commercial real estate and commercial business loans are made to small to medium sized businesses who may have a heightened vulnerability to economic conditions. Moreover, a portion of these loans have been made by us in recent years and the borrowers may not have experienced a complete business or economic cycle. Furthermore, the deterioration of our borrowers' businesses may hinder their ability to repay their loans with us, which could adversely affect our results of operations.

Fluctuations in interest rates could reduce our profitability.

We realize income primarily from the difference between interest earned on loans and securities and the interest paid on deposits and borrowings. We expect that we will periodically experience "gaps" in the interest rate sensitivities of our assets and liabilities, meaning that either our interest-bearing liabilities will be more sensitive to changes in market interest rates than our interest-earning assets, or vice versa. In either event, if market interest rates should move contrary to our position, this "gap" will work against us, and our earnings may be negatively affected.

We are unable to predict fluctuations of market interest rates, which are affected by the following factors outside our control:

- inflation;
- recession;
- competition;
- a rise in unemployment;
- tightening money supply;
- international disorder; and
- instability in domestic and foreign financial markets.

Our asset/liability management strategy, which is designed to address the risk from changes in market interest rates and the shape of the yield curve, may not prevent changes in interest rates from having a material adverse effect on our results of operations and financial condition. In recent years, we have shifted our mix of assets from consisting primarily of loans to a more balanced mix of loans and securities. The value of these securities is subject to interest rate risk, which we must monitor and manage successfully in order to prevent declines in value of these assets if interest rates rise in the future.

Additionally, increasing levels of competition in the banking and financial services business may decrease our net interest spread as well as net interest margin by forcing us to offer lower lending interest rates and pay higher deposit interest rates. Although we believe our current level of interest rate sensitivity is reasonable, significant fluctuations in interest rates (such as a sudden and substantial increase in Prime and Overnight Fed Funds rates) as well as increasing competition may require us to increase rates on deposits at a faster pace than the yield we receive on interest earning assets increases. The impact of any sudden and substantial move in interest rates and/or increased competition may have an adverse effect on our business, results of operations and financial condition as our net interest income (including the net interest spread and margin) may be negatively impacted.

Furthermore, a sustained decrease in market interest rates could adversely affect our earnings. When interest rates decline borrowers tend to refinance higher-rate, fixed-rate loans to lower rates, prepaying their existing loans. Under those circumstances we would not be able to reinvest those prepayments in assets earning interest rates as high as the rates on the prepaid loans. In addition, our commercial real estate and commercial loans, which carry interest rates that, in general, adjust in accordance with changes in the prime rate, will adjust to lower rates. We are also significantly affected by the level of loan demand available in our market. The inability to make sufficient loans directly affects the interest income we earn. Lower loan demand will generally result in lower interest income realized as we place funds in lower yielding investments.

Competition with other financial institutions could adversely affect our profitability.

We face vigorous competition from banks and other financial institutions, including savings institutions, finance companies and credit unions. A number of these banks and other financial institutions have substantially greater resources and lending limits, larger branch systems and a wider array of banking services. To a limited extent, we also compete with other providers of financial services, such as money market mutual funds, brokerage firms, consumer finance companies and insurance companies. This competition may reduce or limit our margins on banking services, reduce our market share and adversely affect our results of operations and financial condition. Additionally, we face competition primarily from other banks in attracting, developing and retaining qualified banking professionals.

Recently, several new banks have opened in our service areas. We are seeing price competition from these new banks, as they work to establish their markets. The existence of competitors, large and small, is a normal and expected part of our operations, but in responding to the particular short-term impact on business of new entrants to the marketplace, we could see a negative impact on revenue and income. Moreover, these near term impacts could be accentuated by the seasonal impact on revenue and income generated by the borrowing and deposit habits of the agricultural community that comprises a significant component of our customer base.

Technology is continually changing and we must effectively implement new technologies.

Our future growth prospects will be highly dependent on our ability to implement changes in technology that affect the delivery of banking services such as the increased demand for computer access to bank accounts and the availability to perform banking transactions electronically. Our ability to compete will depend upon our ability to continue to adapt technology on a timely and cost-effective basis to meet such demands. In addition, our business and operations could be susceptible to adverse effects from computer failures, communication and energy disruption, and activities such as fraud of unethical individuals with the technological ability to cause disruptions or failures of our data processing system.

If our information systems were to experience a system failure, our business and reputation could suffer.
We rely heavily on communications and information systems to conduct our business. The computer systems and network infrastructure we use could be vulnerable to unforeseen problems. Our operations are dependent upon our ability to minimize service disruptions by protecting our computer equipment, systems, and network infrastructure from physical damage due to fire, power loss, telecommunications failure or a similar catastrophic event. We have protective measures in place to prevent or limit the effect of the failure or interruption of our information systems, and will continue to upgrade our security technology and update procedures to help prevent such events. However, if such failures or interruptions were to occur, they could result in damage to our reputation, a loss of customers, increased regulatory scrutiny, or possible exposure to financial liability, any of which could have a material adverse effect on our business, financial condition and results of operations.

The occurrence of fraudulent activity, breaches or failures of our information security controls or cybersecurity-related incidents could have a material adverse effect on our business, financial condition and results of operations.
As a financial institution we are susceptible to fraudulent activity, information security breaches and cybersecurity-related incidents that may be committed against us or our customers which may result in financial losses or increased costs to us or our customers, disclosure or misuse of our information or our customer information, misappropriation of assets, privacy breaches against our customers, litigation, or damage to our reputation. Such fraudulent activity may take many forms, including check fraud, electronic fraud, wire fraud, on-line banking, phishing, social engineering and other dishonest acts. Information security breaches and cybersecurity-related incidents may include fraudulent or unauthorized access to systems used by us or our customers, denial or degradation of service attacks, and malware or other cyber-attacks. In recent periods, there continues to be a rise in electronic fraudulent activity, security breaches and cyber-attacks within the financial services industry, especially in the commercial banking sector due to cyber criminals targeting commercial bank accounts. Consistent with industry trends we have also experienced an increase in attempted electronic fraudulent activity, security breaches and cybersecurity-related incidents in recent periods. Moreover, in recent periods, several large corporations, including financial institutions and retail companies, have suffered major data breaches, in some cases exposing not only confidential and proprietary corporate information, but also sensitive financial and other personal information of their customers and employees and subjecting them to potential fraudulent activity. Some of our customers may have been affected by these breaches which increase their risks of identity theft, credit card fraud and other fraudulent activity that could involve their accounts with us.
Information pertaining to us and our customers is maintained and transactions are executed on the networks and systems of ours, our customers and certain of our third party partners, such as our online banking or core systems. The secure maintenance and transmission of confidential information as well as execution of transactions over these systems are essential to protect us and our customers against fraud and security breaches and to maintain our customers’ confidence. Breaches of information security also may occur, and in infrequent, incidental, cases have occurred, through intentional or unintentional acts by those having access to our systems or our customers’ or counterparties’ confidential information, including employees. In addition, increases in criminal activity levels and sophistication, advances in computer capabilities, new discoveries, vulnerabilities in third-party technologies (including browsers and operating systems) or other developments could result in a compromise or breach of the technology, processes and controls that we use to prevent fraudulent transactions and to protect data about us, our customers and underlying transactions as well as the technology used by our customers to access our systems.

Although we have developed and continue to invest in systems and processes that are designed to detect and prevent security breaches and cyber-attacks and periodically test our security, our inability to anticipate, or failure to adequately mitigate, breaches of security could result in: losses to us or our customers; our loss of business and/or customers; damage to our reputation; the incurrence of additional expenses; disruption to our business; our inability to grow our online services or other businesses; additional regulatory scrutiny or penalties; or our exposure to civil litigation and possible financial liability - any of which could have a material adverse effect on our business, financial condition and results of operations.

More generally, publicized information concerning security and cyber-related problems could inhibit the use or growth of electronic or web-based applications or solutions as a means of conducting commercial transactions. Such publicity may also cause damage to our reputation as a financial institution. As a result, our business, financial condition and results of operations could be adversely affected.

Our controls over financial reporting and related governance procedures may fail or be circumvented.

Management regularly reviews and updates our internal control over financial reporting, disclosure controls and procedures, and corporate governance policies and procedures. We maintain controls and procedures to mitigate risks such as

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processing system failures or errors and customer or employee fraud, and we maintain insurance coverage for certain of these risks. Any system of controls and procedures, however well designed and operated, is based in part on certain assumptions and provides only reasonable, not absolute, assurances that the objectives of the system are met. Events could occur which are not prevented or detected by our internal controls, are not insured against, or are in excess of our insurance limits. Any failure or circumvention of our controls and procedures, or failure to comply with regulations related to controls and procedures, could have an adverse effect on our business.

We may not be successful in raising additional capital needed in the future.

We may need to raise additional capital in the future to provide us with sufficient capital resources and liquidity to meet our commitments and business strategies. Our ability to raise additional capital, if needed, will depend on, among other things, conditions in the capital markets at that time which are outside of our control, and our financial performance. We cannot be assured that such capital will be available to us on acceptable terms or at all. Any occurrence that may limit our access to the capital markets may adversely affect our capital costs and our ability to raise capital. Moreover, if we need to raise capital in the future, we may have to do so when many other financial institutions are also seeking to raise capital and would have to compete with those institutions for investors. An inability to raise additional capital on acceptable terms when needed could have a material adverse effect on our business, results of operations and financial condition.

The effects of changes to FDIC insurance coverage limits are uncertain and increased premiums may adversely affect us.

The Bank’s deposits are insured by the Federal Deposit Insurance Corporation (FDIC) up to applicable legal limits. All of a depositors’ accounts at an insured depository institution, including all non-interest bearing transactions accounts, will be insured by the FDIC up to the standard maximum deposit insurance amount of ($250,000) for each deposit insurance ownership category.

Increases in FDIC insurance premiums will add to our cost of operations and could have a significant impact on the Bank. Depending on any future losses that the FDIC insurance fund may suffer due to failed institutions, there can be no assurance that there will not be additional significant premium increases in order to replenish the fund.

On February 7, 2011, the FDIC Board of Directors adopted the final rule, which redefined the deposit insurance assessment base as required by Dodd-Frank, and makes changes to assessment rates, implements Dodd-Frank’s Deposit Insurance Fund (DIF) dividend provisions, and revises the risk based assessment system for all large institutions. The final rule redefined the deposit insurance assessment base as average consolidated total assets minus average tangible equity, defined as Tier 1 capital. The rule lowered overall assessment rates in order to generate the same approximate amount of revenue under the new larger base as was raised under the old base. In 2016, the FDIC board of directors approved a final rule revising DIF assessment formulas for community banks with less than $10 billion in assets that have been FDIC-insured for at least five years. The revised method better reflects risks and helps ensure that banks that take on greater risks pay more for deposit insurance than their less risk counterparts. The method change is revenue-neutral meaning aggregate assessment revenue collected from established small banks is expected to be approximately the same as it would have been using the prior method. Assessments were expected to drop by an average of approximately one-third. The range of initial assessment rates for all institutions declines to between 3 cents and 30 cents per $100 of the assessment base from between 5 cents and 35 cents.

We have and in the future we may be required to recognize impairment with respect to investment securities, including the FHLB stock we hold.

Our securities portfolio contains whole loan private mortgage-backed securities and currently includes securities with unrecognized losses and securities that have been downgraded to below investment grade by national rating agencies. We may continue to observe declines in the fair market value of these securities. We evaluate the securities portfolio for any other-than-temporary impairment each reporting period, as required by generally accepted accounting principles. Numerous factors, including the lack of liquidity for re-sales of certain securities, the absence of reliable pricing information for securities, adverse changes in the business climate, adverse regulatory actions or unanticipated changes in the competitive environment, could have a negative effect on our securities portfolio and results of operations in future periods. There can be no assurance, however, that future evaluations of the securities portfolio will not require us to recognize further impairment charges with respect to these and other holdings.

In addition, as a condition to membership in the Federal Home Loan Bank of San Francisco (the FHLB), we are required to purchase and hold a certain amount of FHLB stock. Our stock purchase requirement is based, in part, upon the outstanding principal balance of advances from the FHLB. At December 31, 2016, we held stock in the FHLB totaling $5,594,000 as compared to our minimum required stock holding of $5,077,000. The FHLB stock held by us is carried at cost and is subject to recoverability testing under applicable accounting standards. To date, the FHLB has not discontinued the distribution of dividends on its shares. However, there can be no assurance the FHLB’s dividend paying practices will continue. As of December 31, 2016, we did not recognize an impairment charge related to our FHLB stock holdings. There can be no assurance, however, that future negative changes to the financial condition of the FHLB may not require us to recognize an impairment charge with respect to such holdings.

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If the goodwill we have recorded in connection with our acquisitions becomes impaired, it could have an adverse impact on our earnings and capital.

At December 31, 2016, we had approximately $40,231,000 of goodwill on our balance sheet attributable to our acquisitions of the Bank of Madera County in January 2005, Service 1st Bancorp in November 2008, Visalia Community Bank in July 2013, and Sierra Vista Bank in October 2016. In accordance with generally accepted accounting principles, our goodwill is not amortized but rather evaluated for impairment on an annual basis or more frequently if events or circumstances indicate that a potential impairment exists. Such evaluation is based on a variety of factors, including the quoted price of our common stock, market prices of the common stock of other banking organizations, common stock trading multiples, discounted cash flows, and data from comparable acquisitions. There can be no assurance that future evaluations of goodwill will not result in findings of impairment and write-downs, which could be material.

We may raise additional capital, which could have a dilutive effect on the existing holders of our common stock and adversely affect the market price of our common stock.

We are not restricted from issuing additional shares of common stock or securities that are convertible into or exchangeable for, or that represent the right to receive, common stock. We frequently evaluate opportunities to access the capital markets taking into account our regulatory capital ratios, financial condition and other relevant considerations, and subject to market conditions, we may take further capital actions. Such actions could include, among other things, the issuance of additional shares of common stock in public or private transactions in order to further increase our capital levels above the requirements for a well-capitalized institution established by the Federal bank regulatory agencies as well as other regulatory targets.

The issuance of any additional shares of common stock or securities convertible into or exchangeable for common stock or that represent the right to receive common stock, or the exercise of such securities including, without limitation, securities issued upon exercise of outstanding stock options under our stock option plans, could be substantially dilutive to shareholders of our common stock. With the exception of one major shareholder, holders of our shares of common stock have no preemptive rights that entitle holders to purchase their pro rata share of any offering of shares of any class or series and, therefore, such sales or offerings could result in increased dilution to our shareholders. The market price of our common stock could decline as a result of sales of shares of our common stock or the perception that such sales could occur.

We may not be able to maintain our historical growth rate which may adversely impact our results of operations and financial condition.

We have initiated internal asset growth programs, completed various acquisitions and opened additional offices in the past few years. We may not be able to sustain our historical rate of asset growth or may not even be able to grow at all. We may not be able to obtain the financing necessary to fund additional asset growth and may not be able to find suitable candidates for acquisition. Various factors, such as economic conditions and competition, may impede or prohibit the opening of new branch offices. Further, our inability to attract and retain experienced bankers may adversely affect our internal asset growth. A significant decrease in our historical rate of asset growth may adversely impact our results of operations and financial condition.

We may be unable to complete future acquisitions, and once complete, may not be able to integrate our acquisitions successfully.

Our growth strategy includes our desire to acquire other financial institutions. We may not be able to complete any future acquisitions and, for completed acquisitions, we may not be able to successfully integrate the operations, management, products and services of the entities we acquire. We may not realize expected cost savings or make revenue enhancements. Following each acquisition, we must expend substantial managerial, operating, financial and other resources to integrate these entities. In particular, we may be required to install and standardize adequate operational and control systems, deploy or modify equipment, implement marketing efforts in new as well as existing locations and employ and maintain qualified personnel. Our failure to successfully integrate the entities we acquire into our existing operations may adversely affect our financial condition and results of operations.

We operate in a highly regulated environment and may be adversely affected by changes in federal and local laws and regulations.

We are subject to extensive regulation, supervision and examination by federal and state banking authorities. Any change in applicable regulations or federal or state legislation could have a substantial impact on us and our operations. Additional legislation and regulations may be enacted or adopted in the future that could significantly affect our powers, authority and operations, which could have a material adverse effect on our financial condition and results of operations. Further, regulators have significant discretion and power to prevent or remedy unsafe or unsound practices or violations of laws by banks and bank holding companies in the performance of their supervisory and enforcement duties. The exercise of this regulatory discretion and power may have a negative impact on us.

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The price of our common stock may fluctuate significantly, and this may make it difficult for you to resell shares of common stock owned by you at times or at prices you find attractive.

The stock market and, in particular, the market for financial institution stocks, has experienced significant volatility, which, in recent quarters, has reached unprecedented levels. In some cases, the markets have produced downward pressure on stock prices for certain issuers without regard to those issuers' underlying financial strength. As a result, the trading volume in our common stock may fluctuate more than usual and cause significant price variations to occur. This may make it difficult for you to resell shares of common stock owned by you at times or at prices you find attractive. The low trading volume in our common shares on the NASDAQ Capital Market means that our shares may have less liquidity than other publicly traded companies. We cannot ensure that the volume of trading in our common shares will be maintained or will increase in the future.

The trading price of the shares of our common stock will depend on many factors, which may change from time to time and which may be beyond our control, including, without limitation, our financial condition, performance, creditworthiness and prospects, future sales or offerings of our equity or equity related securities, and other factors identified above in the forward-looking statement discussion under the section titled "Cautionary Statements Regarding Forward-Looking Statements" and below. These broad market fluctuations have adversely affected and may continue to adversely affect the market price of our common stock. Among the factors that could affect our stock price are:

- actual or anticipated quarterly fluctuations in our operating results and financial condition;
- changes in financial estimates or publication of research reports and recommendations by financial analysts or actions taken by rating agencies with respect to our common stock or those of other financial institutions;
- failure to meet analysts' revenue or earnings estimates;
- speculation in the press or investment community generally or relating to our reputation, our market area, our competitors or the financial services industry in general;
- strategic actions by us or our competitors, such as acquisitions, restructurings, dispositions or financings;
- actions by our current shareholders, including sales of common stock by existing shareholders and/or directors and executive officers;
- fluctuations in the stock price and operating results of our competitors;
- future sales of our equity, equity-related or debt securities;
- changes in the frequency or amount of dividends or share repurchases;
- proposed or adopted regulatory changes or developments;
- anticipated or pending investigations, proceedings, or litigation that involves or affects us;
- trading activities in our common stock, including short-selling;
- domestic and international economic factors unrelated to our performance; and
- general market conditions and, in particular, developments related to market conditions for the financial services industry.

A significant decline in our stock price could result in substantial losses for individual shareholders.

ITEM 1B - UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2 - DESCRIPTION OF PROPERTY.

The Company owns the property on which full-service branch offices are situated at the following California locations: the Clovis Main office in Clovis, the Foothill office in Prather, the Modesto office, the Kerman office, the Floral office in Visalia, and the Exeter office.

All other property is leased by the Company, including the principal executive offices in Fresno. This facility houses the Company's corporate offices, comprised of various departments, including accounting, information services, human resources, real estate department, loan servicing, credit administration, branch support operations, and compliance.

The Company continually evaluates the suitability and adequacy of the Company's offices and has a program of relocating or remodeling them as necessary to be efficient and attractive facilities. Management believes that its existing facilities are adequate for its present purposes.

Properties owned by the Bank are held without loans or encumbrances. All of the property leased is leased directly from independent parties. Management considers the terms and conditions of each of the existing leases to be in the aggregate favorable to the Company. See Note 13 of the Company's audited Consolidated Financial Statements in Item 8 of this Annual Report.

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ITEM 3 - LEGAL PROCEEDINGS.

The Company is subject to legal proceedings and claims which arise in the ordinary course of business. In the opinion of management, the amount of ultimate liability with respect to such actions will not materially affect the consolidated financial position or consolidated results of operations of the Company.
None of our directors, officers, affiliates, more than 5% shareholders or any associates of these persons is a party adverse to the Company or the Bank or has a material interest adverse to the Company or the Bank in any material legal proceeding.

ITEM 4 - MINE SAFETY DISCLOSURES

None to report.

PART II

ITEM 5 - MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Our common stock is listed for trading on the Nasdaq Capital Market under the ticker symbol CVCY. As of March 13, 2017, we had approximately 970 shareholders of record.
The following table shows the high and low sales prices for the common stock for each quarter as reported by The NASDAQ Stock Market and cash dividend payment for each quarter presented.

Common Stock Prices and Dividends

	Quarter 1 2015	Quarter 2 2015	Quarter 3 2015	Quarter 4 2015	Quarter 1 2016	Quarter 2 2016	Quarter 3 2016	Quarter 4 2016
High	$ 12.16	$ 12.35	$ 12.50	$ 12.50	$ 12.49	$ 14.64	$ 16.42	$ 20.00
Low	$ 9.55	$ 10.25	$ 10.66	$ 10.51	9.45	10.78	13.30	13.75
Dividends per share	$ —	$ 0.06	$ 0.06	$ 0.06	$ 0.06	$ 0.06	$ 0.06	$ 0.06

We paid common share cash dividends of $0.24 and $0.18 per share in 2016 and 2015, respectively. The Company's primary source of income with which to pay cash dividends is dividends from the Bank. The Bank would not pay any dividend that would cause it to be deemed not "well capitalized" under applicable banking laws and regulations. See Note 14 in the audited Consolidated Financial Statements in Item 8 of this Annual Report.
The amount of future dividends will depend upon our earnings, financial condition, capital requirements and other factors, and will be determined by our board of directors on a quarterly basis. It is Federal Reserve policy that bank holding companies generally pay dividends on common stock only out of income available over the past year, and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. It is also Federal Reserve policy that bank holding companies not maintain dividend levels that undermine the holding company's ability to be a source of strength to its banking subsidiaries. Additionally, in consideration of the current financial and economic environment, the Federal Reserve has indicated that bank holding companies should carefully review their dividend policy and has discouraged payment ratios that are at maximum allowable levels unless both asset quality and capital are very strong. Under the federal Prompt Corrective Action regulations, the Federal Reserve or the FDIC may prohibit a bank holding company from paying any dividends if the holding company's bank subsidiary is classified as undercapitalized.
As a holding company, our ability to pay cash dividends is affected by the ability of our bank subsidiary, to pay cash dividends. The ability of the Bank (and our ability) to pay cash dividends in the future and the amount of any such

cash dividends is and could be in the future further influenced by bank regulatory requirements and approvals and capital guidelines.

The decision whether to pay dividends will be made by our board of directors in light of conditions then existing, including factors such as our results of operations, financial condition, business conditions, regulatory capital requirements and covenants under any applicable contractual arrangements, including agreements with regulatory authorities.

The Company has outstanding trust preferred securities from special purpose trust and accompanying subordinated debt. The subordinated debt is senior to our shares of common stock. As a result, we must make payments on the subordinated debt before any dividends can be paid on our common stock. Under the terms of the subordinated debt, we may defer interest payments for up to five years. If the Company should ever defer such interest payments, we would be prohibited from declaring or paying any cash dividends on any shares of our common stock.

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For information on the statutory and regulatory limitations on the ability of the Company to pay dividends and on the Bank to pay dividends to Company see “Item 1 - Business - Supervision and Regulation - Dividends.”
EQUITY COMPENSATION PLAN INFORMATION

The following chart sets forth information for the year ended December 31, 2016, regarding equity based compensation plans of the Company.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)		Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)	
Equity compensation plans approved by security holders	202,215	(1)	$ 6.87	829,200	(2)
Equity compensation plans not approved by security holders	N/A		N/A	N/A	
Total	202,215		$ 6.87	829,200	

(1) Under the Central Valley Community Bancorp 2015 Omnibus Incentive Plan (2015 Plan) and the Central Valley Community Bancorp 2005 Omnibus Incentive Plan (2005 Plan), the Company is authorized to issue restricted stock awards. Restricted stock awards are not included in the total in column (a). During 2016, the Company issued 54,650 shares of restricted stock. During 2014, the Company entered into an agreement with an executive to issue $100,000 of restricted stock per year during each of 2015 and 2016 (based on then-prevailing market prices) from the 2005 Plan. At December 31, 2016, there were 93,501 shares of restricted stock issued and outstanding. See Note 15 in the audited Consolidated Financial Statements in Item 8 of this Annual Report.
(2) Includes securities available for issuance of stock options and restricted stock.

No options to purchase shares of the Company’s common stock were issued during the years ending December 31, 2016 and 2015 from any of the Company’s stock based compensation plans. During the years ended December 31, 2016 and 2015, 54,650 and 9,268 shares of restricted common stock were granted from outstanding grants under the 2015 and 2005 Plans.

ITEM 6 - SELECTED CONSOLIDATED FINANCIAL DATA

	Years Ended December 31,				
(In thousands, except per share amounts)	2016	2015	2014	2013	2012
Statements of Income					
Total interest income	$46,676	$41,822	$41,039	$34,836	$31,820
Total interest expense	1,096	1,047	1,156	1,385	1,883
Net interest income before provision for credit losses	45,580	40,775	39,883	33,451	29,937
(Reversal of) Provision for credit losses	(5,850)	600	7,985	—	700
Net interest income after provision for credit losses	51,430	40,175	31,898	33,451	29,237
Non-interest income	9,591	9,387	8,164	7,831	7,242
Non-interest expenses	38,922	36,016	35,338	31,685	27,274
Income before provision for (benefit from) income taxes	22,099	13,546	4,724	9,597	9,205
Provision for (benefit from) income taxes	6,917	2,582	(570)	1,347	1,685
Net income	15,182	10,964	5,294	8,250	7,520

Preferred stock dividends and accretion of discount	—	—	—	350	350
Net income available to common shareholders	$15,182	$10,964	$5,294	$7,900	$7,170
Basic earnings per share	$1.34	$1.00	$0.48	$0.77	$0.75
Diluted earnings per share	$1.33	$1.00	$0.48	$0.77	$0.75
Cash dividends declared per common share	$0.24	$0.18	$0.20	$0.20	$0.05

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	December 31,				
(In thousands)	2016	2015	2014	2013	2012
Balances at end of year:					
Investment securities, Federal funds sold and deposits in other banks	$558,132	$580,544	$520,511	$529,398	$424,516
Net loans	747,302	588,501	564,280	503,149	385,185
Total deposits	1,255,979	1,116,267	1,039,152	1,004,143	751,432
Total assets	1,443,323	1,276,736	1,192,183	1,145,635	890,228
Shareholders' equity	164,033	139,323	131,045	120,043	117,665
Earning assets	1,319,065	1,173,591	1,074,942	1,042,552	801,098
Average balances:					
Investment securities, Federal funds sold and deposits in other banks	$560,860	$529,046	$513,866	$445,859	$368,818
Net loans	636,475	577,784	531,382	444,770	394,675
Total deposits	1,144,231	1,065,798	1,006,560	848,493	719,601
Total assets	1,321,007	1,222,526	1,157,483	986,924	853,078
Shareholders' equity	154,325	135,062	130,414	119,746	114,561
Earning assets	1,210,082	1,112,758	1,052,097	895,330	766,937

Data from 2016 reflects the partial year impact of the acquisition of Sierra Vista Bank on October 1, 2016. Data from 2013 reflects the partial year impact of the acquisition of Visalia Community Bank on July 1, 2013.

ITEM 7 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Management's discussion and analysis should be read in conjunction with the Company's audited Consolidated Financial Statements, including the Notes thereto, in Item 8 of this Annual Report.

Certain matters discussed in this report constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements contained herein that are not historical facts, such as statements regarding the Company's current business strategy and the Company's plans for future development and operations, are based upon current expectations. These statements are forward-looking in nature and involve a number of risks and uncertainties. Such risks and uncertainties include, but are not limited to (1) significant increases in competitive pressure in the banking industry; (2) the impact of changes in interest rates; (3) a decline in economic conditions in the Central Valley; (4) the Company's ability to continue its internal growth at historical rates; (5) the Company's ability to maintain its net interest margin; (6) the decline quality of the Company's earning assets; (7) decline in credit quality; (8) changes in the regulatory environment; (9) fluctuations in the real estate market; (10) changes in business conditions and inflation; (11) changes in securities markets (12) risks associated with acquisitions, relating to difficulty in integrating combined operations and related negative impact on earnings, and incurrence of substantial expenses. Therefore, the information set forth in such forward-looking statements should be carefully considered when evaluating the business prospects of the Company.

When the Company uses in this Annual Report the words "anticipate," "estimate," "expect," "project," "intend," "commit," "b and similar expressions, the Company intends to identify forward-looking statements. Such statements are not guarantees of performance and are subject to certain risks, uncertainties and assumptions, including those described in this Annual Report. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated, expected, projected, intended, committed or believed. The future results and shareholder values of the Company may differ materially from those expressed in these forward-looking statements. Many of the factors that will determine these results and values are beyond the Company's ability to control or predict. For those statements, the Company claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. See also the discussion of risk factors in Item 1A, "Risk Factors."

We are not able to predict all the factors that may affect future results. You should not place undue reliance on any forward looking statement, which speaks only as of the date of this Report on Form 10-K. Except as required by applicable laws or regulations, we do not undertake any obligation to update or revise any forward looking statement, whether as a result of new information, future events or otherwise.

INTRODUCTION

Central Valley Community Bancorp (NASDAQ: CVCY) (the Company) was incorporated on February 7, 2000. The formation of the holding company offered the Company more flexibility in meeting the long-term needs of customers, shareholders, and the communities it serves. The Company currently has one bank subsidiary, Central Valley Community Bank (the Bank) and one business trust subsidiary, Service 1st Capital Trust 1. The Company and Sierra Vista Bank (SVB) completed a merger under which SVB was merged with and into the Bank on October 1, 2016. SVB had one branch in Folsom, one branch in Fair Oaks, and one branch in Cameron Park which continue to be operated by the Bank. The Company's market area includes the central valley area from Sacramento, California to Bakersfield, California.

During 2016, we focused on asset quality and capital adequacy due to the uncertainty created by the economy. We also focused on assuring that competitive products and services were made available to our clients while adjusting to the many new laws and regulations that affect the banking industry.

As of December 31, 2016, the Bank operated 22 full-service offices. The Bank has a Real Estate Division, an Agribusiness Center and an SBA Lending Division in Fresno. All real estate related transactions are conducted and processed through the Real Estate Division, including interim construction loans for single family residences and commercial buildings. We offer permanent single family residential loans through our mortgage broker services. The SVB acquisition added total assets, at fair value, of approximately $155.15 million, $122.53 million in loans, at fair value, and $138.38 million in deposits, at fair value, at October 1, 2016. SVB’s results of operations have been included in the Company’s results of operations beginning October 1, 2016. The one-time pre-tax severance, retention, acquisition and integration costs totaled $1.78 million for the year ended December 31, 2016.

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ECONOMIC CONDITIONS

The economy in California's Central Valley had been negatively impacted by the recession that began in 2007 and the related real estate market and the slowdown in residential construction. The recession impacted most industries in our market area. Initially, housing values throughout the nation and especially in the Central Valley decreased dramatically, which in turn negatively affected the personal net worth of much of the population in our service area. Over the last several years the economy, as evidenced by the California and Central Valley unemployment rates, and housing prices have shown slow but steady improvement. Housing in the Central Valley continues to be relatively more affordable than the major metropolitan areas in California.
Agriculture and agricultural related businesses remain a critical part of the Central Valley's economy. The Valley's agricultural production is widely diversified, producing nuts, vegetables, fruit, cattle, dairy products, and cotton. The continued future success of agriculture related businesses is highly dependent on the availability of water and is subject to fluctuation in worldwide commodity prices, currency exchanges, and demand. From time to time, California experiences severe droughts, which could significantly harm the business of our customers and the credit quality of the loans to those customers. We closely monitor the water resources and the related issues affecting our customers, and will remain vigilant for signs of deterioration within the loan portfolio in an effort to manage credit quality and work with borrowers where possible to mitigate any losses.

OVERVIEW

Diluted earnings per share (EPS) for the year ended December 31, 2016 was $1.33 compared to $1.00 and $0.48 for the years ended December 31, 2015 and 2014, respectively. Net income for 2016 was $15,182,000 compared to $10,964,000 and $5,294,000 for the years ended December 31, 2015 and 2014, respectively. The increase in net income and EPS was primarily driven by a decrease in provision for credit losses, an increase in net interest income, and an increase in non-interest income offset by increases in non-interest expense and the provision for income taxes in 2016 compared to 2015. Total assets at December 31, 2016 were $1,443,323,000 compared to $1,276,736,000 at December 31, 2015.
Return on average equity for 2016 was 9.84% compared to 8.12% and 4.06% for 2015 and 2014, respectively. Return on average assets for 2016 was 1.15% compared to 0.90% and 0.46% for 2015 and 2014, respectively. Total equity was $164,033,000 at December 31, 2016 compared to $139,323,000 at December 31, 2015. The increase in equity in 2016 compared to 2015 was primarily driven by the issuance of stock in connection with the Sierra Vista Bank acquisition, as well as the retention of earnings, net of dividends paid, partially offset by a decrease in unrealized gains on available-for-sale securities recorded in accumulated other comprehensive income (AOCI).
Average total loans increased $59,811,000 or 10.19% to $646,573,000 in 2016 compared to $586,762,000 in 2015. In 2016, we recorded a reverse provision for $5,850,000 for credit losses compared to a provision for $600,000 in 2015 and $7,985,000 in 2014. The Company had nonperforming assets, consisting of $2,180,000 in nonaccrual loans and $362,000 in repossessed assets, totaling $2,542,000 at December 31, 2016. At December 31, 2015, nonperforming assets totaled $2,413,000. Net recoveries (charge-offs) for 2016 were $5,566,000 compared to $702,000 for 2015 and $(8,885,000) for 2014. Refer to "Asset Quality" below for further information.

Key Factors in Evaluating Financial Condition and Operating Performance

In evaluating our financial condition and operating performance, we focus on several key factors including:

•Return to our shareholders;
•Return on average assets;
•Development of revenue streams, including net interest income and non-interest income;
•Asset quality;
•Asset growth;

•Capital adequacy;
•Operating efficiency; and
•Liquidity.

Return to Our Shareholders

One measure of our return to our shareholders is the return on average equity (ROE). ROE is a ratio that measures net income divided by average shareholders' equity. Our ROE was 9.84% for the year ended 2016 compared to 8.12% and 4.06% for the years ended 2015 and 2014, respectively.
Our net income for the year ended December 31, 2016 increased $4,218,000 compared to 2015 and increased $5,670,000 in 2015 compared to 2014. During 2016, net income increased due to a decrease in the provision for credit losses,

increases in net interest income, and increases in non-interest income, partially offset by an increase in tax expense and increases in non-interest expenses, compared to 2015.

Net interest income increased primarily because of increases in loan and investment income, offset by increases in interest expense on deposits. During 2016, our net interest margin (NIM) increased 8 basis points to 4.09% compared to 2015. Our net interest margin increased as a result of yield changes, asset mix changes, and an increase in average earning assets, partially offset by an increase in interest-bearing liabilities. Net interest income during 2016 was positively impacted by the collection of nonaccrual loans which resulted in a recovery of interest income of approximately $657,000. The recovery was partially offset by reversal of approximately $71,000 in interest income on loans placed on nonaccrual during the year. Net interest income during 2015 was positively impacted by the collection of non-accrual loan which resulted in a recovery of interest income of approximately $431,000. The recovery was partially offset by reversal of approximately $7,000 in interest income on loans put on nonaccrual during the year.

During the year ended 2016, the increase in non-interest income was primarily driven by a $425,000 increase in net realized gains on sales and calls of investment securities, an increase in loan placement fees of $41,000, a $50,000 increase in Federal Home Loan Bank dividends, a $31,000 increase in interchange fees, partially offset by a $48,000 decrease in service charge income, and a $121,000 decrease in other income, in 2016 compared to 2015. The Company also realized $190,000 and $345,000 tax-free gains related to the collection of life insurance proceeds in 2016 and 2015, respectively, which are included in other non-interest income. In addition, the Company recorded an other-than-temporary impairment loss of $136,000 during the year ended December 31, 2016.

Non-interest expenses increased in 2016 compared to 2015 primarily due to the SVB acquisition. The net increase year over year was a result of increases in salary and employee benefit expenses of $1,045,000, increase in acquisition and integration expenses of $1,782,000, data processing expenses of $568,000, occupancy and equipment expenses of $85,000, ATM/Debit card expenses of $85,000, partially offset by a decrease in Internet banking expenses of $31,000, a decrease of regulatory assessments of $417,000, advertising fees of $32,000, professional services of $246,000, and amortization of core deposit intangibles of $171,000. Basic EPS was $1.34 for 2016 compared to $1.00 and $0.48 for 2015 and 2014, respectively. Diluted EPS was $1.33 for 2016 compared to $1.00 and $0.48 for 2015 and 2014, respectively. The increase in EPS for 2016 is primarily due to the increase in net income.

We experienced an increase in capital due to increases in retained earnings and from the issuance of common stock as a result of the Sierra Vista Bank acquisition, offset by a decrease in accumulated other comprehensive income.

Return on Average Assets

Our return on average assets (ROA) is a ratio that measures our performance compared with other banks and bank holding companies. Our ROA for the year ended 2016 was 1.15% compared to 0.90% and 0.46% for the years ended December 31, 2015 and 2014, respectively. The 2016 increase in ROA is primarily due to the increase in net income. Annualized ROA for our peer group was 0.99% at December 31, 2016. Peer group information from SNL Financial data includes bank holding companies in central California with assets from $600 million to $2.5 billion.

Development of Revenue Streams

Over the past several years, we have focused on not only our net income, but improving the consistency of our revenue streams in order to create more predictable future earnings and reduce the effect of changes in our operating environment on our net income. Specifically, we have focused on net interest income through a variety of strategies, including increases in average interest earning assets, and minimizing the effects of the recent interest rate decline on our net interest margin by focusing on core deposits and managing the cost of funds. Our net interest margin (fully tax equivalent basis) was 4.09% for the year ended December 31, 2016, compared to 4.01% and 4.11% for the years ended December 31, 2015 and 2014, respectively. We experienced an increase in 2016 net interest margin compared to 2015, resulting from the increase in loan and investment yields. The effective tax equivalent yield on total earning assets increased 8 basis points, while the cost of total interest-bearing liabilities and total deposits remained unchanged. Our cost of total deposits in 2016 and 2015 was 0.09% compared to 0.11% for the same period in 2014.

Our net interest income before provision for credit losses increased $4,805,000 or 11.78% to $45,580,000 for the year ended 2016 compared to $40,775,000 and $39,883,000 for the years ended 2015 and 2014, respectively.

Our non-interest income is generally made up of service charges and fees on deposit accounts, fee income from loan placements, appreciation in cash surrender value of bank owned life insurance, and net gains from sales and calls of investment securities. Non-interest income in 2016 increased $204,000 or 2.17% to $9,591,000 compared to $9,387,000 in 2015 and $8,164,000 in 2014. The increase resulted primarily from increases in net realized gains on sales and calls of investment securities, loan placement fees, interchange fees, and Federal Home Loan Bank dividends, partially offset by a decrease in service charge income, appreciation in cash surrender value of bank owned life insurance, and gain on sale of other real estate owned compared to 2015. Customer service charges decreased $48,000 or 1.56% to $3,022,000 in 2016 compared to $3,070,000 and $3,280,000 in 2015 and 2014, respectively. Further detail on non-interest income is provided below.

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Asset Quality

For all banks and bank holding companies, asset quality has a significant impact on the overall financial condition and results of operations. Asset quality is measured in terms of classified and nonperforming loans, and is a key element in estimating the future earnings of a company. Total nonperforming assets were $2,542,000 and $2,413,000 at December 31, 2016 and 2015, respectively. Nonperforming assets totaled 0.34% of gross loans as of December 31, 2016 and 0.40% of gross loans as of December 31, 2015. The nonperforming assets for 2016 includes repossessed asset of $362,000 compared to no repossessed asset at December 31, 2015. The Company had no other real estate owned (OREO) at December 31, 2016 or December 31, 2015. Management maintains certain loans that have been brought current by the borrower (less than 30 days delinquent) on nonaccrual status until such time as management has determined that the loans are likely to remain current in future periods.
The ratio of nonperforming loans to total loans was 0.29% as of December 31, 2016 and 0.40% as of December 31, 2015. The allowance for credit losses as a percentage of outstanding loan balance was 1.23% as of December 31, 2016 and 1.61% as of December 31, 2015. The ratio of net recoveries to average loans was 0.86% as of December 31, 2016 and 0.12% as of December 31, 2015.

Asset Growth

As revenues from both net interest income and non-interest income are a function of asset size, the continued growth in assets has a direct impact in increasing net income and therefore ROE and ROA. The majority of our assets are loans and investment securities, and the majority of our liabilities are deposits, and therefore the ability to generate deposits as a funding source for loans and investments is fundamental to our asset growth. Total assets increased 13.05% during 2016 to $1,443,323,000 as of December 31, 2016 from $1,276,736,000 as of December 31, 2015. Total gross loans increased 26.50% to $756,628,000 as of December 31, 2016, compared to $598,111,000 at December 31, 2015. Total investment securities and Federal funds sold increased 7.50% to $547,764,000 as of December 31, 2016 compared to $509,556,000 as of December 31, 2015. Total deposits increased 12.52% to $1,255,979,000 as of December 31, 2016 compared to $1,116,267,000 as of December 31, 2015. Our loan to deposit ratio at December 31, 2016 was 60.24% compared to 53.58% at December 31, 2015. The loan to deposit ratio of our peers was 78.96% at December 31, 2016. The growth information above includes the results of our acquisition of Sierra Vista Bank which added approximately $122,533,000 in net loans and $138,236,000 in deposits during 2016.

Capital Adequacy

At December 31, 2016, we had a total capital to risk-weighted assets ratio of 13.72%, a Tier 1 risk-based capital ratio of 12.74%, common equity Tier 1 ratio of 12.48%, and a leverage ratio of 8.75%. At December 31, 2015, we had a total capital to risk-weighted assets ratio of 15.04%, a Tier 1 risk-based capital ratio of 13.79% and a leverage ratio of 8.65%. At December 31, 2016, on a stand-alone basis, the Bank had a total risk-based capital ratio of 13.57%, a Tier 1 risk based capital ratio of 12.59%, common equity Tier 1 ratio of 12.59%, and a leverage ratio of 8.64%. At December 31, 2015, the Bank had a total risk-based capital ratio of 14.93%, Tier 1 risk-based capital of 13.67% and a leverage ratio of 8.58%. Note 14 of the audited Consolidated Financial Statements provides more detailed information concerning the Company's capital amounts and ratios. As of January 1, 2015, along with other community banking organizations, the Company and the Bank became subject to new capital requirements, and certain provisions of the new rules are being phased in through 2019 under the Dodd-Frank Act and Basel III. The Company's consolidated capital ratios exceeded regulatory guidelines and the Bank's capital ratios exceeded the regulatory guidelines for a well-capitalized financial institution under the Basel III regulatory requirements at December 31, 2016.

Operating Efficiency

Operating efficiency is the measure of how efficiently earnings before taxes are generated as a percentage of revenue. A lower ratio represents greater efficiency. The Company's efficiency ratio (operating expenses, excluding amortization of intangibles and foreclosed property expense, divided by net interest income plus non-interest income, excluding net gains and losses from sale of securities) was 68.45% for 2016 compared to 69.22% for 2015 and 69.33% for 2014. The improvement in the efficiency ratio in 2016 is due to the growth in revenues outpacing the growth in non-interest expense. The increase in the efficiency ratio in 2015 compared to 2014 is due to the growth in revenues outpacing the growth in non-interest expense. The Company's net interest income before provision for credit losses plus non-interest income increased 9.99% to $55,171,000 in 2016 compared to $50,162,000 in 2015 and $48,047,000 in 2014, while operating expenses increased 8.07% in 2016, 1.92% in 2015, and 11.53% in 2014.

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Liquidity

Liquidity management involves our ability to meet cash flow requirements arising from fluctuations in deposit levels and demands of daily operations, which include providing for customers' credit needs, funding of securities purchases, and ongoing repayment of borrowings. Our liquidity is actively managed on a daily basis and reviewed periodically by our management and Directors' Asset/Liability Committee. This process is intended to ensure the maintenance of sufficient funds to meet our needs, including adequate cash flows for off-balance sheet commitments. Our primary sources of liquidity are derived from financing activities which include the acceptance of customer and, to a lesser extent, broker deposits, Federal funds facilities and advances from the Federal Home Loan Bank of San Francisco. We have available unsecured lines of credit with correspondent banks totaling approximately $40,000,000 and secured borrowing lines of approximately $351,713,000 with the Federal Home Loan Bank. These funding sources are augmented by collection of principal and interest on loans, the routine maturities and pay downs of securities from our investment securities portfolio, the stability of our core deposits, and the ability to sell investment securities. Primary uses of funds include origination and purchases of loans, withdrawals of and interest payments on deposits, purchases of investment securities, and payment of operating expenses.
We had liquid assets (cash and due from banks, interest-earning deposits in other banks, Federal funds sold and available-for-sale securities) totaling $586,317,000 or 40.62% of total assets at December 31, 2016 and $572,171,000 or 44.82% of total assets as of December 31, 2015.

RESULTS OF OPERATIONS

Net Income

Net income was $15,182,000 in 2016 compared to $10,964,000 and $5,294,000 in 2015 and 2014, respectively. Basic earnings per share was $1.34, $1.00, and $0.48 for 2016, 2015, and 2014, respectively. Diluted earnings per share was $1.33, $1.00, and $0.48 for 2016, 2015, and 2014, respectively. ROE was 9.84% for 2016 compared to 8.12% for 2015 and 4.06% for 2014. ROA for 2016 was 1.15% compared to 0.90% for 2015 and 0.46% for 2014.
The increase in net income for 2016 compared to 2015 can be attributed to a decrease in the provision for credit losses, an increase in net interest income, and an increase in non-interest income, partially offset by an increase in provision for income taxes and an increase in non-interest expense including acquisition and integration expenses related to the SVB acquisition. The increase in net income for 2015 compared to 2014 was primarily attributed to a decrease in the provision for credit losses, and an increase in non-interest income, partially offset by an increase in provision for income taxes and an increase in non-interest expense.

Interest Income and Expense

Net interest income is the most significant component of our income from operations. Net interest income (the interest rate spread) is the difference between the gross interest and fees earned on the loan and investment portfolios and the interest paid on deposits and other borrowings. Net interest income depends on the volume of and interest rate earned on interest-earning assets and the volume of and interest rate paid on interest-bearing liabilities.

The following table sets forth a summary of average balances with corresponding interest income and interest expense as well as average yield and cost information for the periods presented. Average balances are derived from daily balances, and nonaccrual loans are not included as interest-earning assets for purposes of this table.

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SCHEDULE OF AVERAGE BALANCES, AVERAGE YIELDS AND RATES

(Dollars in thousands)	Year Ended December 31, 2016 Average Balance	Interest Income/ Expense	Average Interest Rate	Year Ended December 31, 2015 Average Balance	Interest Income/ Expense	Average Interest Rate	Year Ended December 31, 2014 Average Balance	Interest Income/ Expense	Average Interest Rate
ASSETS									
Interest-earning deposits in other banks	$53,514	$289	0.54 %	$64,963	$209	0.32 %	$53,781	$175	0.32 %
Securities									
Taxable securities	313,006	5,876	1.88 %	285,585	4,793	1.68 %	296,014	5,538	1.87 %
Non-taxable securities (1)	194,224	9,787	5.04 %	178,247	9,569	5.37 %	163,778	8,837	5.40 %
Total investment securities	507,230	15,663	3.09 %	463,832	14,362	3.10 %	459,792	14,375	3.13 %
Federal funds sold	116	—	0.51 %	251	1	0.25 %	293	1	0.25 %
Total securities and interest-earning deposits	560,860	15,952	2.84 %	529,046	14,572	2.75 %	513,866	14,551	2.83 %
Loans (2) (3)	644,282	34,051	5.29 %	578,899	30,504	5.27 %	533,531	29,493	5.53 %
Federal Home Loan Bank stock	4,940	630	12.75 %	4,813	580	12.05 %	4,700	327	6.96 %
Total interest-earning assets	1,210,082	$50,633	4.18 %	1,112,758	$45,656	4.10 %	1,052,097	$44,371	4.22 %
Allowance for credit losses	(10,098)			(8,978)			(8,147)		
Nonaccrual loans	2,291			7,863			5,998		
Cash and due from banks	23,840			25,019			23,905		
Bank premises and equipment	9,053			9,664			10,511		
Other non-earning assets	85,839			76,200			73,119		
Total average assets	$1,321,007			$1,222,526			$1,157,483		
LIABILITIES AND SHAREHOLDERS’ EQUITY									
Interest-bearing liabilities:									
Savings and NOW accounts	$337,804	$317	0.09 %	$300,741	$261	0.09 %	$265,751	$241	0.09 %
Money market accounts	249,620	133	0.05 %	227,743	141	0.06 %	229,769	174	0.08 %
Time certificates of deposit	139,656	525	0.38 %	149,383	546	0.37 %	162,218	645	0.40 %
Total interest-bearing deposits	727,080	975	0.13 %	677,867	948	0.14 %	657,738	1,060	0.16 %
Other borrowed funds	5,157	121	2.35 %	5,156	99	1.89 %	5,155	96	1.83 %

Total interest-bearing liabilities	732,237	$1,096	0.15	%	683,023	$1,047	0.15	%	662,893	$1,156	0.17	%
Non-interest bearing demand deposits	417,151				387,931				348,822			
Other liabilities	17,294				16,510				15,354			
Shareholders' equity	154,325				135,062				130,414			
Total average liabilities and shareholders' equity	$1,321,007				$1,222,526				$1,157,483			
Interest income and rate earned on average earning assets		$50,633	4.18	%		$45,656	4.10	%		$44,371	4.22	%
Interest expense and interest cost related to average interest-bearing liabilities		1,096	0.15	%		1,047	0.15	%		1,156	0.17	%
Net interest income and net interest margin (4)		$49,537	4.09	%		$44,609	4.01	%		$43,215	4.11	%

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(1) Interest income is calculated on a fully tax equivalent basis, which includes Federal tax benefits relating to income earned on municipal bonds totaling $3,327, $3,254, and $3,005 in 2016, 2015, and 2014, respectively.
(2) Loan interest income includes loan fees of $134 in 2016, $255 in 2015, and $272 in 2014.
(3) Average loans do not include nonaccrual loans.
(4) Net interest margin is computed by dividing net interest income by total average interest-earning assets.

The following table sets forth a summary of the changes in interest income and interest expense due to changes in average asset and liability balances (volume) and changes in average interest rates for the periods indicated. The change in interest due to both rate and volume has been allocated to the change in rate.

Changes in Volume/Rate	For the Years Ended December 31, 2016 Compared to 2015			For the Years Ended December 31, 2015 Compared to 2014		
(In thousands)	Volume	Rate	Net	Volume	Rate	Net
Increase (decrease) due to changes in:						
Interest income:						
Interest-earning deposits in other banks	$(36)	$116	$80	$36	$(2)	$34
Investment securities:						
Taxable	460	623	1,083	(195)	(550)	(745)
Non-taxable (1)	857	(639)	218	780	(48)	732
Total investment securities	1,317	(16)	1,301	585	(598)	(13)
Federal funds sold	(1)	—	(1)	—	—	—
Loans	3,446	101	3,547	2,507	(1,496)	1,011
FHLB Stock	16	34	50	7	246	253
Total earning assets (1)	4,742	235	4,977	3,135	(1,850)	1,285
Interest expense:						
Deposits:						
Savings, NOW and MMA	46	2	48	30	(43)	(13)
Time certificate of deposits	(36)	14	(22)	(53)	(46)	(99)
Total interest-bearing deposits	10	16	26	(23)	(89)	(112)
Other borrowed funds	—	22	22	1	2	3
Total interest bearing liabilities	10	38	48	(22)	(87)	(109)
Net interest income (1)	$4,732	$197	$4,929	$3,157	$(1,763)	$1,394

(1) Computed on a tax equivalent basis for securities exempt from federal income taxes.

Interest and fee income from loans increased $3,547,000 or 11.63% in 2016 compared to 2015. Interest and fee income from loans increased $1,011,000 or 3.43% in 2015 compared to 2014. The increase in 2016 is primarily attributable to an increase in average total loans outstanding, as well as an increase in the yield on loans by 2 basis points. The net interest income during 2016 was positively impacted by the SVB acquisition in addition to the collection of nonaccrual loans which resulted in a recovery of interest income of approximately $657,000. The recovery was partially offset by reversal of approximately $71,000 in interest income on loans placed on nonaccrual status during the year. Interest income during 2015 was positively impacted by the collection of nonaccrual loans which resulted in a recovery of interest income of approximately $431,000. The recovery was partially offset by reversal of approximately $7,000 in interest income on loans placed on nonaccrual status during the year. Average total loans for 2016 increased $59,811,000 to $646,573,000 compared to $586,762,000 for 2015 and $539,529,000 for 2014. Of the increase in 2016, approximately $31.6 million was attributed to organic growth and approximately $28.2 million from the acquisition of SVB. The yield on loans for 2016 was 5.29% compared to 5.27% and 5.53% for 2015 and 2014, respectively.
Interest income from total investments on a non tax-equivalent basis, (total investments include investment securities, Federal funds sold, interest-bearing deposits in other banks, and other securities), increased $1,307,000 or 11.55% in

2016 compared to 2015. The yield on average investments increased 9 basis points to 2.84% for the year ended December 31, 2016 from 2.75% for the year ended December 31, 2015. Average total investments increased $31,814,000 to $560,860,000 in 2016 compared to $529,046,000 in 2015. In 2015, total investment income on a non tax-equivalent basis decreased $228,000 or 1.97% compared to 2014.

A significant portion of the investment portfolio is mortgage-backed securities (MBS) and collateralized mortgage obligations (CMOs). At December 31, 2016, we held $181,064,000 or 33.06% of the total market value of the investment

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portfolio in MBS and CMOs with an average yield of 1.88%. We invest in Collateralized Mortgage Obligations (CMO) and Mortgage Backed Securities, (MBS) as part of our overall strategy to increase our net interest margin. CMOs and MBS by their nature are affected by prepayments which are impacted by changes in interest rates. In a normal declining rate environment, prepayments from MBS and CMOs would be expected to increase and the expected life of the investment would be expected to shorten. Conversely, if interest rates increase, prepayments normally would be expected to decline and the average life of the MBS and CMOs would be expected to extend. However, in the current economic environment, prepayments may not behave according to historical norms. Premium amortization and discount accretion of these investments affects our net interest income. Our management monitors the prepayment speed of these investments and adjusts premium amortization and discount accretion based on several factors. These factors include the type of investment, the investment structure, interest rates, interest rates on new mortgage loans, expectation of interest rate changes, current economic conditions, the level of principal remaining on the bond, the bond coupon rate, the bond origination date, and volume of available bonds in market. The calculation of premium amortization and discount accretion is by nature inexact, and represents management's best estimate of principal pay downs inherent in the total investment portfolio.

The cumulative net of tax effect of the change in market value of the available-for-sale investment portfolio as of December 31, 2016 was an unrealized loss of $516,000 and is reflected in the Company's equity. At December 31, 2016, the average life of the investment portfolio was 6.18 years and the market value reflected a pre-tax unrealized loss of $891,000. Management reviews market value declines on individual investment securities to determine whether they represent other-than-temporary impairment (OTTI). For the year ended December 31, 2016, OTTI was recorded in the amount of $136,000. For the years ended December 31, 2015 and 2014, no OTTI was recorded. Future deterioration in the market values of our investment securities may require the Company to recognize additional OTTI losses.

A component of the Company's strategic plan has been to use its investment portfolio to offset, in part, its interest rate risk relating to variable rate loans. Measured at December 31, 2016, an immediate rate increase of 200 basis points would result in an estimated decrease in the market value of the investment portfolio by approximately $(43,123,000). Conversely, with an immediate rate decrease of 200 basis points, the estimated increase in the market value of the investment portfolio would be $40,501,000. The modeling environment assumes management would take no action during an immediate shock of 200 basis points. However, the Company uses those increments to measure its interest rate risk in accordance with regulatory requirements and to measure the possible future risk in the investment portfolio. For further discussion of the Company's market risk, refer to Quantitative and Qualitative Disclosures about Market Risk.

Management's review of all investments before purchase includes an analysis of how the security will perform under several interest rate scenarios to monitor whether investments are consistent with our investment policy. The policy addresses issues of average life, duration, and concentration guidelines, prohibited investments, impairment, and prohibited practices.

Total interest income in 2016 increased $4,854,000 to $46,676,000 compared to $41,822,000 in 2015 and $41,039,000 in 2014. The increase was the result of yield changes, asset mix changes, and an increase in average earning assets, partially offset by an increase in interest-bearing liabilities. The tax equivalent yield on interest earning assets increased to 4.18% for the year ended December 31, 2016 from 4.10% for the year ended December 31, 2015. Average interest earning assets increased to $1,210,082,000 for the year ended December 31, 2016 compared to $1,112,758,000 for the year ended December 31, 2015. Average interest-earning deposits in other banks decreased $11,449,000 comparing 2016 to 2015. Average yield on these deposits was 0.54% compared to 0.32% on December 31, 2016 and December 31, 2015 respectively. Average investments and interest-earning deposits increased $31,814,000 but the tax equivalent yield on those assets increased 9 basis points. Average total loans increased $59,811,000 and the yield on average loans increased 2 basis points.

The increase in total interest income total for 2015 was the result of yield changes, asset mix changes, and an increase in average earning assets, partially offset by an increase in interest-bearing liabilities. The yield on interest-earning assets increased to 4.10% for the year ended December 31, 2015 from 4.22% for the year ended December 31, 2014. Average interest-earning assets increased to $1,112,758,000 for the year ended December 31, 2015 compared to

$1,052,097,000 for the year ended December 31, 2014.

Interest expense on deposits in 2016 increased $27,000 or 2.85% to $975,000 compared to $948,000 in 2015 and $1,060,000 in 2014. The increase in interest expense in 2016 compared to 2015 was a result of the deposits acquired in the fourth quarter acquisition of Sierra Vista Bank. The yield on interest-bearing deposits decreased 1 basis points to 0.13% in 2016 from 0.14% in 2015. The decrease in interest expense in 2015 compared to 2014 was due to repricing of interest-bearing deposits, which decreased 2 basis points to 0.14% in 2015 from 0.16% in 2014. Average interest-bearing deposits were $727,080,000 for 2016 compared to $677,867,000 and $657,738,000 for 2015 and 2014, respectively. The increases in average interest-bearing deposits in 2016 and 2015 was the result of organic growth and the SVB acquisition in 2016.

Average other borrowings were $5,157,000 with an effective rate of 2.35% for 2016 compared to $5,156,000 with an effective rate of 1.89% for 2015. In 2014, the average other borrowings were $5,155,000 with an effective rate of 1.83%. Included in other borrowings are the junior subordinated deferrable interest debentures acquired from Service 1st, advances on lines of credit, advances from the Federal Home Loan Bank (FHLB), and overnight borrowings. The debentures were acquired in the merger with Service 1st and carry a floating rate based on the three month LIBOR plus a margin of 1.60%. The rate was 2.48% for 2016, 1.92% for 2015, and 1.83% for 2014.

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The cost of all interest-bearing liabilities remained unchanged at 0.15% basis points for 2016 and 2015 compared to 0.17% for 2014. The cost of total deposits remained unchanged at 0.09% for the year ended December 31, 2016 and December 31, 2015 compared to 0.11% for the year ended 2014. Average demand deposits increased 7.53% to $417,151,000 in 2016 compared to $387,931,000 for 2015 and $348,822,000 for 2014. The ratio of non-interest demand deposits to total deposits increased to 36.46% for 2016 compared to 36.40% and 34.65% for 2015 and 2014, respectively.

Net Interest Income before Provision for Credit Losses

Net interest income before provision for credit losses for 2016 increased $4,805,000 or 11.78% to $45,580,000 compared to $40,775,000 for 2015 and $39,883,000 for 2014. The increase in 2016 was due to the increase in average earning assets while the yield on interest bearing liabilities remained unchanged. Our net interest margin (NIM) increased 8 basis points. Yield on interest earning assets increased 8 basis points. The change in the mix of average interest earning assets also affected NIM. Interest-earning deposits in other banks and investment securities, which tend to have lower effective yields, increased reflective of the Federal Reserve rate increase. Net interest income before provision for credit losses increased $892,000 in 2015 compared to 2014, mainly due to the increase in average earning assets and a 2 basis point decrease in the average interest rate on interest-bearing deposits, partially offset by the decrease in the average rate on earning assets. Average interest-earning assets were $1,210,082,000 for the year ended December 31, 2016 with a NIM of 4.09% compared to $1,112,758,000 with a NIM of 4.01% in 2015, and $1,052,097,000 with a NIM of 4.11% in 2014. For a discussion of the repricing of our assets and liabilities, refer to Quantitative and Qualitative Disclosure about Market Risk.

Provision for Credit Losses

We provide for probable incurred credit losses through a charge to operating income based upon the composition of the loan portfolio, delinquency levels, historical losses and nonperforming assets, economic and environmental conditions and other factors which, in management's judgment, deserve recognition in estimating credit losses. Loans are charged off when they are considered uncollectible or when continuance as an active earning bank asset is not warranted.

The establishment of an adequate credit allowance is based on both an accurate risk rating system and loan portfolio management tools. The Board has established initial responsibility for the accuracy of credit risk grades with the individual credit officer. The grading is then submitted to the Chief Credit Officer (CCO), who reviews the grades for accuracy and gives final approval. The CCO is not involved in loan originations. The risk grading and reserve allocation is analyzed quarterly by the Senior Risk Manager, CCO, Chief Financial Officer, and Board; and at least annually by a third party credit reviewer and by various regulatory agencies.

Quarterly, the Senior Risk Manager and the CCO set the specific reserve for all adversely risk-graded credits. This process includes the utilization of loan delinquency reports, classified asset reports, collateral analysis, and portfolio concentration reports to assist in accurately assessing credit risk and establishing appropriate reserves. Reserves are also allocated to credits that are not impaired based on inherent risk in those loans.

The allowance for credit losses is reviewed at least quarterly by the Board's Audit/Compliance Committee and by the Board of Directors. Reserves are allocated to loan portfolio categories using percentages which are based on both historical risk elements such as delinquencies and losses and predictive risk elements such as economic, competitive and environmental factors. We have adopted the specific reserve approach to allocate reserves to each impaired credit for the purpose of estimating potential loss exposure. Although the allowance for credit losses is allocated to various portfolio categories, it is general in nature and available for the loan portfolio in its entirety. Changes in the allowance for credit losses may be required based on the results of independent loan portfolio examinations, regulatory agency examinations, or our own internal review process. Additions are also required when, in management's judgment, the allowance does not properly reflect the portfolio's probable loss exposure. Management believes that all adjustments, if any, to the allowance for credit losses are supported by the timely and consistent application of methodologies and processes resulting in detailed documentation of the allowance of the allowance calculation and other portfolio trending analysis.

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The allocation of the allowance for credit losses is set forth below (in thousands):

Loan Type	December 31, 2016	December 31, 2015
Commercial:		
Commercial and industrial	$ 1,884	$ 3,143
Agricultural land and production	296	419
Real estate:		
Owner occupied	1,408	1,556
Real estate construction and other land loans	698	694
Commercial real estate	1,969	1,686
Agricultural real estate	1,969	1,149
Other real estate	156	119
Consumer:		
Equity loans and lines of credit	483	500
Consumer and installment	369	234
Unallocated reserves	94	110
Total allowance for credit losses	$ 9,326	$ 9,610

Loans are charged to the allowance for credit losses when the loans are deemed uncollectible. It is the policy of management to make additions to the allowance so that it remains adequate to cover all probable incurred credit losses that exist in the portfolio at that time. We assign qualitative and environmental factors (Q factors) to each loan category. Q factors include reserves held for the effects of lending policies, economic trends, and portfolio trends along with other dynamics which may cause additional stress to the portfolio.

Managing credits identified through the risk evaluation methodology includes developing a business strategy with the customer to mitigate our potential losses. Management continues to monitor these credits with a view to identifying as early as possible when, and to what extent, additional provisions may be necessary. While the overall level of loans with an internal risk rating of substandard has increased by $17.7 million or 55.7% to $49.5 million at December 31, 2016 from $31.8 million at December 31, 2015, the classification of those loans has migrated from Agricultural land and production to Agricultural real estate. Management believes that the additional collateral obtained related to these classified assets provides the Company with a reduced risk of loss if a default event was to occur. The increase in substandard loans related to acquired SVB loans was $4.0 million at December 31, 2016. In addition, the level of commercial and industrial loans graded special mention or worse have substantially declined from $24.4 million at December 31, 2015 to $13.4 million at December 31, 2016. However, as of December 31, 2016, 2016, $12.5 million of the $13.4 million are graded substandard as compared to the $1.8 million of the $24.4 million as of December 31, 2015. Management believes that the level of allowance for loan losses allocated to Commercial and Real estate loans has been adjusted accordingly.

During the year ended December 31, 2016, the company recorded a reverse provision for credit losses of $5,850,000 compared to a provision of $600,000 and $7,985,000 for the same periods in 2015 and 2014, respectively. The reversal from the allowance for credit losses is primarily the result of $5,566,000 in net loan loss recoveries and our assessment of the overall adequacy of the allowance for credit losses considering a number of factors as discussed in the "Allowance for Credit Losses" section.

During the years ended December 31, 2016, 2015 and 2014 the Company had net charge-offs (recoveries) totaling $(5,566,000), $(702,000), and $8,885,000 respectively. The net charge-off (recovery) ratio, which reflects net charge-offs (recoveries) to average loans, was (0.86)%, (0.12)% and 1.65% for 2016, 2015, and 2014, respectively. Nonperforming loans were $2,180,000 and $2,413,000 at December 31, 2016 and 2015, respectively. Nonperforming loans as a percentage of total loans were 0.29% at December 31, 2016 compared to 0.40% at December 31, 2015. The Company had no other real estate owned at December 31, 2016, December 31, 2015, and December 31, 2014. The carrying value of foreclosed assets was $362,000 at December 31, 2016, and is included in other assets on the consolidated balance sheets. No foreclosed assets were recorded at December 31, 2015 and December 31, 2014.

We had no loans past due, not including nonaccrual loans at December 31, 2016 compared to $136,000 at December 31, 2015. Excluding 2014, the Company has seen a decline in the amount of non-performing loans to an amount more in line with historical levels before the recession triggered by the financial crisis of 2008. Notwithstanding improvements in the economy, we anticipate weakness in economic conditions on national, state and local levels to continue. Continued economic pressures may negatively impact the financial condition of borrowers to whom the Company has extended credit and as a result we may be required to make further significant provisions to the allowance for credit losses in the future. Many farmers and ranchers have instituted improved farming practices including planting less acreage, as part of the mitigation for the cost of water delivery and the expense of pumping. We continue to closely monitor the

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water and the related issues affecting our customers. We have been and will continue to be proactive in looking for signs of deterioration within the loan portfolio in an effort to manage credit quality and work with borrowers where possible to mitigate any further losses. As of December 31, 2016, there were $49.5 million in classified loans of which $27.1 million related to agricultural real estate, $12.5 million to commercial and industrial loans, $3.8 million to real estate owner occupied, $1.4 million to real estate construction, and $2.7 million to commercial real estate. This compares to $31.8 million in classified loans as of December 31, 2015 of which $8.5 million related to agricultural real estate, $3.1 million to real estate construction, $1.8 million to commercial and industrial, $10.1 million to agricultural production, and $4.7 million to commercial real estate. The reduction in classified agricultural production loans relates to the refinance of a single loan which is now secured by agricultural real estate. The increase in classified agricultural real estate relates primarily to this single borrower with multiple loans totaling approximately $20.0 million which continues to perform under the terms of the loan agreements, while management has observed and continues to monitor some indications of deterioration in the borrower's overall financial condition. These changes in classified loans contributed to the shift in the amount of allowance for credit losses allocated between commercial loans and real estate loans.

As of December 31, 2016, we believe, based on all current and available information, the allowance for credit losses is adequate to absorb probable incurred losses within the loan portfolio; however, no assurance can be given that we may not sustain charge-offs which are in excess of the allowance in any given period. Refer to "Allowance for Credit Losses" below for further information.

Net Interest Income after Provision for Credit Losses

Net interest income, after the provision for credit losses was $51,430,000 for 2016 compared to $40,175,000 and $31,898,000 for 2015 and 2014, respectively.

Non-Interest Income

Non-interest income is comprised of customer service charges, gains on sales and calls of investment securities, income from appreciation in cash surrender value of bank owned life insurance, loan placement fees, Federal Home Loan Bank dividends, and other income. Non-interest income was $9,591,000 in 2016 compared to $9,387,000 and $8,164,000 in 2015 and 2014, respectively. The $204,000 or 2.17% increase in non-interest income in 2016 was due to increases in net realized gains on sales and calls of investment securities, loan placement fees, Federal Home Loan Bank dividends, and interchange fees compared to 2015, partially offset by a decrease in service charge income, appreciation in cash surrender value of bank owned life insurance, gain on other real estate owned, and other income. The $1,223,000 or 14.98% increases in non-interest income in 2015 compared to 2014 was due to increases in net realized gains on sales and calls of investment securities, loan placement fees, Federal Home Loan Bank dividends, and other income, partially offset by a decrease in service charge income, interchange fees, and appreciation in cash surrender value of bank owned life insurance.

Customer service charges decreased $48,000 to $3,022,000 in 2016 compared to $3,070,000 in 2015 and $3,280,000 in 2014. The decrease in 2016 from 2015 and in 2015 from 2014 was the result of lower NSF fees and lower analyzed service charge fee income.

During the year ended December 31, 2016, we realized net gains on sales and calls of investment securities of $1,920,000. In 2016, we recorded an other-than-temporary impairment loss of $136,000 as compared to none during the year ended December 31, 2015, and 2014. In 2015, we realized a net gain of $1,495,000 compared to a net gain of $904,000 in 2014 from sales and calls of investment securities. The net gains in 2016, 2015, and 2014 were the results of partial restructuring of the investment portfolio designed to improve the future performance of the portfolio. See Footnote 4 to the audited Consolidated Financial Statements for more detail.

Income from the appreciation in cash surrender value of bank owned life insurance (BOLI) totaled $558,000 in 2016 compared to $596,000 and $614,000 in 2015 and 2014, respectively. The Bank's salary continuation and deferred compensation plans and the related BOLI are used as a retention tool for directors and key executives of the Bank. Interchange fees totaled $1,228,000 in 2016 compared to $1,197,000 and $1,205,000 in 2015 and 2014, respectively. Part of the increases in 2016 was attributable to the SVB acquisition.

We earn loan placement fees from the brokerage of single-family residential mortgage loans provided for the convenience of our customers. Loan placement fees increased $41,000 in 2016 to $1,083,000 compared to $1,042,000 in 2015 and $544,000 in 2014. Fees were higher in 2016 compared to 2015 and 2014. Refinancing and new mortgage activity increased in 2016 and in 2015. In competing for mortgage loans in our market, we continue to see the historically low mortgage rates and first time home buyer tax incentives driving business in the mortgage market.

The Bank holds stock from the Federal Home Loan Bank in relationship with its borrowing capacity and generally receives quarterly dividends. As of December 31, 2016, we held $5,594,000 in FHLB stock compared to $4,823,000 at December 31, 2015. Dividends in 2016 increased to $630,000 compared to $580,000 in 2015 and $327,000 in 2014.

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Other income decreased to $1,286,000 in 2016 compared to $1,407,000 and $1,290,000 in 2015 and 2014, respectively. The period-to-period decrease in 2016 compared to 2015 was primarily due to the decrease in realized tax-free gain of $190,000 compared to $345,000 related to the collection of life insurance proceeds which is included in other income.

Non-Interest Expenses

Salaries and employee benefits, occupancy and equipment, regulatory assessments, acquisition and integration-related expenses, data processing expenses, ATM/Debit card expenses, license and maintenance contract expenses, and professional services (consisting of audit, accounting, consulting and legal fees) are the major categories of non-interest expenses. Non-interest expenses increased $2,906,000 or 8.07% to $38,922,000 in 2016 compared to $36,016,000 in 2015, and $35,338,000 in 2014. The net increase period-over-period is primarily due to the SVB acquisition and integration expenses of $1,782,000 and various items discussed below.

Our efficiency ratio, measured as the percentage of non-interest expenses (exclusive of amortization of core deposit intangibles, other real estate owned, and repossessed asset expenses) to net interest income before provision for credit losses plus non-interest income (exclusive of realized gains or losses on sale and calls of investments) was 68.45% for 2016 compared to 69.22% for 2015 and 69.33% for 2014. The improvement in the efficiency ratio in 2016 and 2015 is due to the growth in revenues outpacing the growth in non-interest expense.

Salaries and employee benefits increased $1,045,000 or 5.02% to $21,881,000 in 2016 compared to $20,836,000 in 2015 and $19,721,000 in 2014. Full time equivalents were 277 for the year ended December 31, 2016 compared to 273 for the year ended December 31, 2015. The increase in salaries and employee benefits in 2016 compared to 2015 is a result of higher overall salary and benefit expenses; however, direct loan origination costs including salaries and employee benefits, which are capitalized and expensed as an adjustment to interest and fees on loans increased during 2016 compared to 2015. The SVB acquisition attributed to approximately $426,000 of the increase in 2016.

For the years ended December 31, 2016, 2015, and 2014, the compensation cost recognized for share based compensation was $284,000, $238,000 and $173,000, respectively. As of December 31, 2016, there was $1,067,000 of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under all plans. The cost is expected to be recognized over a weighted average period of 3.70 years. See Notes 1 and 15 to the audited Consolidated Financial Statements for more detail. No options to purchase shares of the Company's common stock were issued during the years ending December 31, 2016 and 2015. Restricted stock awards of 54,650 shares and 9,268 shares were awarded in 2016 and 2015, respectively.

Occupancy and equipment expense increased $85,000 or 1.82% to $4,754,000 in 2016 compared to $4,669,000 in 2015 and $4,835,000 in 2014. The addition of three new branches from the SVB acquisition resulted in approximately $68,000 increase in rent expense. The decrease in 2015 was the result of the closure of an ATM location in Visalia. The Company made no changes in depreciation expense methodology.

Regulatory assessments decreased $417,000 or 39.38% to $642,000 in 2016 compared to $1,059,000 and $762,000 in 2015 and 2014, respectively. The assessment base for calculating the amount owed is average assets minus average tangible equity. Beginning in the third quarter of 2016, the FDIC approved a final rule revising DIF assessment formulas which resulted in lower assessments for the Company. The higher assessment rate in 2015 was a result of changes in credit quality ratios used in determining the assessment rate along with higher average assets.

Data processing expenses were $1,707,000 in 2016 compared to $1,139,000 in 2015 and $1,820,000 in 2014. The $568,000 or 49.87% increase in 2016 primarily resulted from transitioning to a new provider for data transmission.

Acquisition and integration expenses related to the SVB merger were $1,782,000 in 2016 compared to none in 2015.

Professional services decreased $246,000 in 2016 compared to 2015.

Amortization of core deposit intangibles was $149,000 for 2016, $320,000 for 2015, and $337,000 for 2014. During 2016, amortization expense related to SVB core deposit intangible (CDI) was $12,000, and amortization expense related to VCB CDI was $137,000. During 2015, amortization expense related to Service 1st Bank CDI was $183,000, and amortization expense related to VCB CDI was $137,000. During 2014, amortization expense related to Service 1st Bank CDI was $200,000, and amortization expense related to VCB CDI was $137,000.

ATM/Debit card expenses increased $85,000 to $633,000 for the year ended December 31, 2016 compared to $548,000 in 2015 and $624,000 in 2014. License and maintenance contracts increased $11,000 to $531,000 for the year ended December 31, 2016 compared to $520,000 and $488,000 in 2015 and 2014, respectively. Other non-interest expenses decreased $136,000 or 3.71% to $3,801,000 in 2016 compared to $3,665,000 in 2015 and $3,965,000 in 2014.

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The following table describes significant components of other non-interest expense as a percentage of average assets.

For the years ended December 31, (Dollars in thousands)	Other Expense 2016	% Average Assets	Other Expense 2015	% Average Assets	Other Expense 2014	% Average Assets
Stationery/supplies	$ 247	0.02 %	$ 269	0.02 %	$ 266	0.02 %
Amortization of software	257	0.02 %	240	0.02 %	224	0.02 %
Director fees and related expenses	333	0.03 %	306	0.03 %	262	0.02 %
Telephone	357	0.03 %	292	0.02 %	230	0.02 %
Postage	200	0.02 %	212	0.02 %	238	0.02 %
Armored courier fees	227	0.02 %	218	0.02 %	221	0.01 %
Risk management expense	150	0.01 %	163	0.01 %	207	0.01 %
Loss on sale or write-down of assets	4	— %	6	— %	201	— %
Donations	171	0.01 %	185	0.02 %	179	0.01 %
Personnel other	161	0.01 %	173	0.01 %	154	0.01 %
Credit card expense	196	0.01 %	124	0.01 %	95	0.01 %
Education/training	154	0.01 %	148	0.01 %	135	0.01 %
General insurance	159	0.01 %	150	0.01 %	141	0.01 %
Appraisal fees	86	0.01 %	66	0.01 %	130	0.01 %
Operating losses	175	0.01 %	56	— %	53	0.01 %
Other	924	0.07 %	1,057	0.09 %	1,229	0.14 %
Total other non-interest expense	$ 3,801	0.29 %	$ 3,665	0.30 %	$ 3,965	0.32 %

Provision for Income Taxes

Our effective income tax rate was 31.3% for 2016 compared to 19.1% for 2015 and (12.0)% for 2014. The Company reported an income tax provision (benefit) of $6,917,000, $2,582,000, and $(570,000) for the years ended December 31, 2016, 2015, and 2014, respectively. The effective tax rate in 2016 was affected by the large negative provision for credit losses which resulted in higher pretax and taxable income and also diluted the impact of the Company’s tax exempt municipal bonds and other tax planning strategies. In addition, changes in the Company’s effective tax rate, other than changes in the level of income before taxes, were due in part to changes in tax law which limited the use of various tax credits and incentives beginning in 2014.

FINANCIAL CONDITION

Summary of Changes in Consolidated Balance Sheets

December 31, 2016 compared to December 31, 2015.

Total assets were $1,443,323,000 as of December 31, 2016, compared to $1,276,736,000 as of December 31, 2015, an increase of 13.05% or $166,587,000. Total gross loans were $756,628,000 as of December 31, 2016, compared to $598,111,000 as of December 31, 2015, an increase of $158,517,000 or 26.50%. The total investment portfolio (including Federal funds sold and interest-earning deposits in other banks) decreased 3.86% or $22,412,000 to $558,132,000. Total deposits increased 12.52% or $139,712,000 to $1,255,979,000 as of December 31, 2016, compared to $1,116,267,000 as of December 31, 2015. Shareholders’ equity increased $24,710,000 or 17.74% to $164,033,000 as of December 31, 2016, compared to $139,323,000 as of December 31, 2015. The increase in shareholders’ equity was driven by the issuance of stock in connection with the Sierra Vista Bank acquisition, as well as the retention of earnings, net of dividends paid, partially offset by a decrease in unrealized gains on available-for-sale securities recorded in accumulated other comprehensive income (AOCI). Accrued interest payable and other liabilities were $17,756,000 as of December 31, 2016, compared to $15,991,000 as of December 31, 2015, an increase of $1,765,000.

Fair Value

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The Company measures the fair value of its financial instruments utilizing a hierarchical framework associated with the level of observable pricing scenarios utilized in measuring financial instruments at fair value. The degree of judgment utilized in measuring the fair value of financial instruments generally correlates to the level of the observable pricing scenario. Financial instruments with readily available actively quoted prices or for which fair value can be measured from actively quoted prices generally will have a higher degree of observable pricing and a lesser degree of judgment utilized in measuring fair value. Conversely, financial instruments rarely traded or not quoted will generally have little or no observable pricing and a higher degree of judgment utilized in measuring fair value. Observable pricing scenarios are impacted by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established and the characteristics specific to the transaction.

See Note 3 of the Notes to Consolidated Financial Statements for additional information about the level of pricing transparency associated with financial instruments carried at fair value.

Investments

The following table reflects the balances for each category of securities at year end:

Available-for-Sale Securities	Amortized Cost at December 31,		
(In thousands)	2016	2015	2014
U.S. Government agencies	$69,005	$52,803	$33,088
Obligations of states and political subdivisions	288,543	181,785	143,343
U.S. Government sponsored entities and agencies collateralized by residential mortgage obligations	181,785	225,636	236,629
Private label residential mortgage backed securities	1,807	2,356	3,079
Other equity securities	7,500	7,500	7,500
Total Available-for-Sale Securities	$548,640	$470,080	$423,639

Held-to-Maturity Securities			
(In thousands)	2016	2015	2014
Obligations of states and political subdivisions	$—	$31,712	$31,964

Our investment portfolio consists primarily of U.S. Government sponsored entities and agencies collateralized by residential mortgage backed obligations and obligations of states and political subdivision securities and are classified at the date of acquisition as available-for-sale or held-to-maturity. As of December 31, 2016, investment securities with a fair value of $88,903,000, or 16.23% of our investment securities portfolio, were held as collateral for public funds, short and long-term borrowings, treasury, tax, and for other purposes. Our investment policies are established by the Board of Directors and implemented by our Investment/Asset Liability Committee. They are designed primarily to provide and maintain liquidity, to enable us to meet our pledging requirements for public money and borrowing arrangements, to generate a favorable return on investments without incurring undue interest rate and credit risk, and to complement our lending activities.

The level of our investment portfolio is generally considered higher than our peers due primarily to a comparatively low loan-to-deposit ratio. Our loan-to-deposit ratio at December 31, 2016 was 60.24% compared to 53.58% at December 31, 2015. The loan to deposit ratio of our peers was 78.96% at December 31, 2016. Peer group information from SNL Financial data includes bank holding companies in central California with assets from $600 million to $2.5 billion. The total investment portfolio, including Federal funds sold and interest-earning deposits in other banks, decreased 3.86% or $22,412,000 to $558,132,000 at December 31, 2016, from $580,544,000 at December 31, 2015. The market value of the portfolio reflected an unrealized loss of $891,000 at December 31, 2016, compared to an unrealized gain of $7,474,000 at December 31, 2015.

Losses recognized in 2016, 2015, and 2014 were incurred in order to reposition the investment securities portfolio based on the current rate environment. The securities which were sold at a loss were acquired when the rate environment was not as volatile. The securities which were sold were primarily purchased several years ago to serve a purpose in the rate environment in which the securities were purchased. The Company is addressing risks in the security portfolio by selling these securities and using proceeds to purchase securities that fit with the Company's current risk profile.

During 2014, to better manage our interest rate risk, the Company transferred from available-for-sale to held-to-maturity selected municipal securities in our portfolio having a book value of approximately $31 million, a market value of approximately $32 million, and a net unrecognized gain of approximately $163,000. This transfer was completed after careful consideration of our intent and ability to hold these securities to maturity. During the first quarter of 2016, management sold certain investment securities of which management identified that five of the 13 securities sold were previously designated as held-to-maturity (HTM). Through an oversight during the portfolio restructuring analysis related to this transaction, management unintentionally sold these five HTM securities. The book value of the HTM securities sold was $8.5 million. The gain realized on the sale of the HTM securities was $696,000. As such, management was required to reclassify the remaining HTM securities with a fair value of $23.1 million to the AFS designation. At December 31, 2016 and December 31, 2015 the remaining unaccreted balance of these HTM securities associated with the original transfer from AFS to HTM and included in accumulated other comprehensive income was $0 and $64,000, respectively.

We periodically evaluate each investment security for other-than-temporary impairment, relying primarily on industry analyst reports, observation of market conditions and interest rate fluctuations. The portion of the impairment that is attributable to a shortage in the present value of expected future cash flows relative to the amortized cost should be recorded as a current period charge to earnings. The discount rate in this analysis is the original yield expected at time of purchase.

As of December 31, 2016, the Company performed an analysis of the investment portfolio to determine whether any of the investments held in the portfolio had an other-than-temporary impairment (OTTI). Management evaluated all investment securities with an unrealized loss at December 31, 2016, and identified those that had an unrealized loss for at least a consecutive 12 month period, which had an unrealized loss at December 31, 2016 greater than 10% of the recorded book value on that date, or which had an unrealized loss of more than $10,000. Management also analyzed any securities that may have been downgraded by credit rating agencies.

For those bonds that met the evaluation criteria, management obtained and reviewed the most recently published national credit ratings for those bonds. For those bonds that were obligations of states and political subdivisions with an investment grade rating by the rating agencies, management also evaluated the financial condition of the municipality and any applicable municipal bond insurance provider and concluded during March 2016 that a $136,000 credit related impairment related to one security with a fair value of $2,995,000 and a pre-impairment amortized cost of $3,131,000 existed. The Company recorded an other-than-temporary impairment loss of $136,000 during the twelve months ended December 31, 2016. There were no OTTI losses recorded during the twelve months ended December 31, 2015.

At December 31, 2016, the Company had a total of 16 PLRMBS with a remaining principal balance of $1,807,000 and a net unrealized gain of approximately $1,036,000. Twelve of these PLRMBS with a remaining principal balance of $2,707,000 had credit ratings below investment grade. The Company continues to monitor these securities for changes in credit ratings or other indications of credit deterioration. No credit related OTTI charges related to PLRMBS were recorded during the year ended December 31, 2016.

The amortized cost, maturities and weighted average yield of investment securities at December 31, 2016 are summarized in the following table.

(Dollars in thousands)	In one year or less		After one through five years		After five through ten years		After ten years		Total	
Available-for-Sale Securities	Amount	Yield(1)	Amount	Yield(1)	Amount	Yield(1)	Amount	Yield(1)	Amount	Yield(1)
Debt securities(1)										
U.S. Government agencies	$—	—	$—	—	$10,745	4.40 %	$58,260	4.30 %	$69,005	4.31 %
Obligations of states and political subdivisions (2)	—	—	15,145	3.49 %	35,667	3.97 %	237,731	4.78 %	288,543	4.61 %
U.S. Government sponsored entities and agencies collateralized by residential mortgage obligations	—	—	2,709	4.54 %	3,190	3.48 %	175,886	3.81 %	181,785	3.81 %
Private label residential mortgage backed securities	—	—	142	4.74 %	4	5.00 %	1,661	5.91 %	1,807	5.81 %
Other equity securities	7,500	2.27 %	—	—	—	—	—	—	7,500	2.27 %
	$7,500	2.27 %	$17,996	3.66 %	$49,606	4.03 %	$473,538	4.36 %	$548,640	4.31 %

(1) Expected maturities will differ from contractual maturities because the issuers of the securities may have the right to call or prepay obligations with or without call or prepayment penalties. Expected maturities will also differ from contractual maturities due to unscheduled principal pay downs.
(2) Not computed on a tax equivalent basis.

Loans

Total gross loans increased $158,517,000 or 26.50% to $756,628,000 as of December 31, 2016, compared to $598,111,000 as of December 31, 2015.

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The following table sets forth information concerning the composition of our loan portfolio as of and for the years ended December 31, 2016, 2015, 2014, 2013, and 2012.

Loan Type (Dollars in thousands)	2016 Amount	% of Total Loans	2015 Amount	% of Total Loans	2014 Amount	% of Total Loans	2013 Amount	% of Total Loans	2012 Amount	% of Total Loans
Commercial:										
Commercial and industrial	$88,652	11.7 %	$102,197	17.1 %	$89,007	15.5 %	$87,082	17.0 %	$77,956	19.7 %
Agricultural land and production	25,509	3.4 %	30,472	5.1 %	39,140	6.8 %	31,649	6.1 %	26,599	6.7 %
Total commercial	114,161	15.1 %	132,669	22.2 %	128,147	22.3 %	118,731	23.1 %	104,555	26.4 %
Real estate:										
Owner occupied	191,665	25.3 %	168,910	28.2 %	176,804	30.9 %	156,781	30.6 %	114,444	28.9 %
Real estate-construction and other land loans	69,200	9.1 %	38,685	6.5 %	38,923	6.8 %	42,329	8.3 %	33,199	8.4 %
Commercial real estate	184,225	24.3 %	117,244	19.6 %	106,788	18.7 %	86,117	16.8 %	53,797	13.6 %
Agricultural real estate	86,761	11.5 %	74,867	12.5 %	57,501	10.0 %	44,164	8.6 %	28,400	7.2 %
Other real estate	18,945	2.7 %	10,520	1.8 %	6,611	1.2 %	4,548	0.9 %	8,098	2.0 %
Total real estate	550,796	72.9 %	410,226	68.6 %	386,627	67.6 %	333,939	65.2 %	237,938	60.1 %
Consumer:										
Equity loans and lines of credit	64,494	8.5 %	42,296	7.1 %	47,575	8.3 %	48,594	9.5 %	42,932	10.9 %
Consumer and installment	25,910	3.5 %	12,503	2.1 %	10,093	1.8 %	11,252	2.2 %	10,346	2.6 %
Total consumer	90,404	12.0 %	54,799	9.2 %	57,668	10.1 %	59,846	11.7 %	53,278	13.5 %
Deferred loan fees, net	1,267		417		146		(159)		(453)	
Total gross loans (1)	756,628	100.0%	598,111	100.0%	572,588	100.0%	512,357	100.0%	395,318	100.0%
Allowance for credit losses	(9,326)		(9,610)		(8,308)		(9,208)		(10,133)	
Total loans (1)	$747,302		$588,501		$564,280		$503,149		$385,185	
(1) Includes nonaccrual loans of:	$2,180		$2,413		$14,052		$7,586		$9,695	

At December 31, 2016, loans acquired in the SVB and VCB acquisitions had a balance of $168,296,000, of which $7,239,000 were commercial loans, $129,520,000 were real estate loans, and $31,537,000 were consumer loans. At December 31, 2015, loans acquired in the VCB acquisition had a balance of $62,395,000, of which $1,617,000 were commercial loans, $51,576,000 were real estate loans, and $9,202,000 were consumer loans.

At December 31, 2016, in management's judgment, a concentration of loans existed in commercial loans and real-estate-related loans, representing approximately 96.5% of total loans of which 15.1% were commercial and 81.4% were real-estate-related. This level of concentration is consistent with 97.9% at December 31, 2015. Although we believe the loans within this concentration have no more than the normal risk of collectability, a substantial decline in the performance of the economy in general or a decline in real estate values in our primary market areas, in particular, could have an adverse impact on collectability, increase the level of real estate-related nonperforming loans, or have other adverse effects which alone or in the aggregate could have a material adverse effect on our business, financial condition, results of operations and cash flows. The Company was not involved in any sub-prime mortgage lending activities at December 31, 2016 and 2015.

We believe that our commercial real estate loan underwriting policies and practices result in prudent extensions of credit, but recognize that our lending activities result in relatively high reported commercial real estate lending levels. Commercial real estate loans include certain loans which represent low to moderate risk and certain loans with higher risks.

The Board of Directors review and approve concentration limits and exceptions to limitations of concentration are reported to the Board of Directors at least quarterly.

Loan Maturities

The following table presents information concerning loan maturities and sensitivity to changes in interest rates of the indicated categories of our loan portfolio, as well as loans in those categories maturing after one year that have fixed or floating interest rates at December 31, 2016.

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(In thousands)	One Year or Less	After One Through Five Years	After Five Years	Total
Loan Maturities:				
Commercial and agricultural	$ 73,243	$ 21,694	$ 19,224	$ 114,161
Real estate construction and other land loans	55,809	4,162	9,229	69,200
Other real estate	47,152	69,067	365,377	481,596
Consumer and installment	9,994	8,464	71,946	90,404
	$ 186,198	$ 103,387	$ 465,776	$ 755,361
Sensitivity to Changes in Interest Rates:				
Loans with fixed interest rates	$ 56,936	$ 67,120	$ 59,980	$ 184,036
Loans with floating interest rates (1)	129,262	36,268	405,795	571,325
	$ 186,198	$ 103,388	$ 465,775	$ 755,361
(1) Includes floating rate loans which are currently at their floor rate in accordance with their respective loan agreement	$ 26,084	$ 32,228	$ 284,506	$ 342,818

Nonperforming Assets

Nonperforming assets consist of nonperforming loans, other real estate owned (OREO), and repossessed assets. Nonperforming loans are those loans which have (i) been placed on nonaccrual status; (ii) been classified as doubtful under our asset classification system; or (iii) become contractually past due 90 days or more with respect to principal or interest and have not been restructured or otherwise placed on nonaccrual status. A loan is classified as nonaccrual when 1) it is maintained on a cash basis because of deterioration in the financial condition of the borrower; 2) payment in full of principal or interest under the original contractual terms is not expected; or 3) principal or interest has been in default for a period of 90 days or more unless the loan is both well secured and in the process of collection. We measure all loans placed on nonaccrual status for impairment based on the fair value of the underlying collateral or the net present value of the expected cash flows.

Our consolidated financial statements are prepared on the accrual basis of accounting, including the recognition of interest income on loans. Interest income from nonaccrual loans is recorded only if collection of principal in full is not in doubt and when cash payments, if any, are received.

Loans are placed on nonaccrual status and any accrued but unpaid interest income is reversed and charged against income when the payment of interest or principal is 90 days or more past due. Loans in the nonaccrual category are treated as nonaccrual loans even though we may ultimately recover all or a portion of the interest due. These loans return to accrual status when the loan becomes contractually current, future collectability of amounts due is reasonably assured, and a minimum of six months of satisfactory principal repayment performance has occurred. See Note 5 of the Company’s audited Consolidated Financial Statements in Item 8 of this Annual Report.

At December 31, 2016, total nonperforming assets totaled $2,542,000, or 0.18% of total assets, compared to $2,413,000, or 0.19% of total assets at December 31, 2015. Total nonperforming assets at December 31, 2016, included nonaccrual loans totaling $2,180,000, no OREO, and $362,000 in repossessed assets. Nonperforming assets at December 31, 2015 consisted of $2,413,000 in nonaccrual loans, no OREO, and no repossessed assets. At December 31, 2016, we had one loan considered a troubled debt restructuring (“TDR”) totaling $20,000 which is included in nonaccrual loans compared to four TDRs totaling $1,337,000 at December 31, 2015. We have no outstanding commitments to lend additional funds to any of these borrowers. See Note 5 of the Company’s audited Consolidated Financial Statements in Item 8 of this Annual Report concerning our recorded investment in loans for which impairment has been recognized.

A summary of nonaccrual, restructured, and past due loans at December 31, 2016, 2015, 2014, 2013, and 2012 is set forth below. The Company had no loans past due more than 90 days and still accruing interest at December 31, 2016 and 2015. Management is not aware of any potential problem loans, which were current and accruing at

December 31, 2016, where serious doubt exists as to the ability of the borrower to comply with the present repayment terms. Management can give no assurance that nonaccrual and other nonperforming loans will not increase in the future.

Composition of Nonaccrual, Past Due and Restructured Loans

(As of December 31, Dollars in thousands)	2016	2015	2014	2013	2012
Nonaccrual Loans:					
Commercial and industrial	$447	$—	$7,265	$335	$—
Owner occupied real estate	87	324	1,363	1,777	213
Agricultural real estate	—	—	360	—	—
Commercial real estate	1,082	567	1,468	158	—
Equity loans and line of credit	526	172	1,751	721	237
Consumer and installment	18	13	19	—	—
Restructured loans (non-accruing):					
Commercial and industrial	—	29	—	1,192	—
Owner occupied	20	23	—	384	1,362
Real estate construction and other land loans	—	—	547	1,450	6,288
Commercial real estate	—	—	—	—	—
Equity loans and line of credit	—	1,285	1,279	1,565	1,595
Consumer and Installment	—	—	—	4	—
Total nonaccrual	2,180	2,413	14,052	7,586	9,695
Accruing loans past due 90 days or more	—	—	—	—	—
Total nonperforming loans	$2,180	$2,413	$14,052	$7,586	$9,695
Interest foregone	$245	$340	$716	$661	$693
Nonperforming loans to total loans	0.29 %	0.40 %	2.45 %	1.48 %	2.45 %
Accruing loans past due 90 days or more	$—	$—	$—	$—	$—
Accruing troubled debt restructurings	$3,089	$4,286	$4,774	$5,771	$7,410
Ratio of nonperforming loans to allowance for credit losses	23.38 %	25.11 %	169.14 %	82.38 %	95.68 %
Loans considered to be impaired	$5,269	$6,699	$18,826	$13,357	$17,105
Related allowance for credit losses on impaired loans	$307	$164	$612	$1,007	$510

As of December 31, 2016 and 2015, we had impaired loans totaling $5,269,000 and $6,699,000, respectively. We measure our impaired loans by using the fair value of the collateral if the loan is collateral dependent and the present value of the expected future cash flows discounted at the loan's original contractual interest rate if the loan is not collateral dependent. Impaired loans are identified from internal credit review reports, past due reports, overdraft listings, and third party reports of examination. Borrowers experiencing problems such as operating losses, marginal working capital, inadequate cash flow or business interruptions which jeopardize collection of the loan are also reviewed for possible impairment classification. A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the original agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on 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. Loans determined to be impaired are individually evaluated for impairment. When a loan is impaired, the Company 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. For collateral dependent loans secured by real estate, we obtain external appraisals which are updated at least annually to determine the fair

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value of the collateral, and we record an immediate charge off for the difference between the book value of the loan and the appraised value less selling costs of the collateral. We perform quarterly internal reviews on substandard loans.

We place loans on nonaccrual status and classify them as impaired when it becomes probable that we will not receive interest and principal under the original contractual terms, or when loans are delinquent 90 days or more, unless the loan is both well secured and in the process of collection. Management maintains certain loans that have been brought current by the borrower (less than 30 days delinquent) on nonaccrual status until such time as management has determined that the loans are likely to remain current in future periods. Foregone interest on nonaccrual loans totaled $245,000 for the year ended December 31, 2016 of which $2,000 was attributable to troubled debt restructurings. Foregone interest on nonaccrual loans totaled $340,000 and $716,000 for the years ended December 31, 2015 and 2014, respectively of which $104,000 and $139,000 was attributable to troubled debt restructurings, respectively.

The following table provides a reconciliation of the change in non-accrual loans for the year ended December 31, 2016.

(In thousands)	Balances December 31, 2015	Additions to Nonaccrual Loans	Net Pay Downs	Transfer to Foreclosed Collateral	Returns to Accrual Status	Charge Offs	Balances December 31, 2016
Non-accrual loans:							
Commercial and industrial	$ —	$ 1,741	$ (405)	$ (321)	$ —	$ (568)	$ 447
Real estate	891	832	(387)	—	(167)	—	1,169
Real estate construction and land development	—	—	—	—	—	—	—
Agricultural real estate	—	—	—	—	—	—	—
Equity loans and lines of credit	172	608	(128)	—	(30)	(96)	526
Consumer	13	72	(8)	(41)	—	(18)	18
Restructured loans (non-accruing):							
Commercial and industrial	29	—	(29)	—	—	—	—
Real estate	23	—	(3)	—	—	—	20
Real estate construction and land development	—	—	—	—	—	—	—
Equity loans and lines of credit	1,285	—	(1,285)	—	—	—	—
Total non-accrual	$ 2,413	$ 3,253	$ (2,245)	$ (362)	$ (197)	$ (682)	$ 2,180

The following table provides a summary of the annual change in the OREO balance:

(In thousands)	Years Ended December 31, 2016	2015
Balance, beginning of year	$ —	$ —
Additions	—	227
1st lien assumed upon foreclosure	—	121
Dispositions	—	(359)
Write-downs	—	—
Net gain on disposition	—	11
Balance, end of year	$ —	$ —

OREO represents real property taken either through foreclosure or through a deed in lieu thereof from the borrower. OREO is carried at the lesser of cost or fair market value less selling costs. As of December 31, 2016 the Bank had no

OREO properties. The carrying value of foreclosed assets was $362,000 at December 31, 2016, and is included in other assets on the consolidated balance sheets. No foreclosed assets were recorded at December 31, 2015.
As of December 31, 2015 the Bank had no OREO properties. In 2015, the Bank foreclosed on one property collateralized by real estate. Proceeds from OREO sales totaled $359,000 during 2015. The Company realized $11,000 in net gains from the sale of all properties.

Allowance for Credit Losses

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We have established a methodology for determining the adequacy of the allowance for credit losses made up of general and specific allocations. The methodology is set forth in a formal policy and takes into consideration the need for an overall allowance for credit losses as well as specific allowances that are tied to individual loans. The allowance for credit losses is an estimate of probable incurred credit losses in the Company's loan portfolio. The allowance consists of two primary components, specific reserves related to impaired loans and general reserves for probable incurred losses related to loans that are not impaired.

For all portfolio segments, the determination of the general reserve for loans that are not impaired is based on estimates made by management, including but not limited to, consideration of historical losses by portfolio segment (and in certain cases peer loss data) over the most recent 20 quarters, and qualitative factors including economic trends in the Company's service areas, industry experience and trends, geographic concentrations, estimated collateral values, the Company's underwriting policies, the character of the loan portfolio, and probable losses incurred in the portfolio taken as a whole. Management has determined that the most recent 20 quarters was an appropriate look-back period based on several factors including the current global economic uncertainty and various national and local economic indicators, and a time period sufficient to capture enough data due to the size of the portfolio to produce statistically accurate historical loss calculations. We believe this period is an appropriate look-back period.

In originating loans, we recognize that losses will be experienced and that the risk of loss will vary with, among other things, the type of loan being made, the creditworthiness of the borrower over the term of the loan, general economic conditions and, in the case of a secured loan, the quality of the collateral securing the loan. The allowance is increased by provisions charged against earnings and recoveries, and reduced by net loan charge offs. Loans are charged off when they are deemed to be uncollectible, or partially charged off when portions of a loan are deemed to be uncollectible. Recoveries are generally recorded only when cash payments are received.

The allowance for credit losses is maintained to cover probable incurred credit losses in the loan portfolio. The responsibility for the review of our assets and the determination of the adequacy lies with management and our Audit Committee. They delegate the authority to the Senior Risk Manager and the Chief Credit Officer (CCO) to determine the loss reserve ratio for each type of asset and to review, at least quarterly, the adequacy of the allowance based on an evaluation of the portfolio, past experience, prevailing market conditions, amount of government guarantees, concentration in loan types and other relevant factors.

The allowance for credit losses is an estimate of the probable incurred credit losses in our loan and lease portfolio. The allowance is based on principles of accounting: (1) losses accrued for on loans when they are probable of occurring and can be reasonably estimated and (2) losses accrued based on the differences between the value of collateral, present value of future cash flows or values that are observable in the secondary market and the loan balance.

Management adheres to an internal asset review system and loss allowance methodology designed to provide for timely recognition of problem assets and adequate valuation allowances to cover probable incurred losses. The Bank's asset monitoring process includes the use of asset classifications to segregate the assets, largely loans and real estate, into various risk categories. The Bank uses the various asset classifications as a means of measuring risk and determining the adequacy of valuation allowances by using a nine-grade system to classify assets. In general, all credit facilities exceeding 90 days of delinquency require classification and are placed on nonaccrual.

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The following table summarizes the Company's loan loss experience, as well as provisions and recoveries (charge-offs) to the allowance and certain pertinent ratios for the periods indicated:

(Dollars in thousands)	2016	2015	2014	2013	2012
Loans outstanding at December 31,	$755,361	$597,694	$572,442	$512,516	$395,771
Average loans outstanding during the year	$646,573	$586,762	$539,529	$454,483	$405,040
Allowance for credit losses:					
Balance at beginning of year	$9,610	$8,308	$9,208	$10,133	$11,396
Deduct loans charged off:					
Commercial and industrial	(621)	(802)	(7,423)	(713)	(123)
Agricultural production	—	—	(1,722)	—	—
Owner occupied	—	—	(183)	(281)	(217)
Real estate construction and other land loans	—	—	—	—	(319)
Commercial real estate	—	—	—	(4)	(1,430)
Consumer loans	(262)	(159)	(506)	(448)	(761)
Total loans charged off	(883)	(961)	(9,834)	(1,446)	(2,850)
Add recoveries of loans previously charged off:					
Commercial and industrial	3,656	954	171	315	515
Agricultural production	1,631	90	—	—	—
Owner occupied	—	—	150	—	45
Real estate construction and other land loans	702	32	364	16	—
Commercial real estate	283	—	—	—	—
Consumer loans	177	587	264	190	327
Total recoveries	6,449	1,663	949	521	887
Net recoveries (charge offs)	5,566	702	(8,885)	(925)	(1,963)
(Reversal) Provision charged to credit losses	(5,850)	600	7,985	—	700
Balance at end of year	$9,326	$9,610	$8,308	$9,208	$10,133
Allowance for credit losses as a percentage of outstanding loan balance	1.23%	1.61%	1.45%	1.80%	2.56%
Net recoveries (charge offs) to average loans outstanding	0.86%	0.12%	(1.65)%	(0.20)%	(0.48)%

Managing credits identified through the risk evaluation methodology includes developing a business strategy with the customer to mitigate our losses. Our management continues to monitor these credits with a view to identifying as early as possible when, and to what extent, additional provisions may be necessary.

The allowance for credit losses is reviewed at least quarterly by the Bank's and our Board of Directors' Audit/Compliance Committee. Reserves are allocated to loan portfolio segments using percentages which are based on both historical risk elements such as delinquencies and losses and predictive risk elements such as economic, competitive and environmental factors. We have adopted the specific reserve approach to allocate reserves to each impaired asset for the purpose of estimating potential loss exposure. Although the allowance for credit losses is allocated to various portfolio categories, it is general in nature and available for the loan portfolio in its entirety. Additions may be required based on the results of independent loan portfolio examinations, regulatory agency examinations, or our own internal review process. Additions are also required when, in management's judgment, the reserve does not properly reflect the potential loss exposure.

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The allocation of the allowance for credit losses is set forth below:

Loan Type (Dollars in thousands)	2016 Amount	Percent of Loans in Each Category to Total Loans	2015 Amount	Percent of Loans in Each Category to Total Loans	2014 Amount	Percent of Loans in Each Category to Total Loans	2013 Amount	Percent of Loans in Each Category to Total Loans	2012 Amount	Percent of Loans in Each Category to Total Loans
Commercial:										
Commercial and industrial	$1,884	11.7 %	$3,143	17.1 %	$2,753	15.5 %	$1,928	17 %	$2,071	19.7 %
Agricultural land and production	296	3.4 %	419	5.1 %	377	6.8 %	516	6.1 %	605	6.7 %
Real estate:										
Owner occupied	1,408	25.3 %	1,556	28.2 %	1,380	30.9 %	1,697	30.6 %	2,153	28.9 %
Real estate construction and other land loans	698	9.1 %	694	6.5 %	837	6.8 %	1,289	8.3 %	1,035	8.4 %
Commercial real estate	1,969	24.3 %	1,686	19.6 %	1,201	18.7 %	1,406	16.8 %	1,886	13.6 %
Agricultural real estate	1,969	11.5 %	1,149	12.5 %	564	10 %	672	8.6 %	646	7.2 %
Other real estate	156	2.7 %	119	1.8 %	76	1.2 %	110	0.9 %	157	2 %
Consumer:										
Equity loans and lines of credit	483	8.5 %	500	7.1 %	811	8.3 %	874	9.5 %	1,158	10.9 %
Consumer and installment	369	3.5 %	234	2.1 %	267	1.8 %	294	2.2 %	383	2.6 %
Unallocated reserves	94		110		42		422		39	
Total allowance for credit losses	$9,326	100 %	$9,610	100 %	$8,308	100 %	$9,208	100 %	$10,133	100 %

Loans are charged to the allowance for credit losses when the loans are deemed uncollectible. It is the policy of management to make additions to the allowance so that it remains adequate to cover all probable loan charge offs that exist in the portfolio at that time. We assign qualitative and environmental factors (Q factors) to each loan category. Q factors include reserves held for the effects of lending policies, economic trends, and portfolio trends along with other dynamics which may cause additional stress to the portfolio.

As of December 31, 2016, the allowance for credit losses (ALLL) stood at $9,326,000, compared to $9,610,000 at December 31, 2015, a net decrease of $284,000. The decrease in the ALLL was due to net recoveries and a reverse provision for credit losses during the year ended December 31, 2016 which was necessitated by management's observations and assumptions about the existing credit quality of the loan portfolio. Net recoveries totaled $5,566,000 while the reversal of provision for credit losses was $5,850,000. The balance of classified loans and loans graded special mention, totaled $49,464,000 and $29,911,000 at December 31, 2016 and $31,764,000 and $28,719,000 at December 31, 2015. This increase in classified loans necessitated additional allocation within the ALLL; however it was offset by improvements in qualitative factors (moderating drought conditions), as well as relative improvements in loss trends, past dues, and other credit variables, causing the allowance level to decrease. The balance of undisbursed commitments to extend credit on construction and other loans and letters of credit was $259,415,000 as of December 31, 2016, compared to $217,166,000 as of December 31, 2015. At December 31, 2016 and 2015, the balance of a contingent allocation for probable loan loss experience on unfunded obligations was $125,000 and $150,000, respectively. The contingent allocation for probable loan loss experience on unfunded obligations is calculated by management using an appropriate, systematic, and consistently applied process. While related to credit losses, this allocation is not a part of ALLL and is considered separately as a liability for accounting and regulatory reporting purposes. Risks and uncertainties exist in all lending transactions and our management and Directors' Loan Committee have established reserve levels based on economic uncertainties and other risks that exist as of each

reporting period.
The ALLL as a percentage of total loans was 1.23% at December 31, 2016, and 1.61% at December 31, 2015. Total loans include SVB and VCB loans that were recorded at fair value in connection with the acquisitions of $168,296,000 at December 31, 2016 and $62,395,000 at December 31, 2015. Excluding these acquired loans from the calculation, the ALLL to total gross loans was 1.59% and 1.79% as of December 31, 2016 and 2015, respectively and general reserves associated with non-impaired loans to total non-impaired loans was 1.55% and 1.79%, respectively. The loan portfolio acquired in the mergers was booked at fair value with no associated allocation in the ALLL. The size of the fair value discount remains adequate for all non-impaired acquired loans; therefore, there is no associated allocation in the ALLL.
The Company's loan portfolio balances in 2016 increased through organic growth and the acquisition of SVB. Management believes that the change in the allowance for credit losses to total loans ratios is directionally consistent with the composition of loans and the level of nonperforming and classified loans, partially offset by the general economic conditions

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experienced in the central California communities serviced by the Company and recent improvements in real estate collateral values.

The determination of the general reserve for loans that are not impaired is based on estimates made by management, including but not limited to, consideration of historical losses (or peer data) by portfolio segment over the most recent 20 quarters, and qualitative factors. Assumptions regarding the collateral value of various under-performing loans may affect the level and allocation of the allowance for credit losses in future periods. The allowance may also be affected by trends in the amount of charge offs experienced or expected trends within different loan portfolios. However, the total reserve rates on non-impaired loans include qualitative factors which are systematically derived and consistently applied to reflect conservatively estimated losses from loss contingencies at the date of the financial statements. Based on the above considerations and given recent changes in historical charge-off rates included in the ALLL modeling and the changes in other factors, management determined that the ALLL was appropriate as of December 31, 2016.

Non-performing loans totaled $2,180,000 as of December 31, 2016, and $2,413,000 as of December 31, 2015. The allowance for credit losses as a percentage of nonperforming loans was 427.80% and 398.26% as of December 31, 2016 and December 31, 2015, respectively. In addition, management believes that the likelihood of recoveries on previously charged-off loans continues to improve based on the collection efforts of management combined with improvements in the value of real estate which serves as the primary source of collateral for loans. Management believes the allowance at December 31, 2016 is adequate based upon its ongoing analysis of the loan portfolio, historical loss trends and other factors. However, no assurance can be given that the Company may not sustain charge-offs which are in excess of the allowance in any given period.

Goodwill and Intangible Assets

Business combinations involving the Bank’s acquisition of the equity interests or net assets of another enterprise give rise to goodwill. Total goodwill at December 31, 2016 was $40,231,000 consisting of $10,314,000, $6,340,000, $14,643,000 and $8,934,000 representing the excess of the cost of Sierra Vista Bank, Visalia Community Bank, Service 1st Bancorp and Bank of Madera County, respectively, over the net amounts assigned to assets acquired and liabilities assumed in the transactions accounted for under the purchase method of accounting. The value of goodwill is ultimately derived from the Bank’s ability to generate net earnings after the acquisitions and is not deductible for tax purposes. A significant decline in net earnings could be indicative of a decline in the fair value of goodwill and result in impairment. For that reason, goodwill is assessed at least annually for impairment.

The Company has selected September 30 as the date to perform the annual impairment test. Management assessed qualitative factors including performance trends and noted no factors indicating goodwill impairment.

Goodwill is also tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of the Company below its carrying amount. No such events or circumstances arose during the fourth quarter of 2016; therefore, goodwill was not required to be retested.

The intangible assets at December 31, 2016 represent the estimated fair value of the core deposit relationships acquired in the 2016 acquisition of Sierra Vista Bank of $508,000 and the 2013 acquisition of Visalia Community Bank of $1,365,000. Core deposit intangibles are being amortized using the straight-line method over an estimated life of ten years from the date of acquisition. The carrying value of intangible assets at December 31, 2016 was $1,383,000, net of $490,000 in accumulated amortization expense. The carrying value at December 31, 2015 was $1,024,000, net of $1,741,000 in accumulated amortization expense. Management evaluates the remaining useful lives quarterly to determine whether events or circumstances warrant a revision to the remaining periods of amortization. Based on the evaluation, no changes to the remaining useful lives was required. Management performed an annual impairment test on core deposit intangibles as of September 30, 2016 and determined no impairment was necessary. In addition, management determined that no events had occurred between the annual evaluation date and December 31, 2016 which would necessitate further analysis. Amortization expense recognized was $149,000 for 2016, $320,000 for 2015 and $337,000 for 2014.

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The following table summarizes the Company's estimated core deposit intangible amortization expense for each of the next five years (in thousands):

Years Ending December 31,	Estimated Core Deposit Intangible Amortization
2017	$ 188
2018	188
2019	188
2020	188
2021	188
Thereafter	443
Total	$ 1,383

Deposits and Borrowings

The Bank's deposits are insured by the Federal Deposit Insurance Corporation (FDIC) up to applicable legal limits. All of a depositor's accounts at an insured depository institution, including all non-interest bearing transactions accounts, will be insured by the FDIC up to the standard maximum deposit insurance amount of $250,000 for each deposit insurance ownership category.

Total deposits increased $139,712,000 or 12.52% to $1,255,979,000 as of December 31, 2016, compared to $1,116,267,000 as of December 31, 2015. Interest-bearing deposits increased $72,670,000 or 10.57% to $760,164,000 as of December 31, 2016, compared to $687,494,000 as of December 31, 2015. Non-interest bearing deposits increased $67,042,000 or 15.64% to $495,815,000 as of December 31, 2016, compared to $428,773,000 as of December 31, 2015. In conjunction with the acquisition of Sierra Vista Bank the Company acquired total interest bearing deposits of $82,197,000, consisting of $10,292,000, $24,704,000, $41,887,000 and $5,314,000 in NOW, MMA, Time and Savings deposits, respectively, and $56,039,000 in non-interest bearing deposits. Average non-interest bearing deposits to average total deposits was 36.46% for the year ended December 31, 2016 compared to 36.40% for the same period in 2015. Our total market share of deposits in Fresno, Madera, San Joaquin, and Tulare counties was 3.76% in 2016 compared to 3.77% in 2015 based on FDIC deposit market share information published as of June 2016.

The composition of the deposits and average interest rates paid at December 31, 2016 and December 31, 2015 is summarized in the table below.

(Dollars in thousands)	December 31, 2016	% of Total Deposits		Effective Rate		December 31, 2015	% of Total Deposits		Effective Rate	
NOW accounts	$ 247,623	19.7	%	0.12	%	$ 227,167	20.4	%	0.10	%
MMA accounts	250,749	19.9	%	0.05	%	239,241	21.4	%	0.06	%
Time deposits	156,694	12.5	%	0.38	%	139,703	12.5	%	0.37	%
Savings deposits	105,098	8.4	%	0.03	%	81,383	7.3	%	0.04	%
Total interest-bearing	760,164	60.5	%	0.13	%	687,494	61.6	%	0.14	%
Non-interest bearing	495,815	39.5	%			428,773	38.4	%		
Total deposits	$ 1,255,979	100.0	%			$ 1,116,267	100.0	%		

We have no known foreign deposits. The following table sets forth the average amount of and the average rate paid on certain deposit categories which were in excess of 10% of average total deposits for the years ended December 31, 2016, 2015, and 2014.

	2016		2015		2014	
(Dollars in thousands)	Balance	Rate	Balance	Rate	Balance	Rate
NOW accounts	$246,770	0.12%	$222,839	0.10%	$197,630	0.11%

Money market accounts	$249,620	0.05%	$227,743	0.06%	$229,769	0.08%
Time certificates of deposit	$139,656	0.38%	$149,383	0.37%	$162,218	0.40%
Non-interest bearing demand	$417,151	—	$387,931	—	$348,822	—
Total deposits	$1,144,231	0.09%	$1,065,798	0.09%	$1,006,560	0.11%

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The following table sets forth the maturity of time certificates of deposit and other time deposits of $100,000 or more at December 31, 2016.

(In thousands)	
Three months or less	$34,009
Over 3 through 6 months	20,108
Over 6 through 12 months	41,186
Over 12 months	14,893
	$110,196

There were no short-term or long-term FHLB borrowings as of December 31, 2016 or December 31, 2015. We maintain a line of credit with the FHLB collateralized by government securities and loans. Refer to Liquidity section below for further discussion of FHLB advances. The Bank had unsecured lines of credit with its correspondent banks which, in the aggregate, amounted to $40,000,000 at December 31, 2016 and 2015, at interest rates which vary with market conditions. As of December 31, 2016, the Company had $400,000 in Federal funds purchased. The Company had no overnight borrowings outstanding under these credit facilities at December 31, 2015.

Capital Resources

Capital serves as a source of funds and helps protect depositors and shareholders against potential losses. Historically, the primary sources of capital for the Company have been internally generated capital through retained earnings and the issuance of common and preferred stock.

The Company has historically maintained substantial levels of capital. The assessment of capital adequacy is dependent on several factors including asset quality, earnings trends, liquidity and economic conditions. Maintenance of adequate capital levels is integral to providing stability to the Company. The Company needs to maintain substantial levels of regulatory capital to give it maximum flexibility in the changing regulatory environment and to respond to changes in the market and economic conditions.

Our shareholders' equity was $164,033,000 as of December 31, 2016, compared to $139,323,000 as of December 31, 2015. The increase in shareholders' equity is the result of an increase in retained earnings from our net income of $15,182,000, the issuance of stock in connection with the Sierra Vista Bank acquisition in the amount of $16,678,000, the exercise of stock options, including the related tax benefit of $261,000, and the effect of share-based compensation expense of $284,000, partially offset by common stock cash dividends of $2,715,000 and a decrease in accumulated other comprehensive income (AOCI) of $4,978,000.

During 2016, the Bank declared and paid cash dividends to the Company in the amount of $13,010,000 in connection with the cash dividends to the Company's shareholders approved by the Company's Board of Directors and the cash portion of the SVB transaction. The Bank may not pay any dividend that would cause it to be deemed not "well capitalized" under applicable banking laws and regulations. The Company declared and paid a total of $2,715,000 or $0.24 per common share cash dividend to shareholders of record during the year ended December 31, 2016.

During 2015, the Bank declared and paid cash dividends to the Company in the amount of $2,260,000 in connection with the cash dividends to the Company's shareholders approved by the Company's Board of Directors. The Company declared and paid a total of $1,979,000 or $0.18 per common share cash dividend to shareholders of record during the year ended December 31, 2015.

During 2014, the Bank declared and paid cash dividends to the Company in the amount of $2,350,000 in connection with the cash dividends to the Company's shareholders approved by the Company's Board of Directors. The Company declared and paid a total of $2,190,000 or $0.20 per common share cash dividend to shareholders of record during the year ended December 31, 2014.

The following table sets forth certain financial ratios for the years ended December 31, 2016, 2015, and 2014.

	2016	2015	2014
Net income:			

To average assets	1.15 %	0.90 %	0.46 %
To average shareholders’ equity	9.84 %	8.12 %	4.06 %
Dividends declared per share to net income per share	19.20%	18.00%	41.67%
Average shareholders’ equity to average assets	11.68%	11.05%	11.27%

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Management considers capital requirements as part of its strategic planning process. The strategic plan calls for continuing increases in assets and liabilities, and the capital required may therefore be in excess of retained earnings. The ability to obtain capital is dependent upon the capital markets as well as our performance. Management regularly evaluates sources of capital and the timing required to meet its strategic objectives. The assessment of capital adequacy is dependent on several factors including asset quality, earnings trends, liquidity and economic conditions. Maintenance of adequate capital levels is integral to providing stability to the Company. The Company needs to maintain substantial levels of regulatory capital to give it maximum flexibility in the changing regulatory environment and to respond to changes in the market and economic conditions including acquisition opportunities.

The Board of Governors, the FDIC and other federal banking agencies have issued risk-based capital adequacy guidelines intended to provide a measure of capital adequacy that reflects the degree of risk associated with a banking organization's operations for both transactions reported on the balance sheet as assets, and transactions, such as letters of credit and recourse arrangements, which are reported as off-balance-sheet items. Under these guidelines, nominal dollar amounts of assets and credit equivalent amounts of off-balance-sheet items are multiplied by one of several risk adjustment percentages, which range from 0% for assets with low credit risk, such as certain U.S. government securities, to 100% for assets with relatively higher credit risk, such as business loans.

A banking organization's risk-based capital ratios are obtained by dividing its qualifying capital by its total risk-adjusted assets and off-balance-sheet items. The regulators measure risk-adjusted assets and off-balance-sheet items against both total qualifying capital (the sum of Tier 1 capital and limited amounts of Tier 2 capital) and Tier 1 capital. Tier 1 capital consists of common stock, retained earnings, noncumulative perpetual preferred stock and minority interests in certain subsidiaries, less most other intangible assets. Tier 2 capital may consist of a limited amount of the allowance for possible loan and lease losses and certain other instruments with some characteristics of equity. The inclusion of elements of Tier 2 capital is subject to certain other requirements and limitations of the federal banking agencies.

In December 2010, the Internal Basel Committee on Bank Supervision ("Basel Committee") released its final framework for strengthening international capital and liquidity regulation, now officially identified as "Basel III," which, when fully phased-in, requires bank holding companies and their bank subsidiaries to maintain substantially more capital than currently required, with a greater emphasis on common equity.

In July 2013, the U.S. banking agencies approved the U.S. version of Basel III. The federal bank regulatory agencies adopted version of Basel III revises the risk-based and leverage capital requirements and the method for calculating risk-weighted assets to make them consistent with Basel III and to meet the requirements of the Dodd-Frank Act. Although many of the rules contained in these final regulations are applicable only to large, internationally active banks, some of them apply on a phased in basis to all banking organizations, including the Company and the Bank. Among other things, the rules establish a new minimum common equity Tier 1 ratio (4.5% of risk-weighted assets), a higher minimum Tier 1 risk-based capital requirement (6.0% of risk-weighted assets) and a minimum non-risk-based leverage ratio (4.00% eliminating a 3.00% exception for higher rated banks). The new additional capital conservation buffer of 2.5% of risk weighted assets over each of the required capital ratios will be phased in from 2016 to 2019 and must be met to avoid limitations on the ability of the Company and the Bank to pay dividends, repurchase shares or pay discretionary bonuses. The additional "countercyclical capital buffer" is also required for larger and more complex institutions. The new rules assign higher risk weighting to exposures that are more than 90 days past due or are on nonaccrual status and certain commercial real estate facilities that finance the acquisition, development or construction of real property. The rules also change the permitted composition of Tier 1 capital to exclude trust preferred securities, mortgage servicing rights and certain deferred tax assets and include unrealized gains and losses on available for sale debt and equity securities (through a one-time opt out option for Standardized Banks (banks with less than $250 billion of total consolidated assets and less than $10 billion of foreign exposures) which the Company and the Bank elected at March 31, 2015. The rules, including alternative requirements for smaller community financial institutions like the Company and the Bank, will be phased in through 2019. The implementation of the Basel III framework commenced on January 1, 2015. As of December 31, 2016 and 2015, the Company and the Bank met or exceeded all of their capital requirements inclusive of the capital buffer.

A bank that does not achieve and maintain the required capital levels may be issued a capital directive by the FDIC to ensure the maintenance of required capital levels. As discussed above, the Company and the Bank are required to maintain certain levels of capital.

The following table presents the Company's and the Bank's Regulatory capital ratios (excluding capital conservation buffer) as of December 31, 2016 and 2015.

	December 31, 2016		December 31, 2015	
(Dollars in thousands)	Amount	Ratio	Amount	Ratio
Tier 1 Leverage Ratio				
Central Valley Community Bancorp and Subsidiary	$122,601	8.75 %	$105,825	8.65 %
Minimum regulatory requirement	$56,057	4.00 %	$48,950	4.00 %
Central Valley Community Bank	$121,079	8.64 %	$104,878	8.58 %
Minimum requirement for "Well-Capitalized" institution	$70,080	5.00 %	$61,148	5.00 %
Minimum regulatory requirement	$56,064	4.00 %	$48,918	4.00 %
Common Equity Tier 1 Ratio				
Central Valley Community Bancorp and Subsidiary	$120,080	12.48 %	$103,152	13.44 %
Minimum regulatory requirement	$43,426	4.50 %	$34,650	4.50 %
Central Valley Community Bank	$121,079	12.59 %	$104,878	13.67 %
Minimum requirement for "Well-Capitalized" institution	$62,665	6.50 %	$50,017	6.50 %
Minimum regulatory requirement	$43,383	4.50 %	$34,627	4.50 %
Tier 1 Risk-Based Capital Ratio				
Central Valley Community Bancorp and Subsidiary	$122,601	12.74 %	$105,825	13.79 %
Minimum regulatory requirement	$57,901	6.00 %	$46,200	6.00 %
Central Valley Community Bank	$121,079	12.59 %	$104,878	13.67 %
Minimum requirement for "Well-Capitalized" institution	$77,126	8.00 %	$61,560	8.00 %
Minimum regulatory requirement	$57,845	6.00 %	$46,170	6.00 %
Total Risk-Based Capital Ratio				
Central Valley Community Bancorp and Subsidiary	$132,052	13.72 %	$115,466	15.04 %
Minimum regulatory requirement	$77,202	8.00 %	$61,601	8.00 %
Central Valley Community Bank	$130,530	13.57 %	$114,513	14.93 %
Minimum requirement for "Well-Capitalized" institution	$96,408	10.00 %	$76,949	10.00 %
Minimum regulatory requirement	$77,126	8.00 %	$61,560	8.00 %

The Company succeeded to all of the rights and obligations of the Service 1st Capital Trust I, a Delaware business trust, in connection with the acquisition of Service 1st as of November 12, 2008. The Trust was formed on August 17, 2006 for the sole purpose of issuing trust preferred securities fully and unconditionally guaranteed by Service 1st. Under applicable regulatory guidance, the amount of trust preferred securities that is eligible as Tier 1 capital is limited to 25% of the Company's Tier 1 capital on a pro forma basis. At December 31, 2016, all of the trust preferred securities that have been issued qualify as Tier 1 capital. The trust preferred securities mature on October 7, 2036, are redeemable at the Company's option beginning five years after issuance, and require quarterly distributions by the Trust to the holder of the trust preferred securities at a variable interest rate which will adjust quarterly to equal the three month LIBOR plus 1.60%.

The Trust used the proceeds from the sale of the trust preferred securities to purchase approximately $5,155,000 in aggregate principal amount of Service 1st's junior subordinated notes (the Notes). The Notes bear interest at the same variable interest rate during the same quarterly periods as the trust preferred securities. The Notes are redeemable by the Company on any January 7, April 7, July 7, or October 7 on or after October 7, 2012 or at any time within 90 days following the occurrence of certain events, such as: (i) a change in the regulatory capital treatment of the Notes (ii) in the event the Trust is deemed an investment company or (iii) upon the occurrence of certain adverse tax events. In each such case, the Company may redeem the Notes for their aggregate principal amount, plus any accrued but unpaid interest.

The Notes may be declared immediately due and payable at the election of the trustee or holders of 25% of the aggregate principal amount of outstanding Notes in the event that the Company defaults in the payment of any interest following the nonpayment of any such interest for 20 or more consecutive quarterly periods. Holders of the trust preferred securities are entitled to a cumulative cash distribution on the liquidation amount of $1,000 per security. For each January 7, April 7, July 7 or October 7 of each year, the rate will be adjusted to equal the three month LIBOR plus 1.60%. As of December 31, 2016, the rate was 2.48%. Interest expense recognized by the Company for the years ended December 31, 2016, 2015, and 2014 was $121,000, $99,000 and $96,000, respectively.

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LIQUIDITY

Liquidity management involves our ability to meet cash flow requirements arising from fluctuations in deposit levels and demands of daily operations, which include funding of securities purchases, providing for customers' credit needs and ongoing repayment of borrowings. Our liquidity is actively managed on a daily basis and reviewed periodically by our management and Director's Asset/Liability Committees. This process is intended to ensure the maintenance of sufficient funds to meet our needs, including adequate cash flows for off-balance sheet commitments.

Our primary sources of liquidity are derived from financing activities which include the acceptance of customer and, to a lesser extent, broker deposits, Federal funds facilities and advances from the Federal Home Loan Bank of San Francisco (FHLB). These funding sources are augmented by payments of principal and interest on loans, the routine maturities and pay downs of securities from the securities portfolio, the stability of our core deposits and the ability to sell investment securities. As of December 31, 2016, the Company had unpledged securities totaling $458,846,000 available as a secondary source of liquidity and total cash and cash equivalents of $38,568,000. Cash and cash equivalents at December 31, 2016 decreased 59.24% compared to December 31, 2015. Primary uses of funds include withdrawal of and interest payments on deposits, origination and purchases of loans, purchases of investment securities, and payment of operating expenses. Due to the negative impact of the slow economic recovery, we have been cautiously managing our asset quality. Consequently, expanding our loan portfolio or finding adequate investments to utilize some of our excess liquidity has been difficult in the current economic environment.

As a means of augmenting our liquidity, we have established Federal funds lines with various correspondent banks. At December 31, 2016, our available borrowing capacity includes approximately $40,000,000 in Federal funds lines with our correspondent banks and $351,713,000 in unused FHLB advances. At December 31, 2016, we were not aware of any information that was reasonably likely to have a material effect on our liquidity position.

The following table reflects the Company's credit lines, balances outstanding, and pledged collateral at December 31, 2016 and 2015:

Credit Lines (In thousands)	December 31, 2016	December 31, 2015
Unsecured Credit Lines (interest rate varies with market):		
Credit limit	$ 40,000	$ 40,000
Balance outstanding	$ 400	$ —
Federal Home Loan Bank (interest rate at prevailing interest rate):		
Credit limit	351,713	308,356
Balance outstanding	$ —	$ —
Collateral pledged	$ 175,160	$ 215,223
Fair value of collateral	$ 175,218	$ 215,307
Federal Reserve Bank (interest rate at prevailing discount interest rate):		
Credit limit	$ 9,102	$ 2,328
Balance outstanding	$ —	$ —
Collateral pledged	$ 2,407	$ 2,578
Fair value of collateral	$ 2,436	$ 2,598

The liquidity of our parent company, Central Valley Community Bancorp, is primarily dependent on the payment of cash dividends by its subsidiary, Central Valley Community Bank, subject to limitations imposed by regulations.

OFF-BALANCE SHEET ITEMS

In the normal course of business, the Company is a party to financial instruments with off-balance sheet risk. These financial instruments include commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received. The balance of commitments to extend credit on undisbursed construction and other loans and letters of credit was $259,415,000 as of December 31, 2016 compared to $217,166,000 as of December 31, 2015. For a more detailed discussion of these financial instruments, see Note 13 to the audited Consolidated Financial Statements in this Annual Report.

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Contractual Obligations

The contractual obligations of the Company, summarized by type of obligation and contractual maturity, at December 31, 2016, are as follows:

(In thousands)	Less Than One Year	One to Three Years	Three to Five Years	After Five Years	Total
Deposits	$1,232,953	$19,089	$3,225	$712	$1,255,979
Subordinated debentures	—	—	—	5,155	5,155
Operating leases	2,350	3,498	2,267	1,425	9,540
Total	$1,235,303	$22,587	$5,492	$7,292	$1,270,674

Deposits represent both non-interest bearing and interest bearing deposits. Interest bearing deposits include interest bearing transaction accounts, money market and savings deposits and certificates of deposit. Deposits with indeterminate maturities, such as demand, savings and money market accounts are reflected as obligations due in less than one year.
Subordinated debentures represent notes issued to a capital trust which was formed solely for the purpose of issuing trust preferred securities. These subordinated debentures were acquired as a part of the merger with Service 1st. The aggregate amount indicated above represents the full amount of the contractual obligation. All of these securities are variable rate instruments. The trust preferred securities mature on October 7, 2036, and are redeemable quarterly at the Company's option.
In the ordinary course of business, the Company is party to various operating leases. For operating leases, the dollar balances reflected in the table above are categorized by the due date of the lease payments. Operating leases represent the total minimum lease payments under non-cancelable operating leases.

CRITICAL ACCOUNTING POLICIES

The Securities and Exchange Commission (SEC) has issued disclosure guidance for "critical accounting policies." The SEC defines "critical accounting policies" as those that require application of management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in future periods.
Our accounting policies are integral to understanding the results reported. Our significant accounting policies are described in detail in Note 1 in the audited Consolidated Financial Statements. Not all of the significant accounting policies presented in Note 1 of the audited Consolidated Financial Statements in this Annual Report require management to make difficult, subjective or complex judgments or estimates.

Use of Estimates

The preparation of these financial statements requires management to make estimates and judgments that affect the reported amount of assets, liabilities, revenues and expenses. On an ongoing basis, management evaluates the estimates used. Estimates are based upon historical experience, current economic conditions and other factors that management considers reasonable under the circumstances.
These estimates result in judgments regarding the carrying values of assets and liabilities when these values are not readily available from other sources, as well as assessing and identifying the accounting treatments of contingencies and commitments. 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 may differ from these estimates under different assumptions.

Accounting Principles Generally Accepted in the United States of America

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP).

We follow accounting policies typical to the commercial banking industry and in compliance with various regulation and guidelines as established by the Public Company Accounting Oversight Board (PCAOB), Financial Accounting Standards Board (FASB), the American Institute of Certified Public Accountants (AICPA), and the Bank’s primary federal regulator, the FDIC. The following is a brief description of our current accounting policies involving significant management judgments.

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Allowance for Credit Losses

Our most significant management accounting estimate is the appropriate level for the allowance for credit losses. The allowance for credit losses is an estimate of probable incurred credit losses in the Company's loan portfolio. The adequacy of the allowance is monitored on an on-going basis and is based on our management's evaluation of numerous factors. These factors include the quality of the current loan portfolio, the trend in the loan portfolio's risk ratings, current economic conditions, loan concentrations, loan growth rates, past-due and nonperforming trends, evaluation of specific loss estimates for all significant problem loans, historical charge-off and recovery experience and other pertinent information. See Note 1 to the audited Consolidated Financial Statements in this Annual Report for more detail regarding our allowance for credit losses.

The calculation of the allowance for credit losses is by nature inexact, as the allowance represents our management's best estimate of the probable losses inherent in our credit portfolios at the reporting date. These credit losses will occur in the future, and as such cannot be determined with absolute certainty at the reporting date.

Impairment of Investment Securities

Investment securities are impaired when the amortized cost exceeds fair value. Investment securities are evaluated for impairment on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation to determine whether a decline in their value is other than temporary. Management utilizes criteria such as the magnitude and duration of the decline and the intent and ability of the Company 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 prospect 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 we do not intend to sell the security or it is more likely than not that we 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 we will be required to sell the security before recovering its forecasted cost, the entire impairment loss is recognized as a charge to earnings.

Goodwill

Business combinations involving the Company's acquisition of the equity interests or net assets of another enterprise or the assumption of net liabilities in an acquisition of branches constituting a business may give rise to goodwill. Goodwill represents the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed in transactions accounted for under the purchase method of accounting. The value of goodwill is ultimately derived from the Company's ability to generate net earnings after the acquisition. A decline in net earnings could be indicative of a decline in the fair value of goodwill and result in impairment. For that reason, goodwill is assessed for impairment at a reporting unit level at least annually or more often if an event occurs or circumstances change that would more likely than not reduce the fair value of the Company below its carrying amount. While the Company believes all assumptions utilized in its assessment of goodwill for impairment are reasonable and appropriate, changes could cause the Company to record impairment in the future.

Accounting for Income Taxes

The Company files its income taxes on a consolidated basis with its subsidiary. The allocation of income tax expense (benefit) represents each entity's proportionate share of the consolidated provision for income taxes.

Deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. On the balance sheet, net deferred tax assets are included in accrued interest receivable and other 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 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.

Only tax positions that meet the more-likely-than-not recognition threshold are recognized. The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more likely than not that the position will be sustained upon examination, including the resolution of appeals or

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litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination. Interest expense and penalties associated with unrecognized tax benefits are classified as income tax expense in the consolidated statement of income.

INFLATION

The impact of inflation on a financial institution differs significantly from that exerted on other industries primarily because the assets and liabilities of financial institutions consist largely of monetary items. However, financial institutions are affected by inflation in part through non-interest expenses, such as salaries and occupancy expenses, and to some extent by changes in interest rates.

At December 31, 2016, we do not believe that inflation will have a material impact on our consolidated financial position or results of operations. However, if inflation concerns cause short term rates to rise in the near future, we may benefit by immediate repricing of a portion of our loan portfolio. Refer to Quantitative and Qualitative Disclosures About Market Risk for further discussion.

ITEM 7A - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest rate risk (IRR) and credit risk constitute the two greatest sources of financial exposure for insured financial institutions that operate like we do. IRR represents the impact that changes in absolute and relative levels of market interest rates may have upon our net interest income (NII). Changes in the NII are the result of changes in the net interest spread between interest-earning assets and interest-bearing liabilities (timing risk), the relationship between various rates (basis risk), and changes in the shape of the yield curve.

We realize income principally from the differential or spread between the interest earned on loans, investments, other interest-earning assets and the interest incurred on deposits and borrowings. The volumes and yields on loans, deposits and borrowings are affected by market interest rates. As of December 31, 2016, 75.64% of our loan portfolio was tied to adjustable-rate indices. The majority of our adjustable rate loans are tied to prime and reprice within 90 days. However, in the current low rate environment, several of our loans, tied to prime, are at their floors and will not reprice until prime plus the factor is greater than the floor. The majority of our time deposits have a fixed rate of interest. As of December 31, 2016, 85.39% of our time deposits matures within one year or less.

Changes in the market level of interest rates directly and immediately affect our interest spread, and therefore profitability. Sharp and significant changes to market rates can cause the interest spread to shrink or expand significantly in the near term, principally because of the timing differences between the adjustable rate loans and the maturities (and therefore repricing) of the deposits and borrowings.

Our management and Board of Directors' Asset/Liability Committees (ALCO) are responsible for managing our assets and liabilities in a manner that balances profitability, IRR and various other risks including liquidity. The ALCO operates under policies and within risk limits prescribed, reviewed, and approved by the Board of Directors.

The ALCO seeks to stabilize our NII by matching rate-sensitive assets and liabilities through maintaining the maturity and repricing of these assets and liabilities at appropriate levels given the interest rate environment. When the amount of rate-sensitive liabilities exceeds rate-sensitive assets within specified time periods, NII generally will be negatively impacted by an increasing interest rate environment and positively impacted by a decreasing interest rate environment. Conversely, when the amount of rate-sensitive assets exceeds the amount of rate-sensitive liabilities within specified time periods, net interest income will generally be positively impacted by an increasing interest rate environment and negatively impacted by a decreasing interest rate environment. In recent years, we have shifted our mix of assets from consisting primarily of loans to a current mix that is approximately half loans and half securities, none of which are held for trading purposes. The value of these securities is subject to interest rate risk, which we must monitor and manage successfully in order to prevent declines in value of these assets if interest rates rise in the future. The speed and velocity of the repricing of assets and liabilities will also contribute to the effects on our NII, as will the presence or absence of periodic and lifetime interest rate caps and floors.

Simulation of earnings is the primary tool used to measure the sensitivity of earnings to interest rate changes. Earnings simulations are produced using a software model that is based on actual cash flows and repricing characteristics for all of our financial instruments and incorporates market-based assumptions regarding the impact of changing interest rates on current volumes of applicable financial instruments.

Interest rate simulations provide us with an estimate of both the dollar amount and percentage change in NII under various rate scenarios. All assets and liabilities are normally subjected to up to 400 basis point increases and decreases in interest rates in 100 basis point increments. Under each interest rate scenario, we project our net interest income. From these results, we can then develop alternatives in dealing with the tolerance thresholds.

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The assets and liabilities of a financial institution are primarily monetary in nature. As such they represent obligations to pay or receive fixed and determinable amounts of money that are not affected by future changes in prices. Generally, the impact of inflation on a financial institution is reflected by fluctuations in interest rates, the ability of customers to repay their obligations and upward pressure on operating expenses. Although inflationary pressures are not considered to be of any particular hindrance in the current economic environment, they may have an impact on the company's future earnings in the event those pressures become more prevalent.

As a financial institution, the Company's primary component of market risk is interest rate volatility. Fluctuations in interest rates will ultimately impact both the level of interest income and interest expense recorded on a large portion of the Company's assets and liabilities, and the market value of all interest earning assets and interest bearing liabilities, other than those which possess a short term to maturity. Virtually all of the Company's interest earning assets and interest bearing liabilities are located at the Bank level. Thus, virtually all of the Company's interest rate risk exposure lies at the Bank level other than $5.2 million in subordinated debentures issued by the Company's subsidiary Service 1st Capital Trust I. As a result, all significant interest rate risk procedures are performed at the Bank level.

The fundamental objective of the Company's management of its assets and liabilities is to maximize the Company's economic value while maintaining adequate liquidity and an exposure to interest rate risk deemed by management to be acceptable. Management believes an acceptable degree of exposure to interest rate risk results from the management of assets and liabilities through maturities, pricing and mix to attempt to neutralize the potential impact of changes in market interest rates. The Company's profitability is dependent to a large extent upon its net interest income, which is the difference between its interest income on interest earning assets, such as loans and investments, and its interest expense on interest bearing liabilities, such as deposits and borrowings. The Company is subject to interest rate risk to the degree that its interest earning assets re-price differently than its interest bearing liabilities. The Company manages its mix of assets and liabilities with the goals of limiting its exposure to interest rate risk, ensuring adequate liquidity, and coordinating its sources and uses of funds.

The Company seeks to control interest rate risk exposure in a manner that will allow for adequate levels of earnings and capital over a range of possible interest rate environments. The Company has adopted formal policies and practices to monitor and manage interest rate risk exposure. Management believes historically it has effectively managed the effect of changes in interest rates on its operating results and believes that it can continue to manage the short-term effects of interest rate changes under various interest rate scenarios.

Management employs asset and liability management software and engages consultants to measure the Company's exposure to future changes in interest rates. The software measures the expected cash flows and re-pricing of each financial asset/liability separately in measuring the Company's interest rate sensitivity. Based on the results of the software's output, management believes the Company's balance sheet is evenly matched over the short term and slightly asset sensitive over the longer term as of December 31, 2016. This means that the Company would expect (all other things being equal) to experience a limited change in its net interest income if rates rise or fall. The level of potential or expected change indicated by the tables below is considered acceptable by management and is compliant with the Company's ALCO policies. Management will continue to perform this analysis each quarter.

The hypothetical impacts of sudden interest rate movements applied to the Company's asset and liability balances are modeled quarterly. The results of these models indicate how much of the Company's net interest income is "at risk" from various rate changes over a one year horizon. This exercise is valuable in identifying risk exposures. Management believes the results for the Company's December 31, 2016 balances indicate that the net interest income at risk over a one year time horizon for a 100 basis points ("bps"), 200 bps, 300 bps, and 400 bps rate increase and a 100 bps decrease is acceptable to management and within policy guidelines at this time. Given the low interest rate environment, 200 bps, 300 bps, and 400 bps decreases are not considered a realistic possibility and are therefore not modeled.

The results in the table below indicate the change in net interest income the Company would expect to see as of December 31, 2016, if interest rates were to change in the amounts set forth:

Sensitivity Analysis of Impact of Rate Changes on Interest Income

Hypothetical Change in Rates (Dollars in thousands)	Projected Net	$ Change from Rates at	% Change from Rates at

	Interest Income	December 31, 2016	December 31, 2016
Up 400 bps	$ 64,907	$ 10,788	19.93 %
Up 300 bps	62,135	8,016	14.81 %
Up 200 bps	59,381	5,262	9.72 %
Up 100 bps	56,651	2,532	4.68 %
Unchanged	54,119	—	—
Down 100 bps	51,686	(2,433)	(4.50)%

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It is important to note that the above table is a summary of several forecasts and actual results may vary from any of the forecasted amounts and such difference may be material and adverse. The forecasts are based on estimates and assumptions made by management, and that may turn out to be different, and may change over time. Factors affecting these estimates and assumptions include, but are not limited to: 1) competitor behavior, 2) economic conditions both locally and nationally, 3) actions taken by the Federal Reserve Board, 4) customer behavior and 5) management's responses to each of the foregoing. Factors that vary significantly from the assumptions and estimates may have material and adverse effects on the Company's net interest income; therefore, the results of this analysis should not be relied upon as indicative of actual future results.

The following table shows management's estimates of how the loan portfolio is segregated between variable-daily, variable other than daily and fixed rate loans, and estimates of re-pricing opportunities for the entire loan portfolio at December 31, 2016 and 2015:

	December 31, 2016		December 31, 2015	
Rate Type (Dollars in thousands)	Balance	Percent of Total	Balance	Percent of Total
Variable rate	$571,325	75.64 %	$471,757	78.87 %
Fixed rate	184,036	24.36 %	126,354	21.13 %
Total gross loans	$755,361	100.00%	$598,111	100.00%

Approximately 75.64% of our loan portfolio is tied to adjustable rate indices and 34.09% of our loan portfolio reprices within 90 days. As of December 31, 2016, we had 2,511 commercial and real estate loans totaling $444,796,000 with floors ranging from 3.25% to 7.50% and ceilings ranging from 7.00% to 30.00%.

The following table shows the repricing categories of the Company's loan portfolio at December 31, 2016 and 2015:

	December 31, 2016		December 31, 2015	
Repricing (Dollars in thousands)	Balance	Percent of Total	Balance	Percent of Total
< 1 Year	$309,397	40.95 %	$250,705	41.91 %
1-3 Years	153,680	20.35 %	124,385	20.80 %
3-5 Years	183,834	24.34 %	139,417	23.31 %
> 5 Years	108,450	14.36 %	83,604	13.98 %
Total gross loans	$755,361	100.00%	$598,111	100.00%

Assumptions are inherently uncertain, and, consequently, the model cannot precisely measure net interest income or precisely predict the impact of changes in interest rates on net interest income. Actual results will differ from simulated results due to timing, magnitude and frequency of interest rate changes, as well as changes in market conditions and management strategies which might moderate the negative consequences of interest rate deviations.

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ITEM 8 - FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

MANAGEMENT’S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The Shareholders and Board of Directors
Central Valley Community Bancorp and Subsidiary
Fresno, California

The management of Central Valley Community Bancorp is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) promulgated under the Securities Exchange Act of 1934 as a process designed by, or under the supervision of our Chief Executive Officer and Chief Financial Officer and effected by the board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with U.S. generally accepted accounting principles and includes those policies and procedures that:

* Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of our assets:

* Provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with U.S. generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and

* Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of our internal control over financial reporting as of December 31, 2016. In making this assessment, management used the criteria issued in the 2013 Internal Control-Integrated Framework (Framework) established and updated by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”). Based on that assessment, the Company’s management believes that, as of December 31, 2016, our internal control over financial reporting is effective based on those criteria.

Crowe Horwath LLP, the independent registered public accounting firm that audited the Company’s consolidated financial statements included in the Annual Report on Form 10-K for the year ended December 31, 2016, has issued an audit report on the effectiveness of the Company’s internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board that appears on the next page.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Shareholders and Board of Directors
Central Valley Community Bancorp and Subsidiary
Fresno, California

We have audited the accompanying consolidated balance sheets of Central Valley Community Bancorp and subsidiary (the "Company") as of December 31, 2016 and 2015, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2016. We also have audited the Company's internal control over financial reporting as of December 31, 2016, based on criteria established in the 2013 Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Central Valley Community Bancorp and subsidiary as of December 31, 2016 and 2015, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2016 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, Central Valley Community Bancorp and subsidiary maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in the 2013 Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

/s/ Crowe Horwath LLP

Sacramento, California
March 29, 2017

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CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
December 31, 2016 and 2015

(In thousands, except share amounts)	2016	2015
ASSETS		
Cash and due from banks	$28,185	$23,339
Interest-earning deposits in other banks	10,368	70,988
Federal funds sold	15	290
Total cash and cash equivalents	38,568	94,617
Available-for-sale investment securities (Amortized cost of $548,640 at December 31, 2016 and $470,080 at December 31, 2015)	547,749	477,554
Held-to-maturity investment securities (Fair value of $35,142 at December 31, 2015)	—	31,712
Loans, less allowance for credit losses of $9,326 at December 31, 2016 and $9,610 at December 31, 2015	747,302	588,501
Bank premises and equipment, net	9,407	9,292
Bank owned life insurance	23,189	20,702
Federal Home Loan Bank stock	5,594	4,823
Goodwill	40,231	29,917
Core deposit intangibles	1,383	1,024
Accrued interest receivable and other assets	29,900	18,594
Total assets	$1,443,323	$1,276,736
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits:		
Non-interest bearing	$495,815	$428,773
Interest bearing	760,164	687,494
Total deposits	1,255,979	1,116,267
Short-term borrowings	400	—
Junior subordinated deferrable interest debentures	5,155	5,155
Accrued interest payable and other liabilities	17,756	15,991
Total liabilities	1,279,290	1,137,413
Commitments and contingencies (Note 13)		
Shareholders' equity:		
Preferred stock, no par value, $1,000 per share liquidation preference; 10,000,000 shares authorized, none issued and outstanding	—	—
Common stock, no par value; 80,000,000 shares authorized; issued and outstanding: 12,143,815 at December 31, 2016 and 10,996,773 at December 31, 2015	71,645	54,424
Retained earnings	92,904	80,437
Accumulated other comprehensive (loss) income, net of tax	(516)	4,462
Total shareholders' equity	164,033	139,323
Total liabilities and shareholders' equity	$1,443,323	$1,276,736

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

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CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
For the Years Ended December 31, 2016, 2015, and 2014

(In thousands, except per share amounts)	2016	2015	2014
Interest income:			
Interest and fees on loans	$34,051	$30,504	$29,493
Interest on deposits in other banks	289	210	176
Interest and dividends on investment securities:			
Taxable	5,876	4,793	5,538
Exempt from Federal income taxes	6,460	6,315	5,832
Total interest income	46,676	41,822	41,039
Interest expense:			
Interest on deposits	975	948	1,060
Interest on junior subordinated deferrable interest debentures	121	99	96
Total interest expense	1,096	1,047	1,156
Net interest income before provision for credit losses	45,580	40,775	39,883
(Reversal of) Provision for credit losses	(5,850)	600	7,985
Net interest income after provision for credit losses	51,430	40,175	31,898
Non-interest income:			
Service charges	3,022	3,070	3,280
Appreciation in cash surrender value of bank owned life insurance	558	596	614
Interchange fees	1,228	1,197	1,205
Loan placement fees	1,083	1,042	544
Net realized gains on sales and calls of investment securities	1,920	1,495	904
Other-than-temporary impairment loss on investment securities	(136)	—	—
Federal Home Loan Bank dividends	630	580	327
Other income	1,286	1,407	1,290
Total non-interest income	9,591	9,387	8,164
Non-interest expenses:			
Salaries and employee benefits	21,881	20,836	19,721
Occupancy and equipment	4,754	4,669	4,835
Regulatory assessments	642	1,059	762
Data processing expense	1,707	1,139	1,820
Professional services	1,258	1,504	1,176
ATM/Debit card expenses	633	548	624
License & maintenance contracts	531	520	488
Directors' expenses	530	439	501
Advertising	576	608	589
Internet banking expenses	678	709	520
Acquisition and integration expenses	1,782	—	—
Amortization of core deposit intangibles	149	320	337
Other expense	3,801	3,665	3,965
Total non-interest expenses	38,922	36,016	35,338
Income before provision for income taxes	22,099	13,546	4,724
Provision (benefit) for income taxes	6,917	2,582	(570)
Net income available to common shareholders	$15,182	$10,964	$5,294
Basic earnings per common share	$1.34	$1.00	$0.48
Diluted earnings per common share	$1.33	$1.00	$0.48

Cash dividends per common share	$0.24	$0.18	$0.20

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

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CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

For the Years Ended December 31, 2016, 2015, and 2014

(In thousands)	2016	2015	2014
Net income	$15,182	$10,964	$5,294
Other Comprehensive Income (Loss):			
Unrealized gains (losses) on securities:			
Unrealized holdings (losses) gains arising during the period	(9,924)	59	13,847
Less: reclassification for net gains included in net income	1,224	1,481	904
Less: reclassification for other-than-temporary impairment loss included in net income	(136)	—	—
Transfer of investment securities from held-to-maturity to available-for-sale	2,647	—	—
Amortization of net unrealized gains transferred	(64)	(78)	(21)
Other comprehensive (loss) income, before tax	(8,429)	(1,500)	12,922
Tax benefit (expense) related to items of other comprehensive income	3,451	585	(5,259)
Total other comprehensive (loss) income	(4,978)	(915)	7,663
Comprehensive income	$10,204	$10,049	$12,957

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

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CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

For the Years Ended December 31, 2016, 2015, and 2014

(In thousands, except share amounts)	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss) (Net of Taxes)	Total Shareholders' Equity
Balance, January 1, 2014	10,914,680	$53,981	$68,348	$ (2,286)	$ 120,043
Net income	—	—	5,294	—	5,294
Other comprehensive income	—	—	—	7,663	7,663
Restricted stock granted, forfeited and related tax benefit	56,850	—	—	—	—
Cash dividend ($0.20 per common share)	—	—	(2,190)	—	(2,190)
Stock-based compensation expense	—	173	—	—	173
Stock options exercised and related tax benefit	8,910	62	—	—	62
Balance, December 31, 2014	10,980,440	54,216	71,452	5,377	131,045
Net income	—	—	10,964	—	10,964
Other comprehensive loss	—	—	—	(915)	(915)
Restricted stock granted, forfeited and related tax benefit	7,263	(96)	—	—	(96)
Stock-based compensation expense	—	238	—	—	238
Cash dividend ($0.18 per common share)	—	—	(1,979)	—	(1,979)
Stock options exercised and related tax benefit	9,070	66	—	—	66
Balance, December 31, 2015	10,996,773	54,424	80,437	4,462	139,323
Net income	—	—	15,182	—	15,182
Other comprehensive loss	—	—	—	(4,978)	(4,978)
Stock issued for acquisition	1,058,851	16,678			16,678
Restricted stock granted, forfeited and related tax benefit	52,911	(2)	—	—	(2)
Stock-based compensation expense	—	284	—	—	284
Cash dividend ($0.24 per common share)	—	—	(2,715)	—	(2,715)
Stock options exercised and related tax benefit	35,280	261	—	—	261
Balance, December 31, 2016	12,143,815	$71,645	$92,904	$ (516)	$ 164,033

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

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CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2016, 2015, and 2014

(In thousands)	2016	2015	2014
Cash flows from operating activities:			
Net income	$15,182	$10,964	$5,294
Adjustments to reconcile net income to net cash provided by operating activities:			
Net decrease in deferred loan costs	(851)	(270)	(305)
Depreciation	1,320	1,392	1,355
Accretion	(1,142)	(1,196)	(1,015)
Amortization	7,912	8,024	7,949
Stock-based compensation	284	238	173
Excess tax benefit from exercise of stock options	(30)	(6)	(7)
(Reversal of) provision for credit losses	(5,850)	600	7,985
Other than temporary impairment losses on investment securities	136	—	—
Net realized gains on sales and calls of available-for-sale investment securities	(1,224)	(1,481)	(904)
Net realized gains on sales or calls of held-to-maturity investment securities	(696)	(14)	—
Net loss on sale and disposal of equipment	4	6	201
Net gain on sale of other real estate owned	—	(11)	(63)
Increase in bank owned life insurance, net of expenses	(558)	(596)	(614)
Net gain on bank owned life insurance	(190)	(345)	—
Net (increase) decrease in accrued interest receivable and other assets	(4,711)	2,109	(3,021)
Net increase (decrease) in accrued interest payable and other liabilities	821	(963)	537
Benefit (provision) for deferred income taxes	2,592	(933)	(408)
Net cash provided by operating activities	12,999	17,518	17,157
Cash Flows From Investing Activities:			
Net cash and cash equivalents acquired in acquisition	13,241	—	—
Purchases of available-for-sale investment securities	(278,664)	(198,851)	(146,468)
Proceeds from sales or calls of available-for-sale investment securities	167,163	93,167	79,757
Proceeds from sales or calls of held-to-maturity investment securities	9,257	810	—
Proceeds from maturity and principal repayment of available-for-sale investment securities	50,531	53,593	52,665
Net increase in loans	(29,930)	(24,776)	(69,047)
Proceeds from sale of other real estate owned	—	359	488
Purchases of premises and equipment	(861)	(741)	(1,328)
Purchases of bank owned life insurance	—	(325)	(900)
FHLB stock purchased	—	(32)	(292)
Proceeds from bank owned life insurance	928	1,365	—
Proceeds from sale of premises and equipment	7	—	363
Net cash used in investing activities	(68,328)	(75,431)	(84,762)
Cash Flows From Financing Activities:			
Net increase in demand, interest-bearing and savings deposits	26,372	90,732	50,643
Net decrease in time deposits	(25,038)	(13,617)	(15,634)
Proceeds of borrowings from other financial institutions	400	—	—
Proceeds from exercise of stock options	231	60	55
Excess tax benefit from exercise of stock options	30	6	7
Cash dividend payments on common stock	(2,715)	(1,979)	(2,190)
Net cash (used in) provided by financing activities	(720)	75,202	32,881
(Decrease) increase in cash and cash equivalents	(56,049)	17,289	(34,724)

CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	94,617	77,328	112,052
CASH AND CASH EQUIVALENTS AT END OF YEAR	$38,568	$94,617	$77,328
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Cash paid during the year for:			
Interest	$1,053	$1,059	$1,171
Income taxes	$5,840	$1,865	$1,360

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CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(continued)
For the Years Ended December 31, 2016, 2015, and 2014

(In thousands)	2016	2015	2014
Non-cash investing and financing activities:			
Transfer of securities from held-to-maturity to available-for-sale	$23,131	$—	$—
Unrealized gain on transfer of securities from held-to-maturity to available-for-sale	$526	$—	$—
Transfer of securities from available-for-sale to held-to-maturity	$—	$—	$31,346
Unrealized gain on transfer of securities from available-for-sale to held-to-maturity	$—	$—	$163
Foreclosure of loan collateral and recognition of other real estate owned	$—	$227	$235
Transfer of loans to other assets	$363	$—	$—
Assumption of debt related to foreclosure of other real estate owned	$—	$121	$—
Common stock issued in Sierra Vista Bank acquisition	$16,678	$—	$—

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

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Central Valley Community Bancorp and Subsidiary
Notes to Consolidated Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General - Central Valley Community Bancorp (the “Company”) was incorporated on February 7, 2000 and subsequently obtained approval from the Board of Governors of the Federal Reserve System to be a bank holding company in connection with its acquisition of Central Valley Community Bank (the “Bank”). The Company became the sole shareholder of the Bank on November 15, 2000 in a statutory merger, pursuant to which each outstanding share of the Bank’s common stock was exchanged for one share of common stock of the Company.

Service 1st Capital Trust I (the Trust) is a business trust formed by Service 1st for the sole purpose of issuing trust preferred securities. The Company succeeded to all the rights and obligations of Service 1st in connection with the acquisition of Service 1st. The Trust is a wholly-owned subsidiary of the Company.

The Bank operates 22 full service offices throughout California’s San Joaquin Valley and Greater Sacramento Region. The Bank’s primary source of revenue is providing loans to customers who are predominately small and middle-market businesses and individuals.

The deposits of the Bank are insured by the Federal Deposit Insurance Corporation (FDIC) up to applicable legal limits. Depositors’ accounts at an insured depository institution, including all non-interest bearing transactions accounts, will be insured by the FDIC up to the standard maximum deposit insurance amount of $250,000 for each deposit insurance ownership category.

The accounting and reporting policies of Central Valley Community Bancorp and Subsidiary conform with accounting principles generally accepted in the United States of America and prevailing practices within the banking industry.

Management has determined that because all of the banking products and services offered by the Company are available in each branch of the Bank, all branches are located within the same economic environment and management does not allocate resources based on the performance of different lending or transaction activities, it is appropriate to aggregate the Bank branches and report them as a single operating segment. No customer accounts for more than 10 percent of revenues for the Company or the Bank.

Principles of Consolidation - The consolidated financial statements include the accounts of the Company and the consolidated accounts of its wholly-owned subsidiary, the Bank. Intercompany transactions and balances are eliminated in consolidation.

For financial reporting purposes, Service 1st Capital Trust I, is a wholly-owned subsidiary acquired in the merger of Service 1st Bancorp and formed for the exclusive purpose of issuing trust preferred securities. The Company is not considered the primary beneficiary of this trust (variable interest entity), therefore the trust is not consolidated in the Company’s financial statements, but rather the subordinated debentures are shown as a liability on the Company’s consolidated financial statements. The Company’s investment in the common stock of the Trust is included in accrued interest receivable and other assets on the consolidated balance sheet.

Use of Estimates - The preparation of these financial statements in accordance with U.S. Generally Accepted Accounting Principles requires management to make estimates and judgments that affect the reported amount of assets, liabilities, revenues and expenses. On an ongoing basis, management evaluates the estimates used. Estimates are based upon historical experience, current economic conditions and other factors that management considers reasonable under the circumstances.

These estimates result in judgments regarding the carrying values of assets and liabilities when these values are not readily available from other sources, as well as assessing and identifying the accounting treatments of contingencies and commitments. 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 may differ from these estimates under different assumptions.

Cash and Cash Equivalents - For the purpose of the statement of cash flows, cash, due from banks with maturities less than 90 days, interest-earning deposits in other banks, and Federal funds sold are considered to be cash equivalents. Generally, Federal funds are sold and purchased for one-day periods. Net cash flows are reported for customer loan and deposit transactions, interest-bearing deposits in other banks, and Federal funds purchased.

Investment Securities - Investments 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 to maturity, reported at amortized cost, adjusted for the accretion of discounts and amortization of premiums.

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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 in the period which the transfer occurs. For the year ended December 31, 2016 management transferred $23.1 million of securities from held-to-maturity to available-for-sale. During the year ended December 31, 2015, there were no transfers between categories. Due to the 2016 transfer, management is precluded from utilizing the held-to-maturity designation until the second quarter of 2018.

Gains or losses on the sale of investment securities are computed on 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. Premiums and discounts on securities are amortized or accreted on the level yield method without anticipating prepayments, except for mortgage backed securities where prepayments are anticipated.

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 Company 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 prospect 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 Company will not be required to sell the security before recovery, for debt securities, 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 Company will be required to sell the security before recovering its forecasted cost, the entire impairment loss is recognized as a charge to earnings.

Loans - All loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at principal balances outstanding net of deferred loan fees and costs, and the allowance for credit losses. Interest is accrued daily based upon outstanding loan principal balances. However, when a loan becomes impaired and the future collectability of interest and principal is in serious doubt, the loan is placed on nonaccrual status and the accrual of interest income is suspended. Any loan 90 days or more delinquent is automatically placed on nonaccrual status. Any interest accrued but unpaid is charged against income. Subsequent payments on these loans, or payments received on nonaccrual loans for which the ultimate collectability of principal is not in doubt, are applied first to principal until fully collected and then to interest.

Interest income on loans is discontinued at the time the loan is 90 days delinquent unless the loan is well-secured and in process of collection. Consumer and credit card loans are typically charged off no later than 90 days past due. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. A loan placed on non-accrual status may be restored to accrual status when principal and interest are no longer past due and unpaid, or the loan otherwise becomes both well secured and in the process of collection. When a loan is brought current, the Company must also have a reasonable assurance that the obligor has the ability to meet all contractual obligations in the future, that the loan will be repaid within a reasonable period of time, and that a minimum of six months of satisfactory repayment performance has occurred.

Substantially all loan origination fees, commitment fees, direct loan origination costs and purchase premiums and discounts on loans are deferred and recognized as an adjustment of yield, and 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.

Acquired loans and Leases - Loans and leases acquired through purchase or through a business combination are recorded at their fair value at the acquisition date. Credit discounts are included in the determination of fair value; therefore, an allowance for loan and lease losses is not recorded at the acquisition date. Should the Company’s allowance for credit losses methodology indicate that the credit discount associated with acquired, non-purchased credit impaired loans, is no longer sufficient to cover probable losses inherent in those loans, the Company will establish an allowance for those loans through a charge to provision for credit losses. At the time of an acquisition, we evaluate loans to determine if they are purchase credit impaired loans. Purchased credit impaired loans are those acquired loans with evidence of credit deterioration for which it was probable at acquisition that we would be unable to collect all contractual payments. We make this determination by considering past due and/or nonaccrual status, prior designation of a troubled debt restructuring, or other factors that may suggest we will not be able to collect all contractual payments. Purchased credit impaired loans are initially recorded at fair value with the difference between fair value and estimated future cash flows accreted over the expected cash flow period as income only to the extent we can reasonably estimate the timing and amount of future cash flows. In this case, these loans would be classified as accruing. In the event we are unable to reasonably estimate timing and amount of future cash flows, or if the loan is acquired primarily for the rewards of ownership of the underlying collateral, the loan is classified as non-accrual. An acquired loan previously

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classified by the seller as a troubled debt restructuring is no longer classified as such at the date of acquisition. Past due status is reported based on contractual payment status.

All loans not otherwise classified as purchase credit impaired are recorded at fair value with the discount to contractual value accreted over the life of the loan.

Allowance for Credit Losses - The allowance for credit losses (the "allowance") is a valuation allowance for probable incurred credit losses in the Company's loan portfolio. The allowance is established through a provision for credit losses which is charged to expense. Additions to the allowance are made 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 Company will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the original agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Loans determined to be impaired are individually evaluated for impairment. When a loan is impaired, the Company 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 come solely from the sale or operation of underlying collateral.

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the Company 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.

When determining the allowance for loan losses on acquired loans, we bifurcate the allowance between legacy loans and acquired loans. Loans remain designated as acquired until either (i) loan is renewed or (ii) loan is substantially modified whereby modification results in a new loan. When determining the allowance on acquired loans, the Company estimates probable incurred credit losses as compared to the Company's recorded investment, with the recorded investment being net of any unaccreted discounts from the acquisition.

The determination of the general reserve for loans that are not impaired is based on estimates made by management, including but not limited to, consideration of a simple average of historical losses by portfolio segment (and in certain cases peer loss data) over the most recent 20 quarters, and qualitative factors including economic trends in the Company's service areas, industry experience and trends, geographic concentrations, estimated collateral values, the Company's underwriting policies, the character of the loan portfolio, and probable losses inherent in the portfolio taken as a whole.

The Company segregates the allowance by portfolio segment. These portfolio segments include commercial, real estate, and consumer loans. The relative significance of risk considerations vary by portfolio segment. For commercial and real estate loans, the primary risk consideration is a borrower's ability to generate sufficient cash flows to repay their loan. Secondary considerations include the creditworthiness of guarantors and the valuation of collateral. In addition to the creditworthiness of a borrower, the type and location of real estate collateral is an important risk factor for real estate loans. The primary risk considerations for consumer loans are a borrower's personal cash flow and liquidity, as well as collateral value. The allowance for credit losses attributable to each portfolio segment, which includes both impaired loans and loans that are not impaired, is combined to determine the Company's overall allowance, which is included on the consolidated balance sheet.

Commercial:
Commercial and industrial - Commercial and industrial loans are generally underwritten to existing cash flows of operating businesses. Additionally, economic trends influenced by unemployment rates and other key economic indicators are closely correlated to the credit quality of these loans. Past due payments may indicate the borrower's capacity to repay their obligations may be deteriorating.
Agricultural land and production - Loans secured by crop production and livestock are especially vulnerable to two risk factors that are largely outside the control of Company and borrowers: commodity prices and weather conditions.

Real Estate:

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Owner-occupied commercial real estate - Real estate collateral secured by commercial or professional properties with repayment arising from the owner's business cash flows. To meet this classification, the owner's operation must occupy no less than 50% of the real estate held. Financial profitability and capacity to meet the cyclical nature of the industry and related real estate market over a significant timeframe is essential.
Real estate construction and other land loans - Land and construction 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 costs 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.
Agricultural real estate - Agricultural loans secured by real estate generally possess a higher inherent risk of loss caused by changes in concentration of permanent plantings, government subsidies, and the value of the U.S. dollar affecting the export of commodities.
Investor commercial real estate - Investor 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 flows to service debt obligations.
Other real estate - Primarily loans secured by agricultural real estate for development and production of permanent plantings that have not reached maximum yields. Also real estate loans where agricultural vertical integration exists in packing and shipping of commodities. Risk is primarily based on the liquidity of the borrower to sustain payment during the development period.

Consumer:
Equity loans and lines of credit - The degree of risk in residential real estate lending 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 may indicate that the borrowers' capacity to repay their obligations may be deteriorating.
Installment and other consumer loans - An installment loan portfolio is usually comprised of a large number of small loans scheduled to be amortized over a specific period. Most installment loans are made directly for consumer purchases. Other consumer loans include credit card and other open ended unsecured consumer loans. Credit cards and open ended unsecured loans generally have a higher rate of default than all other portfolio segments and are also impacted by weak economic conditions and trends. Credit cards and open ended unsecured loans in homogeneous loan portfolio segments are not evaluated for specific impairment.
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 Company's primary regulators, the FDIC and California Department of Business Oversight, 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.

Risk Rating - The Company 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. The most recent review of risk rating was completed in December 2016. These risk ratings are also subject to examination by independent specialists engaged by the Company, and the Company'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 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 Company's credit position at some future date. Special Mention loans are not adversely classified and do not expose the Company 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 Company 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. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors, which may work to the advantage and strengthening of the asset, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition, or liquidation procedures, capital injection, perfecting liens on additional collateral, and refinancing plans. Doubtful classification is considered temporary and short term.
Loss - Loans classified as loss are considered uncollectible and charged off immediately.
The general reserve component of the allowance for credit 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 including economic trends in the Company’s service areas, industry experience and trends, geographic concentrations, estimated collateral values, the Company’s underwriting policies, the character of the loan portfolio, and probable losses inherent in the portfolio taken as a whole. Inherent credit risk and qualitative reserve factors are inherently subjective and are driven by the repayment risk associated with each class of loans.

Bank Premises and Equipment - Land is carried at cost. Bank premises and equipment are carried at cost less accumulated depreciation. Depreciation is determined using the straight-line method over the estimated useful lives of the related assets. The useful lives of Bank premises are estimated to be between twenty and forty years. The useful lives of improvements to Bank premises, furniture, fixtures and equipment are estimated to be three to ten years. Leasehold improvements are amortized over the life of the asset or the term of the related lease, whichever is shorter. When assets are sold or otherwise disposed of, the cost and related accumulated depreciation 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.
The Bank evaluates premises and equipment for financial impairment as events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable.

Federal Home Loan Bank (FHLB) Stock - The Bank is a member of the FHLB system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. FHLB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income.

Investments in Low Income Housing Tax Credit Funds - The Bank has invested in limited partnerships that were formed to develop and operate affordable housing projects for low or moderate income tenants throughout California. Our ownership in each limited partnership is less than two percent. In accordance with ASU No. 2014-01, Investments - Equity Method and Joint Ventures (Topic 323), we elected to account for the investments in qualified affordable housing tax credit funds using the proportional amortization method. Under the proportional amortization method, the initial cost of the investment is amortized in proportion to the tax credits and other tax benefits received and the net investment performance is recognized as part of income tax expense (benefit). Each of the partnerships must meet the regulatory minimum requirements for affordable housing for a minimum 15-year compliance period to fully utilize the tax credits. If the partnerships cease to qualify during the compliance period, the credit may be denied for any period in which the project is not in compliance and a portion of the credit previously taken is subject to recapture with interest. The investment in Low Income Housing Tax Credit Funds is reported as part of other assets.

Other Real Estate Owned - Other real estate owned (OREO) is comprised of property acquired through foreclosure proceedings or acceptance of deeds-in-lieu of foreclosure. Losses recognized at the time of acquiring property in full or partial satisfaction of debt are charged against the allowance for credit losses. OREO, when acquired, is initially recorded at fair value less estimated disposition costs, establishing a new cost basis. Fair value of OREO is generally based on an independent appraisal of the property. Subsequent to initial measurement, OREO is carried at the lower of the recorded investment or fair value less disposition costs. If fair value declines subsequent to foreclosure, a valuation allowance is recorded through noninterest expense. Revenues and expenses associated with OREO are reported as a component of noninterest expense when incurred.

Foreclosed Assets - Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. If fair value declines subsequent to foreclosure, a valuation allowance is recorded through operations. Operating costs after acquisition are expensed. Gains and losses on disposition are included in noninterest expense.
The carrying value of foreclosed assets was $362,000 at December 31, 2016, and is included in other assets on the consolidated balance sheets. No foreclosed assets were recorded at December 31, 2015.

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

Business Combinations - The Company accounts for acquisitions of businesses using the acquisition method of accounting. Under the acquisition method, assets and liabilities assumed are recorded at their estimated fair values at the date of acquisition. Management utilizes various valuation techniques included discounted cash flow analyses to determine these fair values. Any excess of the purchase price over amounts allocated to the acquired assets, including identifiable intangible assets, and liabilities assumed is recorded as goodwill.

Goodwill - Business combinations involving the Bank's acquisition of the equity interests or net assets of another enterprise give rise to goodwill. Total goodwill at December 31, 2016 and 2015 represents the excess of the cost of Sierra Vista Bank, Visalia Community Bank, Service 1st Bancorp and Bank of Madera County over the net of the amounts assigned to assets acquired and liabilities assumed in the transactions accounted for under the purchase method of accounting. The value of goodwill is ultimately derived from the Bank's ability to generate net earnings after the acquisitions. A decline in net earnings could be indicative of a decline in the fair value of goodwill and result in impairment. For that reason, goodwill is assessed at least annually for impairment.
The Company has selected September 30 as the date to perform the annual impairment test. Management assessed qualitative factors including performance trends and noted no factors indicating goodwill impairment. Goodwill is also tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of the Company below its carrying amount. No such events or circumstances arose during the fourth quarter of 2016, so goodwill was not required to be retested. Goodwill is the only intangible asset with an indefinite life on our balance sheet.

Intangible Assets - The intangible assets at December 31, 2016 represent the estimated fair value of the core deposit relationships acquired in the acquisition of Sierra Vista Bank in 2016, and the 2013 acquisition of Visalia Community Bank. Core deposit intangibles are being amortized using the straight-line method over an estimated life of ten years from the date of acquisition. Management evaluates the remaining useful lives quarterly to determine whether events or circumstances warrant a revision to the remaining periods of amortization. Based on the evaluation, no changes to the remaining useful lives was required. Management performed an annual impairment test on core deposit intangibles as of September 30, 2016 and determined no impairment was necessary. Core deposit intangibles are also tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value below its carrying amount. No such events or circumstances arose during the fourth quarter of 2016, so core deposit intangibles were not required to be retested.

Loan Commitments and Related Financial Instruments - Financial instruments include off balance sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer financing needs. The face amount of these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

Income Taxes - The Company files its income taxes on a consolidated basis with its Subsidiary. The allocation of income tax expense represents each entity's proportionate share of the consolidated provision for income taxes. Income tax expense represents the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. On the balance sheet, net deferred tax assets are included in accrued interest receivable and other assets.
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 assets 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.

Accounting for Uncertainty in Income Taxes - The Company 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 consolidated statement of income.

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Retirement Plans - Employee 401(k) plan expense is the amount of employer matching contributions. Profit sharing plan expense is the amount of employer contributions. Contributions to the profit sharing plan are determined at the discretion of the Board of Directors. Deferred compensation and supplemental retirement plan expense is allocated over years of service.

Earnings Per Common Share - Basic earnings per common share (EPS), which excludes dilution, is computed by dividing income available to common shareholders (net income after deducting dividends, if any, on preferred stock and accretion of discount) by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock, such as stock options or warrants, result in the issuance of common stock which shares in the earnings of the Company. All data with respect to computing earnings per share is retroactively adjusted to reflect stock dividends and splits and the treasury stock method is applied to determine the dilutive effect of stock options in computing diluted EPS.

Comprehensive Income - Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on securities available for sale which are also recognized as separate components of equity.

Loss Contingencies - Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there are such matters that will have a material effect on the financial statements.

Restrictions on Cash: - Cash on hand or on deposit with the Federal Reserve Bank was required to meet regulatory reserve and clearing requirements.

Share-Based Compensation - Compensation cost is recognized for stock options and restricted stock awards issued to employees, based on the fair value of these awards at the date of grant. A Black-Scholes-Merton model is utilized to estimate the fair value of stock options, while the market price of the Company’s common stock at the date of grant is used for restricted stock awards.
Compensation cost is recognized over the required service period, generally defined as the vesting period. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award.
The cash flows from the tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) are classified as cash flows from financing activity in the statement of cash flows. Excess tax benefits for the years ended December 31, 2016, 2015, and 2014 were $30,000, $6,000, and $7,000, respectively.

Dividend Restriction: - Banking regulations require maintaining certain capital levels and may limit the dividends paid by the Bank to the Company or by the Company to shareholders.

Fair Value of Financial Instruments - Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in Note 3. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect these estimates.

Recently Issued Accounting Standards:

FASB Accounting Standards Update (ASU) 2016-01 - Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities, was issued January 2016. ASU 2016-01 addresses certain aspects of recognition, measurement presentation, and disclosure of financial instruments by making targeted improvements to GAAP as follows: (1) require equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. However, an entity may choose to measure equity investments that do not have readily determinable fair values at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer; (2) simplify the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment. When a qualitative assessment indicates that impairment exists, an entity is required to measure the investment at fair value; (3) eliminate the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities; (4) eliminate the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; (5) require public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (6)

require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments; (7) require separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements; and (8) clarify that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. ASU No. 2016-01 is effective for interim and annual reporting periods beginning after December 15, 2017. Early application is permitted as of the beginning of the fiscal year of adoption only for provisions (3) and (6) above. Early adoption of the other provisions mentioned above is not permitted. The Company has performed a preliminary evaluation of the provisions of ASU No. 2016-01. Based on this evaluation, the Company has determined that ASU No. 2016-01 is not expected to have a material impact on the Company's financial position, results of operations or cash flows.

FASB Accounting Standards Update (ASU) 2016-02 - Leases - Overall (Subtopic 845): was issued February 2016. Under the new guidance, lessees will be required to recognize the following for all leases (with the exception of short-term leases): 1) a lease liability, which is the present value of a lessee's obligation to make lease payments, and 2) a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Lessor accounting under the new guidance remains largely unchanged as it is substantially equivalent to existing guidance for sales-type leases, direct financing leases, and operating leases. Leveraged leases have been eliminated, although lessors can continue to account for existing leveraged leases using the current accounting guidance. Other limited changes were made to align lessor accounting with the lessee accounting model and the new revenue recognition standard. All entities will classify leases to determine how to recognize lease-related revenue and expense. Quantitative and qualitative disclosures will be required by lessees and lessors to meet the objective of enabling users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases. The intention is to require enough information to supplement the amounts recorded in the financial statements so that users can understand more about the nature of an entity's leasing activities. ASU No. 2016-02 is effective for interim and annual reporting periods beginning after December 15, 2018; early adoption is permitted. All entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. They have the option to use certain relief; full retrospective application is prohibited. The Company is currently evaluating the provisions of ASU No. 2016-02. The Company has determined that the provisions of ASU No. 2016-02 may result in an increase in assets to recognize the present value of the lease obligations with a corresponding increase in liabilities, however, the Company does not expect this to have a material impact on the Company's results of operations.

FASB Accounting Standards Update (ASU) 2016-09 - Compensation - Stock Compensation (Subtopic 718): Improvements to Employee Share-Based Payment Accounting, was issued March 2016. This ASU includes provisions intended to simplify various aspects related to how share-based payments are accounted for and presented in the financial statements. Some of the key provisions of this new ASU include: (1) companies will no longer record excess tax benefits and certain tax deficiencies in additional paid-in capital ("APIC"). Instead, they will record all excess tax benefits and tax deficiencies as income tax expense or benefit in the income statement, and APIC pools will be eliminated. The guidance also eliminates the requirement that excess tax benefits be realized before companies can recognize them. In addition, the guidance requires companies to present excess tax benefits as an operating activity on the statement of cash flows rather than as a financing activity; (2) increase the amount an employer can withhold to cover income taxes on awards and still qualify for the exception to liability classification for shares used to satisfy the employer's statutory income tax withholding obligation. The new guidance will also require an employer to classify the cash paid to a tax authority when shares are withheld to satisfy its statutory income tax withholding obligation as a financing activity on its statement of cash flows (current guidance did not specify how these cash flows should be classified); and (3) permit companies to make an accounting policy election for the impact of forfeitures on the recognition of expense for share-based payment awards. Forfeitures can be estimated, as required today, or recognized when they occur. ASU No. 2016-09 is effective for interim and annual reporting periods beginning after December 15, 2016. Early adoption was permitted, but all of the guidance must be adopted in the same period. The Company has evaluated the provisions of ASU No. 2016-09 to determine the potential impact of the new standard and has determined that it is not expected to have a material impact on the Company's financial position, results of operations or cash flows.

FASB Accounting Standards Update (ASU) 2016-13 - Measurement of Credit Losses on Financial Instruments (Subtopic 326): Financial Instruments - Credit Losses was issued June 2016. This ASU significantly changes how entities will measure credit losses for most financial assets and certain other instruments that aren't measured at fair value through net income. In issuing the standard, the FASB is responding to criticism that today's guidance delays recognition of credit losses. The standard will replace today's "incurred loss" approach with an "expected loss" model. The new model, referred to as the current expected credit loss ("CECL") model, will apply to: (1) financial assets subject to credit losses and measured at amortized cost, and (2) certain off-balance sheet credit exposures. This includes, but is not limited to, loans, leases, held-to-maturity securities, loan commitments, and financial guarantees. The CECL model does not apply to available-for-sale ("AFS") debt securities. For AFS

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debt securities with unrealized losses, entities will measure credit losses in a manner similar to what they do today, except that the losses will be recognized as allowances rather than reductions in the amortized cost of the securities. As a result, entities will recognize improvements to estimated credit losses immediately in earnings rather than as interest income over time, as they do today. The ASU also simplifies the accounting model for purchased credit-impaired debt securities and loans. ASU 2016-13 also expands the disclosure requirements regarding an entity’s assumptions, models, and methods for estimating the allowance for loan and lease losses. In addition, entities will need to disclose the amortized cost balance for each class of financial asset by credit quality indicator, disaggregated by the year of origination. ASU No. 2016-13 is effective for interim and annual reporting periods beginning after December 15, 2019; early adoption is permitted for interim and annual reporting periods beginning after December 15, 2018. Entities will apply the standard’s provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (i.e., modified retrospective approach). While the Company is currently evaluating the provisions of ASU No. 2016-13 to determine the potential impact the new standard will have on the Company’s Consolidated Financial Statements, it has taken steps to prepare for the implementation when it becomes effective, such as forming an internal task force, gathering pertinent data, consulting with outside professionals, and evaluating its current IT systems.

2. ACQUISITION OF SIERRA VISTA BANK

Effective October 1, 2016, the Company acquired Sierra Vista Bank, headquartered in Folsom, California, wherein Sierra Vista Bank, with one branch in Folsom, one branch in Fair Oaks, and one branch in Cameron Park, merged with and into Central Valley Community Bancorp’s subsidiary, Central Valley Community Bank, in a combined cash and stock transaction. Sierra Vista Bank’s assets (unaudited) as of October 1, 2016 totaled approximately $155.154 million. The acquired assets and liabilities were recorded at fair value at the date of acquisition. Under the terms of the merger agreement, the Company issued an aggregate of approximately 1.059 million shares of its common stock and cash totaling approximately $9.469 million to the former shareholders of Sierra Vista Bank.

In accordance with GAAP guidance for business combinations, the Company recorded $10.314 million of goodwill and $508,000 of other intangible assets on the acquisition date. The other intangible assets are primarily related to core deposits and are being amortized using a straight-line method over a period of ten years with no significant residual value. For tax purposes, purchase accounting adjustments including goodwill are all non-taxable and/or non-deductible. Acquisition related costs of $1,782,000 are included in the income statement for the year ended December 31, 2016.

The acquisition was consistent with the Company’s strategy to build a regional presence in Central California. The acquisition offers the Company the opportunity to increase profitability by introducing existing products and services to the acquired customer base as well as add new customers in the expanded region. Goodwill arising from the acquisition consisted largely of synergies and the cost savings resulting from the combined operations.

The following table summarizes the consideration paid for Sierra Vista Bank and the amounts of the assets acquired and liabilities assumed recognized at the acquisition date (in thousands):

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Merger consideration:	
Cash	$9,468
Common stock issued	16,793
Fair Value of Total Consideration Transferred	$26,261
Recognized amounts of identifiable assets acquired and liabilities assumed:	
Cash and cash equivalents	$22,709
Loans, net	122,533
Core deposit intangible	508
Premises and equipment	586
Federal Home Loan Bank stock	771
Deferred taxes and taxes receivable	4,417
Bank owned life insurance	2,664
Other assets	966
Total assets acquired	155,154
Deposits	138,236
Deposit premium	142
Other liabilities	829
Total liabilities assumed	139,207
Total identifiable net assets	15,947
Goodwill	$10,314

The fair value of net assets acquired includes fair value adjustments to certain loans that were not considered impaired as of the acquisition date. The fair value adjustments were determined using discounted contractual cash flows. As such, these loans were not considered impaired at the acquisition date and were not subject to the guidance relating to purchased credit impaired loans, which have shown evidence of credit deterioration since origination. Loans acquired that were not subject to these requirements include non-impaired loans and customer receivables with a fair value and gross contractual amounts receivable of $121,902,000 and $124,396,000, respectively, on the date of acquisition. See Note 5 for discussion of purchased credit impaired loans.

Pro Forma Results of Operations

The accompanying consolidated financial statements include the accounts of Sierra Vista Bank since October 1, 2016. The following table presents pro forma results of operations information for the periods presented as if the acquisition had occurred on January 1, 2015 after giving effect to certain adjustments. The unaudited pro forma results of operations for the years ended December 31, 2016 and 2015 include the historical accounts of the Company and Sierra Vista Bank and pro forma adjustments as may be required, including the amortization of intangibles with definite lives and the amortization or accretion of any premiums or discounts arising from fair value adjustments for assets acquired and liabilities assumed. The pro forma information is intended for informational purposes only and is not necessarily indicative of the Company’s future operating results or operating results that would have occurred had the acquisition been completed at the beginning of 2015. No assumptions have been applied to the pro forma results of operations regarding possible revenue enhancements, expense efficiencies or asset dispositions. (In thousands, except per-share amounts):

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	For the Years Ended December 31,	
	2016	2015
Net interest income	$50,491	$46,499
Provision for credit losses	(5,750)	645
Non-interest income	9,930	9,912
Non-interest expense	47,350	40,971
Income before provision for income taxes	18,821	14,795
Provision for income taxes	5,817	3,101
Net income	$13,004	$11,694
Net income available to common shareholders	$13,004	$11,694
Basic earnings per common share	$1.15	$1.07
Diluted earnings per common share	$1.14	$1.06

3. FAIR VALUE MEASUREMENTS

Fair Value Hierarchy

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. In accordance with applicable guidance, the Company 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 (unadjusted) for identical instruments traded in active exchange markets that the Company has the ability to access as of the measurement date.

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 Company’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, we report the transfer at the beginning of the reporting period.
The estimated carrying and fair values of the Company’s financial instruments are as follows (in thousands):

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	December 31, 2016				
	Carrying	Fair Value			
	Amount	Level 1	Level 2	Level 3	Total
Financial assets:					
Cash and due from banks	$28,185	$28,185	$ —	$ —	$ 28,185
Interest-earning deposits in other banks	10,368	10,368	—	—	10,368
Federal funds sold	15	15	—	—	15
Available-for-sale investment securities	547,749	7,416	540,333	—	547,749
Loans, net	747,302	—	—	761,023	761,023
Federal Home Loan Bank stock	5,594	N/A	N/A	N/A	N/A
Accrued interest receivable	7,885	26	4,517	3,342	7,885
Financial liabilities:					
Deposits	1,255,979	1,099,200	156,711	—	1,255,911
Short-term borrowings	400	—	400	—	400
Junior subordinated deferrable interest debentures	5,155	—	—	3,235	3,235
Accrued interest payable	144	—	111	33	144

	December 31, 2015				
	Carrying	Fair Value			
	Amount	Level 1	Level 2	Level 3	Total
Financial assets:					
Cash and due from banks	$23,339	$23,339	$ —	$ —	$ 23,339
Interest-earning deposits in other banks	70,988	70,988	—	—	70,988
Federal funds sold	290	290	—	—	290
Available-for-sale investment securities	477,554	7,536	470,018	—	477,554
Held-to-maturity investment securities	31,712	—	35,142	—	35,142
Loans, net	588,501	—	—	585,737	585,737
Federal Home Loan Bank stock	4,823	N/A	N/A	N/A	N/A
Accrued interest receivable	6,355	27	3,414	2,914	6,355
Financial liabilities:					
Deposits	1,116,267	976,433	139,353	—	1,115,786
Junior subordinated deferrable interest debentures	5,155	—	—	3,200	3,200
Accrued interest payable	101	—	76	25	101

These estimates do not reflect any premium or discount that could result from offering the Company'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. These estimates are made at a specific point in time based on relevant market data and information about the financial instruments. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the fair values presented.

The methods and assumptions used to estimate fair values are described as follows:

(a) Cash and Cash Equivalents — The carrying amounts of cash and due from banks, interest-earning deposits in other banks, and Federal funds sold approximate fair values and are classified as Level 1.

(b) Investment Securities — Investment securities in Level 1 are mutual funds and fair values are based on quoted market prices for identical instruments traded in active markets. Fair values for investment securities classified in Level 2 are based on quoted market prices for similar securities in active markets. For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators.

(c) Loans — Fair values of loans are estimated as follows: For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values resulting in a Level 3 classification. Purchased credit impaired (PCI) loans are measured at estimated fair value on the date of acquisition. Carrying value is calculated as the present value of expected cash flows and approximates fair value. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality resulting in a Level 3 classification. Impaired loans are initially valued at the lower of cost or fair value. Impaired loans carried at fair value generally receive specific allocations of the allowance for credit losses. For collateral dependent loans, fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

(d) FHLB Stock — It is not practicable to determine the fair value of FHLB stock due to restrictions placed on its transferability.

e) Other real estate owned — OREO is measured at fair value less estimated costs to sell when acquired, establishing a new cost basis. Fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process to adjust for differences between the comparable sales and income data available. The Company records OREO as non-recurring with level 3 measurement inputs.

(f) Deposits — Fair value of demand deposit, savings, and money market accounts are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amount) resulting in a Level 1 classification. Fair value for fixed and variable rate certificates of deposit are estimated using discounted cash flow analyses using interest rates offered at each reporting date by the Company for certificates with similar remaining maturities resulting in a Level 2 classification.

(g) Short-Term Borrowings — The carrying amounts of federal funds purchased, borrowings under repurchase agreements, and other short-term borrowings, generally maturing within ninety days, approximate their fair values resulting in a Level 2 classification.

(h) Other Borrowings — The fair values of the Company's long-term borrowings are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 2 classification.

The fair values of the Company's Subordinated Debentures are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 3 classification.

(i) Accrued Interest Receivable/Payable — The fair value of accrued interest receivable and payable is based on the fair value hierarchy of the related asset or liability.

(j) Off-Balance Sheet Instruments — Fair values for off-balance sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value of commitments is not material.

Assets Recorded at Fair Value

The following tables present information about the Company's assets and liabilities measured at fair value on a recurring and non-recurring basis as of December 31, 2016:

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Recurring Basis

The Company is required or permitted to record the following assets at fair value on a recurring basis under other accounting pronouncements (in thousands):

	Fair Value	Level 1	Level 2	Level 3
Available-for-sale investment securities				
Debt Securities:				
U.S. Government agencies	$68,970	$—	$68,970	$ —
Obligations of states and political subdivisions	290,299	—	290,299	—
U.S. Government sponsored entities and agencies collateralized by residential mortgage obligations	178,221	—	178,221	—
Private label residential mortgage backed securities	2,843	—	2,843	—
Other equity securities	7,416	7,416	—	—
Total assets measured at fair value on a recurring basis	$547,749	$7,416	$540,333	$ —

Securities in Level 1 are mutual funds and fair values are based on quoted market prices for identical instruments traded in active markets. Fair values for available-for-sale investment securities in Level 2 are based on quoted market prices for similar securities in active markets. For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators. 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. During the year ended December 31, 2016, no transfers between levels occurred.
There were no Level 3 assets measured at fair value on a recurring basis at December 31, 2016. Also there were no liabilities measured at fair value on a recurring basis at December 31, 2016.

Non-recurring Basis

The Company may be required, from time to time, to measure certain assets and liabilities at fair value on a non-recurring basis. These include the following assets and liabilities that are measured at the lower of cost or fair value that were recognized at fair value which was below cost at December 31, 2016 (in thousands):