UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(MARK ONE)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2024

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 000-23877

Heritage Commerce Corp

(Exact name of Registrant as Specified in its Charter)

California (State or Other Jurisdiction of Incorporation or Organization)	**77-0469558** (I.R.S. Employer Identification No.)
224 Airport Parkway, San Jose, California (Address of Principal Executive Offices)	**95110** (Zip Code)

(408) 947-6900
(Registrant's Telephone Number, Including Area Code)

N/A
(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:	Trading Symbol:	Name of each exchange on which registered:
Common Stock, No Par Value	**HTBK**	**The Nasdaq Stock Market LLC**

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 ☒ NO ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). YES ☒ NO ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐	Accelerated filer ☒	Non-accelerated filer ☐	Smaller reporting company ☐
			Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ☐ NO ☒

The Registrant had 61,255,913 shares of Common Stock outstanding on April 29, 2024.

HERITAGE COMMERCE CORP
QUARTERLY REPORT ON FORM 10-Q
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Cautionary Note Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q (this "Report") of Heritage Commerce Corp ("we," "us," "our" or the "Company") contains various statements that may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, Rule 175 promulgated thereunder, and Section 21E of the Securities Exchange Act of 1934, as amended, Rule 3b-6 promulgated thereunder and are intended to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. All statements about our expectations, beliefs, plans, objectives, assumptions or future events or performance are not historical facts and may be forward-looking. These forward-looking statements often can be, but are not always, identified by the use of words such as "assume," "expect," "intend," "plan," "project," "believe," "estimate," "predict," "anticipate," "may," "might," "should," "could," "goal," "potential" and similar expressions. We base these forward-looking statements on our current expectations and projections about future events, our assumptions regarding these events and our knowledge of facts at the time the statements are made. Forward-looking statements may include, among other things, statements relating to our projected growth, anticipated future financial performance, management's long-term performance goals and operational strategies, the performance of our loan and investment portfolios, as well as statements relating to the anticipated effects of those conditions, events and developments on the Company's financial condition and results of operations.

These forward-looking statements are subject to various risks and uncertainties that may be outside our control and our actual results could differ materially and adversely from our projected results. Risks and uncertainties that could cause our financial performance to differ materially from our goals, plans, expectations and projections expressed in forward-looking statements including those set forth below under "*Part II, Item 1A—Risk Factors*" of this Report, and including, but not limited to the following:

- factors that affect our liquidity and our ability to meet customer demands for deposit withdrawals, including our cash on hand and the availability of funds from our lines of credit;
- media items and consumer confidence as those factors affect depositors' confidence in the banking system generally and in our bank specifically;
- factors that affect the value and liquidity of our investment portfolios, particularly the values of securities available-for-sale;
- market fluctuations that affect the costs we pay for sources of funding, including the interest we pay on deposits and loans;
- effects of and changes in trade, monetary and fiscal policies and laws, including the interest rate policies of the Federal Open Market Committee of the Federal Reserve Board and other factors that affect market interest rates generally;
- our ability to estimate accurately, and to establish adequate reserves against, the risk of loss associated with our loan and lease portfolio;
- events and circumstances that affect our borrowers' financial condition, results of operations and cash flows, which may, during periods of economic uncertainty or decline, adversely affect those borrowers' ability to repay our loans timely and in full, or to comply with their other obligations under our loan agreements with those customers;
- factors that affect the relative strength or weakness of loan guarantees and the ability of the guarantors to fulfill the obligations of their guaranty agreements;
- geopolitical and domestic political developments, including recent, current and potential future wars and international and multinational conflicts, acts of terrorism, insurrection, piracy and civil unrest, and events reflecting or resulting from social instability, any of which can increase levels of political and economic unpredictability, contribute to rising energy and commodity prices, can affect the physical security of our assets and the assets of our customers, and which may increase the volatility of financial markets;

- current and future economic and market conditions in the United States generally or in the communities we serve, including the effects of declines in property values and overall slowdowns in economic growth should these events occur;
- inflationary pressures and changes in the interest rate environment that reduce our margins and yields, the fair value of financial instruments or our level of loan originations, or increase the level of defaults, losses and prepayments on loans to customers, whether held in the portfolio or in the secondary market;
- changes in the level of nonperforming assets and charge offs and other credit quality measures, and their impact on the adequacy of our allowance for credit losses and our provision for credit losses;
- volatility in credit and equity markets and its effect on the global economy;
- conditions relating to the impact of recent and potential future pandemics, epidemics and other infectious illness outbreaks that may arise in the future, on our customers, employees, businesses, liquidity, financial results and overall condition including severity and duration of the associated uncertainties in U.S. and global markets;
- our ability to compete effectively with other banks and financial services companies and the effects of competition in the financial services industry on our business;
- our ability to achieve loan growth and attract deposits in our market area;
- risks associated with concentrations in real estate related loans;
- the relative strength or weakness of the commercial and real estate markets where our borrowers are located, including related vacancy rates, and asset and market prices;
- increased capital requirements for our continual growth or as imposed by banking regulators, which may require us to raise capital at a time when capital is not available on favorable terms or at all;
- regulatory limits and practical factors that affect Heritage Bank of Commerce’s ability to pay dividends to the Company;
- operational issues stemming from, and/or capital spending necessitated by, the potential need to adapt to industry changes in information technology systems, on which we are highly dependent;
- our inability to attract, recruit, and retain qualified officers and other personnel could harm our ability to implement our strategic plan, impair our relationships with customers and adversely affect our business, results of operations and growth prospects;
- possible adjustment of the valuation of our deferred tax assets or of the goodwill associated with previous acquisitions;
- our ability to keep pace with technological changes, including our ability to identify and address cyber-security risks, including those posed by the increasing use of artificial intelligence, such as data security breaches, “denial of service” attacks, “hacking” and identity theft affecting us or third party vendors or service providers;
- inability of our framework to manage risks associated with our business, including operational risk and credit risk;
- risks of loss of funding of the Small Business Administration (“SBA”) or SBA loan programs, or changes in those programs;
- compliance with applicable laws and governmental and regulatory requirements, including the Dodd-Frank Act and others relating to banking, consumer protection, securities, accounting and tax matters;

- effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard setters;
- the expense and uncertain resolution of litigation matters whether occurring in the ordinary course of business or otherwise;
- availability of and competition for acquisition opportunities;
- geographic and sociopolitical factors that arise by virtue of the fact that we operate primarily in the general San Francisco Bay Area of Northern California;
- risks of natural disasters (including earthquakes, fires, and flooding) and other events beyond our control;
- actions taken, planned, or announced by federal, state, regional and local governments in response to the occurrence or threat of any of the foregoing; and
- our success in managing the risks involved in the foregoing factors.

Forward-looking statements speak only as of the date they are made. The Company does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date the forward-looking statements are made or to reflect the occurrence of unanticipated events. *You should consider any forward-looking statements in light of this explanation, and we caution you about relying on forward-looking statements.*

Part I—FINANCIAL INFORMATION

ITEM 1—CONSOLIDATED FINANCIAL STATEMENTS

HERITAGE COMMERCE CORP
CONSOLIDATED BALANCE SHEETS
(Unaudited)

	March 31, 2024	December 31, 2023
	(Dollars in thousands)	
Assets		
Cash and due from banks	$ 32,543	$ 41,592
Other investments and interest-bearing deposits in other financial institutions	508,816	366,537
Total cash and cash equivalents	541,359	408,129
Securities available-for-sale, at fair value	404,474	442,636
Securities held-to-maturity, at amortized cost, net of allowance for credit losses of $12 (fair value of $542,858 and $564,127, respectively)	636,249	650,565
Loans held-for-sale - SBA, at lower of cost or fair value, including deferred costs	1,946	2,205
Loans, net of deferred fees	3,336,102	3,350,378
Allowance for credit losses on loans	(47,888)	(47,958)
Loans, net	3,288,214	3,302,420
Federal Home Loan Bank ("FHLB"), Federal Reserve Bank ("FRB") stock and other investments, at cost	32,544	32,540
Company-owned life insurance	80,007	79,489
Premises and equipment, net	9,986	9,857
Goodwill	167,631	167,631
Other intangible assets	8,074	8,627
Accrued interest receivable and other assets	85,590	89,996
Total assets	$ 5,256,074	$ 5,194,095
Liabilities and Shareholders' Equity		
Liabilities:		
Deposits:		
Demand, noninterest-bearing	$ 1,242,059	$ 1,292,486
Demand, interest-bearing	925,100	914,066
Savings and money market	1,124,900	1,087,518
Time deposits - under $250	38,105	38,055
Time deposits - $250 and over	200,739	192,228
Insured Cash Sweep ("ICS")/Certificates of Deposit Account Registry Service ("CDARS") - interest-bearing demand, money market and time deposits	913,757	854,105
Total deposits	4,444,660	4,378,458
Subordinated debt, net of issuance costs	39,539	39,502
Accrued interest payable and other liabilities	95,579	103,234
Total liabilities	4,579,778	4,521,194
Shareholders' equity:		
Preferred stock, no par value; 10,000,000 shares authorized; none issued and outstanding at March 31, 2024 and December 31, 2023	—	—
Common stock, no par value; 100,000,000 shares authorized; 61,253,625 and 61,146,835 shares issued and outstanding, respectively	507,578	506,539
Retained earnings	181,306	179,092
Accumulated other comprehensive loss	(12,588)	(12,730)
Total shareholders' equity	676,296	672,901
Total liabilities and shareholders' equity	$ 5,256,074	$ 5,194,095

See notes to consolidated financial statements (unaudited).

HERITAGE COMMERCE CORP
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	March 31, 2024	March 31, 2023
	(Dollars in thousands, except per share amounts)	
Interest income:		
Loans, including fees	$ 44,600	$ 44,112
Securities, taxable	6,183	7,056
Securities, exempt from Federal tax	226	247
Other investments, interest-bearing deposits in other financial institutions and Federal funds sold	6,542	4,859
Total interest income	57,551	56,274
Interest expense:		
Deposits	16,920	5,901
Short-term borrowings	—	578
Subordinated debt	538	537
Total interest expense	17,458	7,016
Net interest income before provision for credit losses on loans	40,093	49,258
Provision for credit losses on loans	184	32
Net interest income after provision for credit losses on loans	39,909	49,226
Noninterest income:		
Service charges and fees on deposit accounts	877	1,743
Increase in cash surrender value of life insurance	518	493
Gain on sales of SBA loans	178	76
Servicing income	90	131
Termination fees	13	11
Other	371	312
Total noninterest income	2,047	2,766
Noninterest expense:		
Salaries and employee benefits	15,509	14,809
Occupancy and equipment	2,443	2,400
Professional fees	1,327	1,399
Other	8,257	6,793
Total noninterest expense	27,536	25,401
Income before income taxes	14,420	26,591
Income tax expense	4,254	7,674
Net income	$ 10,166	$ 18,917
Earnings per common share:		
Basic	$ 0.17	$ 0.31
Diluted	$ 0.17	$ 0.31

See notes to consolidated financial statements (unaudited).

HERITAGE COMMERCE CORP
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended March 31,	
	2024	**2023**
	(Dollars in thousands)	
Net income	$ 10,166	$ 18,917
Other comprehensive income:		
Change in net unrealized holding gains on available-for-sale securities and I/O strips	248	3,631
Deferred income taxes	(72)	(1,054)
Change in unrealized gains on securities and I/O strips, net of deferred income taxes	176	2,577
Change in net pension and other benefit plan liability adjustment	(26)	(34)
Deferred income taxes	(8)	(4)
Change in pension and other benefit plan liability, net of deferred income taxes	(34)	(38)
Other comprehensive income	142	2,539
Total comprehensive income	$ 10,308	$ 21,456

See notes to consolidated financial statements (unaudited).

HERITAGE COMMERCE CORP
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Unaudited)

	Common Stock		Retained	Accumulated Other Comprehensive	Total Shareholders'
	Shares	Amount	Earnings	Loss	Equity
		(Dollars in thousands, except per share amounts)			
Balance, January 1, 2023	60,852,723	$ 502,923	$ 146,389	$ (16,856)	$ 632,456
Net income	—	—	18,917	—	18,917
Other comprehensive income	—	—	—	2,539	2,539
Amortization of restricted stock awards, net of forfeitures and taxes	—	382	—	—	382
Cash dividend declared $0.13 per share	—	—	(7,916)	—	(7,916)
Stock option expense, net of forfeitures and taxes	—	147	—	—	147
Stock options exercised	95,884	683	—	—	683
Balance March 31, 2023	60,948,607	$ 504,135	$ 157,390	$ (14,317)	$ 647,208
Balance, January 1, 2024	61,146,835	$ 506,539	$ 179,092	$ (12,730)	$ 672,901
Net income	—	—	10,166	—	10,166
Other comprehensive income	—	—	—	142	142
Issuance of restricted stock awards, net of forfeitures	33,908	—	—	—	—
Amortization of restricted stock awards, net of forfeitures and taxes	—	311	—	—	311
Cash dividend declared $0.13 per share	—	—	(7,952)	—	(7,952)
Restricted stock units ("RSUs") and performance-based restricted stock units ("PRSUs") expense, net of taxes	—	198	—	—	198
Stock option expense, net of forfeitures and taxes	—	145	—	—	145
Stock options exercised	72,882	385	—	—	385
Balance March 31, 2024	61,253,625	$ 507,578	$ 181,306	$ (12,588)	$ 676,296

See notes to consolidated financial statements (unaudited).

HERITAGE COMMERCE CORP
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	March 31, 2024	March 31, 2023
	(Dollars in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 10,166	$ 18,917
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of premiums and accretion of discounts on securities	(936)	(1,258)
Gain on sale of SBA loans	(178)	(76)
Proceeds from sale of SBA loans originated for sale	1,978	1,045
SBA loans originated for sale	(1,541)	(1,305)
Provision for credit losses on loans	184	32
Increase in cash surrender value of life insurance	(518)	(493)
Depreciation and amortization	300	272
Amortization of other intangible assets	553	602
Stock option expense, net	145	147
RSUs and PRSUs expense	198	—
Amortization of restricted stock awards, net	311	382
Amortization of subordinated debt issuance costs	37	37
Effect of changes in:		
Accrued interest receivable and other assets	4,861	(519)
Accrued interest payable and other liabilities	(8,222)	12,175
Net cash provided by operating activities	7,338	29,958
CASH FLOWS FROM INVESTING ACTIVITIES:		
Maturities/paydowns/calls of securities available-for-sale	39,596	3,014
Maturities/paydowns/calls of securities held-to-maturity	14,072	16,485
Net change in loans	14,022	36,364
Changes in FHLB stock and other investments	(4)	(4)
Purchase of premises and equipment	(429)	(113)
Net cash provided by investing activities	67,257	55,746
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net change in deposits	66,202	54,934
Net change in short-term borrowings	—	300,000
Exercise of stock options	385	683
Payment of cash dividends	(7,952)	(7,916)
Net cash provided by financing activities	58,635	347,701
Net increase in cash and cash equivalents	133,230	433,405
Cash and cash equivalents, beginning of period	408,129	306,603
Cash and cash equivalents, end of period	$ 541,359	$ 740,008
Supplemental disclosures of cash flow information:		
Interest paid	$ 16,350	$ 5,657
Supplemental schedule of non-cash activity:		
Recording of right of use assets in exchange for lease obligations	$ —	$ 384

See notes to consolidated financial statements (unaudited).

HERITAGE COMMERCE CORP
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2024
(Unaudited)

1) Basis of Presentation

The unaudited consolidated financial statements of Heritage Commerce Corp (the "Company" or "HCC") and its wholly owned subsidiary, Heritage Bank of Commerce (the "Bank" or "HBC"), have been prepared pursuant to the rules and regulations for reporting on Form 10-Q. Accordingly, certain information and notes required by accounting principles generally accepted in the United States of America ("GAAP") for annual financial statements are not included herein. The interim statements should be read in conjunction with the consolidated financial statements and notes that were included in the Company's Form 10-K for the year ended December 31, 2023.

HBC is a commercial bank serving customers primarily located in Alameda, Contra Costa, Marin, San Benito, San Francisco, San Mateo, and Santa Clara counties of California. CSNK Working Capital Finance Corp. a California corporation, dba Bay View Funding ("Bay View Funding") is a wholly owned subsidiary of HBC, and provides business-essential working capital factoring financing to various industries throughout the United States. No customer accounts for more than 10% of revenue for HBC or the Company. The Company reports its results for two segments: banking and factoring. The Company's management uses segment results in its operating and strategic planning.

In management's opinion, all adjustments necessary for a fair presentation of these consolidated financial statements have been included and are of a normal and recurring nature. All intercompany transactions and balances have been eliminated.

The preparation of financial statements in accordance with GAAP requires management to make a number of judgments, estimates and assumptions that affect the reported amount of assets, liabilities, income and expense in the financial statements. Various elements of our accounting policies, by their nature, involve the application of highly sensitive and judgmental estimates and assumptions. Some of these policies and estimates relate to matters that are highly complex and contain inherent uncertainties. Material estimates that are particularly susceptible to significant change include the determination of the allowance for credit losses and any impairment of goodwill or intangible assets. It is possible that, in some instances, different estimates and assumptions could reasonably have been made and used by management, instead of those we applied, which might have produced different results that could have had a material effect on the financial statements.

The results for the three months ended March 31, 2024 are not necessarily indicative of the results expected for any subsequent period or for the entire year ending December 31, 2024.

Reclassifications

Certain reclassifications of prior year balances have been made to conform to the current year presentation. These reclassifications had no impact on the Company's consolidated financial position, results of operations or net change in cash and cash equivalents.

Adoption of New Accounting Standards

Accounting Standards Update ("ASU") No. 2023-07,"Segment Reporting (Topic 280): Improvements to Reportable Segment Disclosures." ("ASU 2023-07) requires filers to disclose significant segment expenses, an amount and description for other segment items, the title and position of the entity's chief operating decision maker ("CODM") and an explanation of how the CODM uses the reported measures of profit or loss to assess segment performance, and, on an interim basis, certain segment related disclosures that previously were required only on an annual basis. ASU 2023-07 also clarifies that entities with a single reportable segment are subject to both new and existing segment reporting requirements and that an entity is permitted to disclose multiple measures of segment profit or loss, provided that certain criteria are met. ASU 2023-07 is effective for the Company for fiscal years beginning after December 15, 2023 and interim periods within fiscal years beginning after December 15, 2024, with early adoption permitted. Effective January 1, 2024, the Company adopted the guidance prescribed under ASU 2023-07, and it did not have a material impact on our consolidated financial statements for the first quarter of 2024.

Accounting Guidance Issued But Not Yet Adopted

In December 2023, the Financial Accounting Standards Board ("FASB") issued ASU No. 2023-09, Income Taxes (Topic 740): *Improvements to Income Tax Disclosures* . The updated accounting guidance requires expanded income tax disclosures, including the disaggregation of existing disclosures related to the tax rate reconciliation and income taxes paid. The guidance is effective for annual periods beginning after December 15, 2024. Prospective application is required, with retrospective application permitted. Management is evaluating the impact of this ASU to the financial statement disclosures.

2) Earnings Per Share

Basic earnings per common share is computed by dividing net income by the weighted average common shares outstanding. Diluted earnings per share reflect potential dilution from outstanding stock options using the treasury stock method. Unvested restricted stock units are not considered participating securities and as a result are not considered outstanding under the two class method of computing basic earnings per common share. There were 1,904,786 weighted average stock options outstanding for the three months ended March 31, 2024 considered to be antidilutive and excluded from the computation of diluted earnings per share. There were 1,314,428 weighted average stock options outstanding for the three months ended March 31, 2023 considered to be antidilutive and excluded from the computation of diluted earnings per share. There were 65,805 weighted average RSUs outstanding for the three months ended March 31, 2024 considered to be antidilutive and excluded from the computation of diluted earnings per shares. There were no weighted average RSUs outstanding for the three months ended March 31, 2023 considered to be antidilutive and excluded from the computation of diluted earnings per shares. A reconciliation of these factors used in computing basic and diluted earnings per common share is as follows:

	Three Months Ended March 31,	
	2024	2023
	(Dollars in thousands, except per share amounts)	
Net income	$ 10,166	$ 18,917
Weighted average common shares outstanding		
for basic earnings per common share	61,186,623	60,908,221
Dilutive potential common shares	283,929	359,851
Shares used in computing diluted earnings per common share	$ 61,470,552	$ 61,268,072
Basic earnings per share	$ 0.17	$ 0.31
Diluted earnings per share	$ 0.17	$ 0.31

3) Accumulated Other Comprehensive Income (Loss) ("AOCI")

The following table reflects the changes in AOCI by component for the periods indicated:

	Three Months Ended March 31, 2024 and 2023		
	Unrealized Gains (Losses) on Available-for-Sale Securities and I/O Strips	Defined Benefit Pension Plan Items(1)	Total
	(Dollars in thousands)		
Beginning balance January 1, 2024, net of taxes	$ (7,029)	$ (5,701)	$ (12,730)
Other comprehensive income (loss) before reclassification, net of taxes	176	(16)	160
Amounts reclassified from other comprehensive income (loss), net of taxes	—	(18)	(18)
Net current period other comprehensive income (loss), net of taxes	176	(34)	142
Ending balance March 31, 2024, net of taxes	$ (6,853)	$ (5,735)	$ (12,588)
Beginning balance January 1, 2023, net of taxes	$ (11,394)	$ (5,462)	$ (16,856)
Other comprehensive income (loss) before reclassification, net of taxes	2,577	(14)	2,563
Amounts reclassified from other comprehensive income (loss), net of taxes	—	(24)	(24)
Net current period other comprehensive income (loss), net of taxes	2,577	(38)	2,539
Ending balance March 31, 2023, net of taxes	$ (8,817)	$ (5,500)	$ (14,317)

(1) This AOCI component is included in the computation of net periodic benefit cost (see Note 8—Benefit Plans) and includes split-dollar life insurance benefit plan.

Details About AOCI Components	Amounts Reclassified from AOCI Three Months Ended March 31, 2024	2023	Affected Line Item Where Net Income is Presented
	(Dollars in thousands)		
Amortization of defined benefit pension plan items [1]			
Prior transition obligation and actuarial losses [2]	$ 52	$ 47	
Prior service cost and actuarial losses [3]	(26)	(13)	
	26	34	Other noninterest expense
	(8)	(10)	Income tax benefit
	18	24	Net of tax
Total reclassification from AOCI for the period	$ 18	$ 24	

(1) This AOCI component is included in the computation of net periodic benefit cost (see Note 8—Benefit Plans).
(2) This is related to the split dollar life insurance benefit plan.
(3) This is related to the supplemental executive retirement plan.

4) Securities

The amortized cost and estimated fair value of securities were as follows for the periods indicated:

March 31, 2024	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Allowance for Credit Losses	Estimated Fair Value
			(Dollars in thousands)		
Securities available-for-sale:					
U.S. Treasury	$ 352,237	$ —	$ (4,784)	$ —	$ 347,453
Agency mortgage-backed securities	61,916	—	(4,895)	—	57,021
Total	$ 414,153	$ —	$ (9,679)	$ —	$ 404,474

March 31, 2024	Amortized Cost	Gross Unrecognized Gains	Gross Unrecognized (Losses)	Estimated Fair Value	Allowance for Credit Losses
			(Dollars in thousands)		
Securities held-to-maturity:					
Agency mortgage-backed securities	$ 604,458	$ 83	$ (92,415)	$ 512,126	$ —
Municipals - exempt from Federal tax	31,803	1	(1,072)	30,732	(12)
Total	$ 636,261	$ 84	$ (93,487)	$ 542,858	$ (12)

December 31, 2023	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Allowance for Credit Losses	Estimated Fair Value
			(Dollars in thousands)		
Securities available-for-sale:					
U.S. Treasury	$ 387,990	$ —	$ (5,621)	$ —	$ 382,369
Agency mortgage-backed securities	64,580	—	(4,313)	—	60,267
Total	$ 452,570	$ —	$ (9,934)	$ —	$ 442,636

December 31, 2023	Amortized Cost	Gross Unrecognized Gains	Gross Unrecognized (Losses)	Estimated Fair Value	Allowance for Credit Losses
			(Dollars in thousands)		
Securities held-to-maturity:					
Agency mortgage-backed securities	$ 618,374	$ 282	$ (86,011)	$ 532,645	$ —
Municipals - exempt from Federal tax	32,203	3	(724)	31,482	(12)
Total	$ 650,577	$ 285	$ (86,735)	$ 564,127	$ (12)

Securities with unrealized/unrecognized losses aggregated by investment category and length of time that individual securities have been in a continuous unrealized/unrecognized loss position are as follows for the periods indicated:

	Less Than 12 Months		12 Months or More		Total	
March 31, 2024	Fair Value	Unrealized (Losses)	Fair Value	Unrealized (Losses)	Fair Value	Unrealized (Losses)
			(Dollars in thousands)			
Securities available-for-sale:						
U.S. Treasury	$ 4,907	$ (65)	$ 342,546	$ (4,719)	$ 347,453	$ (4,784)
Agency mortgage-backed securities	—	—	57,021	(4,895)	57,021	(4,895)
Total	$ 4,907	$ (65)	$ 399,567	$ (9,614)	$ 404,474	$ (9,679)
Securities held-to-maturity:						
Agency mortgage-backed securities	$ —	$ —	$ 500,329	$ (92,415)	$ 500,329	$ (92,415)
Municipals — exempt from Federal tax	9,246	(147)	20,226	(925)	29,472	(1,072)
Total	$ 9,246	$ (147)	$ 520,555	$ (93,340)	$ 529,801	$ (93,487)

December 31, 2023	Less Than 12 Months Fair Value	Less Than 12 Months Unrealized (Losses)	12 Months or More Fair Value	12 Months or More Unrealized (Losses)	Total Fair Value	Total Unrealized (Losses)
			(Dollars in thousands)			
Securities available-for-sale:						
U.S. Treasury	$ 4,926	$ (40)	$ 377,443	$ (5,581)	$ 382,369	$ (5,621)
Agency mortgage-backed securities	—	—	60,267	(4,313)	60,267	(4,313)
Total	$ 4,926	$ (40)	$ 437,710	$ (9,894)	$ 442,636	$ (9,934)
Securities held-to-maturity:						
Agency mortgage-backed securities	$ —	$ —	$ 520,615	$ (86,011)	$ 520,615	$ (86,011)
Municipals — exempt from Federal tax	9,790	(176)	13,151	(548)	22,941	(724)
Total	$ 9,790	$ (176)	$ 533,766	$ (86,559)	$ 543,556	$ (86,735)

The Company conducts a regular assessment of its investment securities to determine whether securities are experiencing credit losses. Factors for consideration include the nature of the securities, credit ratings or financial condition of the issuer, the extent of the unrealized loss, expected cash flows, market conditions and the Company's ability to hold the securities through the anticipated recovery period. No credit losses are expected in the Company investment securities.

There were no holdings of securities of any one issuer, other than the U.S. Government and its sponsored entities, in an amount greater than 10% of shareholders' equity. At March 31, 2024, the Company held 429 securities (157 available-for-sale and 272 held-to-maturity), of which 419 had fair value below amortized cost. The unrealized/unrecognized losses were due to higher interest rates at period end compared to when the securities were purchased. The issuers are of high credit quality and all principal amounts are expected to be paid when securities mature. The fair value is expected to recover as the securities approach their maturity date and/or market rates decline. The Company does not believe that it is more likely than not that the Company will be required to sell a security in an unrealized loss position prior to recovery in value.

The amortized cost and estimated fair values of securities as of March 31, 2024 are shown by contractual maturity below. The expected maturities will differ from contractual maturities if borrowers have the right to call or pre-pay obligations with or without call or pre-payment penalties. Securities not due at a single maturity date are shown separately.

	Available-for-sale Amortized Cost	Available-for-sale Estimated Fair Value
	(Dollars in thousands)	
Due three months or less	$ 110,872	$ 110,511
Due after three months through one year	100,763	99,531
Due after one through five years	140,602	137,411
Agency mortgage-backed securities	61,916	57,021
Total	$ 414,153	$ 404,474

	Held-to-maturity Amortized Cost (1)	Held-to-maturity Estimated Fair Value
	(Dollars in thousands)	
Due after three months through one year	$ 665	$ 661
Due after one through five years	8,362	8,140
Due after five through ten years	22,776	21,931
Agency mortgage-backed securities	604,458	512,126
Total	$ 636,261	$ 542,858

(1) Gross of the allowance for credit losses of ($12,000) at March 31, 2024.

Securities with amortized cost of $991,078,000 and $1,041,608,000 as of March 31, 2024 and December 31, 2023, respectively, were pledged to secure public deposits and for other purposes as required or permitted by law or contract. The decrease in pledged securities at March 31, 2024 was due to securities maturities.

The table below presents a roll-forward by major security type for the three months ended March 31, 2024 of the allowance for credit losses on debt securities held-to-maturity at period end:

	Municipals
	(Dollars in thousands)
Beginning balance January 1, 2024	$ 12
Provision for credit losses	—
Ending balance March 31, 2024	$ 12

The bond ratings for the Company’s municipal investment securities at March 31, 2024 were consistent with the ratings at December 31, 2023.

5) Loans and Allowance for Credit Losses on Loans

In accordance with Accounting Standards Codification (“ASC”) 326, the Company is required to measure the allowance for credit losses of financial assets with similar risk characteristics on a collective or pooled basis. In considering the segmentation of financial assets measured at amortized cost into pools, the Company considered various risk characteristics in its analysis. Generally, the segmentation utilized represents the level at which the Company develops and documents its systematic methodology to determine the allowance for credit losses for the financial assets held at amortized cost, specifically the Company's loan portfolio and debt securities classified as held-to-maturity.

In accordance with ASC 326, the Company elected to not measure an allowance for credit losses on accrued interest. As such accrued interest is written off in a timely manner when deemed uncollectible. Any such write-off of accrued interest will reverse previously recognized interest income. In addition, the Company elected to not include accrued interest within presentation and disclosures of the carrying amount of financial assets held at amortized cost. This election is applicable to the various disclosures included within the Company's financial statements. Accrued interest related to financial assets held at amortized cost is included within accrued interest receivable and other assets within the Company's Consolidated Statements of Condition and totaled $16,246,000 at March 31, 2024 and $14,959,000 at December 31, 2023.

The loan portfolio is classified into eight segments of loans – commercial, commercial real estate – owner occupied, commercial real estate – non-owner occupied, land and construction, home equity, multifamily, residential mortgages and consumer and other.

The risk characteristics of each loan portfolio segment are as follows:

Commercial

Commercial loans primarily rely on the identified cash flows of the borrower for repayment and secondarily on the underlying collateral provided by the borrower. However, the cash flows of the borrowers may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets such as accounts receivable, inventory or equipment and may incorporate a personal guarantee; however, some loans may be unsecured. Included in commercial loans are $55,698,000 of Bay View Funding factored receivables at March 31, 2024, compared to $ $57,458,000 at December 31, 2023.

Commercial Real Estate (“CRE”)

CRE loans rely primarily on the cash flows of the properties securing the loan and secondarily on the value of the property that is securing the loan. CRE loans comprise two segments differentiated by owner occupied CRE and non-owner occupied CRE. Owner occupied CRE loans are secured by commercial properties that are at least 50% occupied by the borrower or borrower affiliate. Although CRE loans often incorporate a personal guarantee, the commercial property collateral is typically sufficient and reliance on personal guarantees is minimal. Non-owner occupied CRE loans are secured by commercial properties that are less than 50% occupied by the borrower or borrower affiliate. CRE loans may be adversely affected by conditions in the real estate markets or in the general economy.

Land and Construction

Land and construction loans are generally based on estimates of costs and value associated with the complete project. Construction loans usually involve the disbursement of funds with repayment substantially dependent on the success of the completion of the project. Sources of repayment for these loans may be permanent loans from HBC or other lenders, or proceeds from the sales of the completed project. These loans are monitored by on-site inspections and are considered to have higher risk than other real estate loans due to the final repayment dependent on numerous factors including general economic conditions.

Home Equity

Home equity loans are secured by 1-4 family residences that are generally owner occupied. Repayment of these loans depends primarily on the personal income of the borrower and secondarily on the value of the property securing the loan which can be impacted by changes in economic conditions such as the unemployment rate and property values. These loans are generally revolving lines of credit.

Multifamily

Multifamily loans are loans on residential properties with five or more units. These loans rely primarily on the cash flows of the properties securing the loan for repayment and secondarily on the value of the properties securing the loan. The cash flows of these borrowers can fluctuate along with the values of the underlying property depending on general economic conditions.

Residential Mortgages

Residential mortgage loans are secured by 1-4 family residences which are generally owner-occupied. Repayment of these loans depends primarily on the personal income of the borrower and secondarily on the value of the property securing the loan which can be impacted by changes in economic conditions such as the unemployment rate and property values. These are term loans and are acquired.

Consumer and Other

Consumer and other loans are secured by personal property or are unsecured and rely primarily on the income of the borrower for repayment and secondarily on the collateral value for secured loans. Borrower income and collateral values can vary depending on economic conditions.

Loan Distribution

Loans by portfolio segment and the allowance for credit losses on loans were as follows for the periods indicated:

	March 31, 2024	December 31, 2023
	(Dollars in thousands)	
Loans held-for-investment:		
Commercial	$ 452,231	$ 463,778
Real estate:		
CRE - owner occupied	585,031	583,253
CRE - non-owner occupied	1,271,184	1,256,590
Land and construction	129,712	140,513
Home equity	122,794	119,125
Multifamily	269,263	269,734
Residential mortgages	490,035	496,961
Consumer and other	16,439	20,919
Loans	3,336,689	3,350,873
Deferred loan fees, net	(587)	(495)
Loans, net of deferred fees	3,336,102	3,350,378
Allowance for credit losses on loans	(47,888)	(47,958)
Loans, net	$ 3,288,214	$ 3,302,420

The allowance for credit losses on loans was calculated by pooling loans of similar credit risk characteristics and credit monitoring procedures.

Changes in the allowance for credit losses on loans were as follows for the periods indicated:

	Three Months Ended March 31, 2024								
	Commercial	CRE Owner Occupied	CRE Non-owner Occupied	Land & Construction	Home Equity	Multi-Family	Residential Mortgages	Consumer and Other	Total
	(Dollars in thousands)								
Beginning of period balance	$ 5,853	$ 5,121	$ 25,323	$ 2,352	$ 644	$ 5,053	$ 3,425	$ 187	$ 47,958
Charge-offs	(358)	—	—	—	—	—	—	—	(358)
Recoveries	82	4	—	—	18	—	—	—	104
Net (charge-offs) recoveries	(276)	4	—	—	18	—	—	—	(254)
Provision for (recapture of) credit losses on loans	(548)	16	1,086	(470)	91	(744)	774	(21)	184
End of period balance	$ 5,029	$ 5,141	$ 26,409	$ 1,882	$ 753	$ 4,309	$ 4,199	$ 166	$ 47,888

	Three Months Ended March 31, 2023								
	Commercial	CRE Owner Occupied	CRE Non-owner Occupied	Land & Construction	Home Equity	Multi-Family	Residential Mortgages	Consumer and Other	Total
	(Dollars in thousands)								
Beginning of period balance	$ 6,617	$ 5,751	$ 22,135	$ 2,941	$ 666	$ 3,366	$ 5,907	$ 129	$ 47,512
Charge-offs	(134)	—	—	—	(246)	—	—	—	(380)
Recoveries	80	4	—	—	25	—	—	—	109
Net (charge-offs) recoveries	(54)	4	—	—	(221)	—	—	—	(271)
Provision for (recapture of) credit losses on loans	(29)	(302)	542	235	243	1,026	(1,711)	28	32
End of period balance	$ 6,534	$ 5,453	$ 22,677	$ 3,176	$ 688	$ 4,392	$ 4,196	$ 157	$ 47,273

The following tables present the amortized cost basis of nonperforming loans and loans past due over 90 days and still accruing at the periods indicated:

	March 31, 2024			
	Nonaccrual with no Specific Allowance for Credit Losses	Nonaccrual with Specific Allowance for Credit Losses	Loans over 90 Days Past Due and Still Accruing	Total
	(Dollars in thousands)			
Commercial	$ 924	$ 203	$ 1,443	$ 2,570
Real estate:				
CRE - Owner Occupied	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—
Land and construction	4,673	—	—	4,673
Home equity	120	—	—	120
Residential mortgages	—	—	508	508
Total	$ 5,717	$ 203	$ 1,951	$ 7,871

	December 31, 2023			
	Nonaccrual with no Specific Allowance for Credit Losses	Nonaccrual with no Specific Allowance for Credit Losses	Loans over 90 Days Past Due and Still Accruing	Total
	(Dollars in thousands)			
Commercial	$ 946	$ 290	$ 889	$ 2,125
Real estate:				
CRE - Owner Occupied	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—
Land and construction	4,661	—	—	4,661
Home equity	142	—	—	142
Residential mortgages	779	—	—	779
Total	$ 6,528	$ 290	$ 889	$ 7,707

The following tables present the aging of past due loans by class for the periods indicated:

	March 31, 2024					
	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total
	(Dollars in thousands)					
Commercial	$ 3,522	$ 1,180	$ 1,955	$ 6,657	$ 445,574	$ 452,231
Real estate:						
CRE - Owner Occupied	—	—	—	—	585,031	585,031
CRE - Non-Owner Occupied	5,662	—	—	5,662	1,265,522	1,271,184
Land and construction	3,550	—	4,672	8,222	121,490	129,712
Home equity	441	—		441	122,353	122,794
Multifamily	—	—	—	—	269,263	269,263
Residential mortgages	—	—	508	508	489,527	490,035
Consumer and other	—	—	—	—	16,439	16,439
Total	$ 13,175	$ 1,180	$ 7,135	$ 21,490	$ 3,315,199	$ 3,336,689

	December 31, 2023					
	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total
	(Dollars in thousands)					
Commercial	$ 6,688	$ 2,030	$ 1,264	$ 9,982	$ 453,796	$ 463,778
Real estate:						
CRE - Owner Occupied	—	—	—	—	583,253	583,253
CRE - Non-Owner Occupied	1,289	—	—	1,289	1,255,301	1,256,590
Land and construction	955	—	3,706	4,661	135,852	140,513
Home equity	—	—	142	142	118,983	119,125
Multifamily	—	—	—	—	269,734	269,734
Residential mortgages	3,794	510	779	5,083	491,878	496,961
Consumer and other	—	—	—	—	20,919	20,919
Total	$ 12,726	$ 2,540	$ 5,891	$ 21,157	$ 3,329,716	$ 3,350,873

The following table presents the past due loans on nonaccrual and current loans on nonaccrual for the periods indicated:

	March 31, 2024	December 31, 2023
	(Dollars in thousands)	
Past due nonaccrual loans	$ 5,184	$ 6,100
Current nonaccrual loans	736	718
Total nonaccrual loans	$ 5,920	$ 6,818

Management's classification of a loan as "nonaccrual" is an indication that there is reasonable doubt as to the full recovery of principal or interest on the loan. At that point, the Company stops accruing interest income, and reverses any uncollected interest that had been accrued as income. The Company resumes recognizing interest income only as cash interest payments are received and it has been determined the collection of all outstanding principal is not in doubt.

Credit Quality Indicators

Concentrations of credit risk arise when a number of customers are engaged in similar business activities, or activities in the same geographic region, or have similar features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic conditions. The Company's loan portfolio is concentrated in commercial (primarily manufacturing, wholesale, and service) and real estate lending, with the remaining balance in consumer loans. While no specific industry concentration is considered significant, the Company's lending operations are located in the Company's market areas that are dependent on the technology and real estate industries and their supporting companies. Thus, the Company's borrowers and their guarantors could be adversely impacted by a downturn in these sectors of the economy which could reduce the demand for loans and adversely impact the borrowers' ability to repay their loans.

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, and other factors. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis is performed on a quarterly basis. Nonclassified loans generally include those loans that are expected to be repaid in accordance with their contractual loan terms. Loans categorized as special mention have potential weaknesses that may, if not checked or corrected, weaken the credit or inadequately protect the Company's position at some future date. These loans pose elevated risk, but their weaknesses do not yet justify a substandard classification. Classified loans are those loans that are assigned a substandard, substandard-nonaccrual, or doubtful risk rating using the following definitions:

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

Substandard. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that will jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Substandard-Nonaccrual. Loans classified as substandard-nonaccrual are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any, and it is probable that the Company will not receive payment of the full contractual principal and interest. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected. In addition, the Company no longer accrues interest on the loan because of the underlying weaknesses.

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

Loss. Loans classified as loss are considered uncollectable or of so little value that their continuance as assets is not warranted. This classification does not necessarily mean that a loan has no recovery or salvage value; but rather, there is much doubt about whether, how much, or when the recovery would occur. Loans classified as loss are immediately charged off against the allowance for credit losses on loans. Therefore, there is no balance to report as of March 31, 2024 and December 31, 2023.

Loans may be reviewed at any time throughout a loan’s duration. If new information is provided, a new risk assessment may be performed if warranted.

The following tables present term loans amortized cost by vintage and loan grade classification, and revolving loans amortized cost by loan grade classification at March 31, 2024 and December 31, 2023. The loan grade classifications are based on the Bank’s internal loan grading methodology. Loan grade categories for doubtful and loss rated loans are not included on the tables below as there are no loans with those grades at March 31, 2024 and December 31, 2023. The vintage year represents the period the loan was originated or in the case of renewed loans, the period last renewed. The amortized balance is the loan balance less any purchase discounts, plus any loan purchase premiums. The loan categories are based on the loan segmentation in the Company's CECL reserve methodology based on loan purpose and type.

	Term Loans Amortized Cost Basis by Originated Period as of March 31, 2024						Revolving Loans Amortized Cost Basis	
	3/31/2024	2023	2022	2021	2020	Prior Periods	Cost Basis	Total
					(Dollars in thousands)			
Commercial:								
Pass	$ 74,006	$ 36,626	$ 23,777	$ 18,808	$ 13,368	$ 30,291	$ 239,157	$ 436,033
Special Mention	2,020	82	1,062	38	—	3,272	2,471	8,945
Substandard	4	—	1,478	—	97	4,490	57	6,126
Substandard-Nonaccrual	—	—	—	343	—	784	—	1,127
Total	76,030	36,708	26,317	19,189	13,465	38,837	241,685	452,231
CRE - Owner Occupied:								
Pass	12,117	32,194	84,349	109,741	64,592	262,613	10,107	575,713
Special Mention	—	—	249	3,219	457	1,251	—	5,176
Substandard	—	—	—	—	3,042	1,100	—	4,142
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	12,117	32,194	84,598	112,960	68,091	264,964	10,107	585,031
CRE - Non-Owner Occupied:								
Pass	21,427	226,112	240,250	260,618	27,717	465,826	5,116	1,247,066
Special Mention	—	—	—	708	—	10,958	—	11,666
Substandard	—	—	—	4,564	—	7,562	326	12,452
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	21,427	226,112	240,250	265,890	27,717	484,346	5,442	1,271,184
Land and construction:								
Pass	9,596	38,701	39,325	23,083	9,246	1,844	—	121,795
Special Mention	—	—	—	—	—	2,163	—	2,163
Substandard	—	—	—	—	—	1,081	—	1,081
Substandard-Nonaccrual	—	—	—	3,706	967	—	—	4,673
Total	9,596	38,701	39,325	26,789	10,213	5,088	—	129,712
Home equity:								
Pass	—	—	—	—	—	2,055	114,967	117,022
Special Mention	—	—	—	—	—	—	2,256	2,256
Substandard	—	—	—	—	—	—	3,396	3,396
Substandard-Nonaccrual	—	—	—	—	—	120	—	120
Total	—	—	—	—	—	2,175	120,619	122,794
Multifamily:								
Pass	4,523	47,031	40,893	54,977	5,358	116,026	455	269,263
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	4,523	47,031	40,893	54,977	5,358	116,026	455	269,263
Residential mortgage:								
Pass	—	1,678	178,340	271,180	1,030	34,206	—	486,434
Special Mention	—	—	1,326	—	—	—	—	1,326
Substandard	—	—	764	—	—	1,511	—	2,275
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	—	1,678	180,430	271,180	1,030	35,717	—	490,035
Consumer and other:								
Pass	—	1,566	1,373	58	—	2,060	10,588	15,645
Special Mention	—	705	—	—	—	89	—	794
Substandard	—	—	—	—	—	—	—	—
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	—	2,271	1,373	58	—	2,149	10,588	16,439
Total loans	$ 123,693	$ 384,695	$ 613,186	$ 751,043	$ 125,874	$ 949,302	$ 388,896	$ 3,336,689
Risk Grades:								
Pass	$ 121,669	$ 383,908	$ 608,307	$ 738,465	$ 121,311	$ 914,921	$ 380,390	$ 3,268,971
Special Mention	2,020	787	2,637	3,965	457	17,733	4,727	32,326
Substandard	4	—	2,242	4,564	3,139	15,744	3,779	29,472
Substandard-Nonaccrual	—	—	—	4,049	967	904	—	5,920
Grand Total	$ 123,693	$ 384,695	$ 613,186	$ 751,043	$ 125,874	$ 949,302	$ 388,896	$ 3,336,689

	Term Loans Amortized Cost Basis by Originated Period as of December 31, 2023						Revolving Loans Amortized	
	2023	2022	2021	2020	2019	Prior Periods	Cost Basis	Total
	(Dollars in thousands)							
Commercial:								
Pass	$ 99,387	$ 25,250	$ 19,732	$ 14,929	$ 11,893	$ 22,134	$ 258,461	$ 451,786
Special Mention	2,107	1,092	41	—	133	1,134	467	4,974
Substandard	4	1,516	—	100	185	3,835	142	5,782
Substandard-Nonaccrual	—	—	349	—	116	771	—	1,236
Total	101,498	27,858	20,122	15,029	12,327	27,874	259,070	463,778
CRE - Owner Occupied:								
Pass	32,993	86,688	110,613	68,184	52,885	214,729	10,302	576,394
Special Mention	—	250	3,241	462	—	1,802	—	5,755
Substandard	—	—	—	—	1,100	4	—	1,104
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	32,993	86,938	113,854	68,646	53,985	216,535	10,302	583,253
CRE - Non-Owner Occupied:								
Pass	225,505	243,080	267,870	28,315	92,648	370,552	3,199	1,231,169
Special Mention	—	—	—	—	7,493	10,040	—	17,533
Substandard	—	—	—	—	—	7,614	274	7,888
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	225,505	243,080	267,870	28,315	100,141	388,206	3,473	1,256,590
Land and construction:								
Pass	40,142	52,862	27,419	9,273	1,864	—	—	131,560
Special Mention	2,163	—	—	—	—	—	—	2,163
Substandard	2,129	—	—	—	—	—	—	2,129
Substandard-Nonaccrual	—	—	3,706	955	—	—	—	4,661
Total	44,434	52,862	31,125	10,228	1,864	—	—	140,513
Home equity:								
Pass	—	—	—	—	—	1,463	111,250	112,713
Special Mention	—	—	—	—	—	—	2,110	2,110
Substandard	—	—	—	—	—	—	4,160	4,160
Substandard-Nonaccrual	—	—	—	—	—	—	142	142
Total	—	—	—	—	—	1,463	117,662	119,125
Multifamily:								
Pass	47,089	41,112	55,557	5,394	42,129	75,890	355	267,526
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	2,208	—	2,208
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	47,089	41,112	55,557	5,394	42,129	78,098	355	269,734
Residential mortgage:								
Pass	1,684	187,417	268,617	1,037	6,861	28,892	—	494,508
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	973	—	—	—	701	—	1,674
Substandard-Nonaccrual	—	779	—	—	—	—	—	779
Total	1,684	189,169	268,617	1,037	6,861	29,593	—	496,961
Consumer and other:								
Pass	2,332	1,376	3	—	—	2,089	14,961	20,761
Special Mention	—	—	62	—	—	96	—	158
Substandard	—	—	—	—	—	—	—	—
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	2,332	1,376	65	—	—	2,185	14,961	20,919
Total loans	$ 455,535	$ 642,395	$ 757,210	$ 128,649	$ 217,307	$ 743,954	$ 405,823	$ 3,350,873
Risk Grades:								
Pass	$ 449,132	$ 637,785	$ 749,811	$ 127,132	$ 208,280	$ 715,749	$ 398,528	$ 3,286,417
Special Mention	4,270	1,342	3,344	462	7,626	13,072	2,577	32,693
Substandard	2,133	2,489	—	100	1,285	14,362	4,576	24,945
Substandard-Nonaccrual	—	779	4,055	955	116	771	142	6,818
Grand Total	$ 455,535	$ 642,395	$ 757,210	$ 128,649	$ 217,307	$ 743,954	$ 405,823	$ 3,350,873

The following tables present the gross charge-offs by class of loans and year of origination for the periods indicated:

	Gross Charge-offs by Originated Period for the Three Months Ended March 31, 2024							
	3/31/2024	2023	2022	2021	2020	Prior Periods	Revolving Loans	Total
	(Dollars in thousands)							
Commercial	$ —	$ —	$ —	$ —	$ —	$ 358	$ —	$ 358
Real estate:								
CRE - Owner Occupied	—	—	—	—	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—	—	—	—	—
Land and construction	—	—	—	—	—	—	—	—
Home equity	—	—	—	—	—	—	—	—
Multifamily	—	—	—	—	—	—	—	—
Residential mortgages	—	—	—	—	—	—	—	—
Consumer and other	—	—	—	—	—	—	—	—
Total	$ —	$ —	$ —	$ —	$ —	$ 358	$ —	$ 358

	Gross Charge-offs by Originated Period for the Three Months Ended March 31, 2023							
	03/31/2023	2022	2021	2020	2019	Prior Periods	Revolving Loans	Total
	(Dollars in thousands)							
Commercial	$ —	$ —	$ —	$ —	$ 49	$ 85	$ —	$ 134
Real estate:								
CRE - Owner Occupied	—	—	—	—	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—	—	—	—	—
Land and construction	—	—	—	—	—	—	—	—
Home equity	—	—	—	—	—	—	246	246
Multifamily	—	—	—	—	—	—	—	—
Residential mortgages	—	—	—	—	—	—	—	—
Consumer and other	—	—	—	—	—	—	—	—
Total	$ —	$ —	$ —	$ —	$ 49	$ 85	$ 246	$ 380

The amortized cost basis of collateral-dependent loans at March 31, 2024 and December 31, 2023 was $ 203,000 and $290,000, respectively, and were secured by business assets.

When management determines that foreclosures are probable, expected credit losses for collateral-dependent loans are based on the fair value of the collateral at the reporting date, adjusted for selling costs as appropriate. For loans which foreclosure is not probable, but for which repayment is expected to be provided substantially through the operation or sale of the collateral and the borrower is experiencing financial difficulty, management has elected the practical expedient under ASC 326 to estimate expected credit losses based on the fair value of collateral, adjusted for selling costs as appropriate. The class of loan represents the primary collateral type associated with the loan. Significant quarter over quarter changes are reflective of changes in nonaccrual status and not necessarily associated with credit quality indicators like appraisal value.

Loan Modifications

Occasionally, the Company modifies loans to borrowers experiencing financial difficulty by providing principal forgiveness, term extension, payment delay, or interest reduction. When principal forgiveness is provided, the amount of forgiveness is charged-off against the allowance for credit losses.

In some cases, the Company provides multiple types of concessions on one loan. Typically, one type of concession, such as a term extension, is granted initially. If the borrower continues to experience financial difficulty, another concession, such as principal forgiveness, may be granted. For the loans included in the “combination” columns below, multiple types of modifications have been made on the same loan within the current reporting period. The combination is at least two of the following: a term extension, principal forgiveness, payment delay, and/or interest rate reduction.

The following tables present the amortized cost basis of loans that were both experiencing financial difficulty and modified through the periods indicated, by segment and type of modification. The percentage of the amortized cost basis of the loans that were modified to borrowers experiencing financial difficulty as compared to the amortized cost basis of each class of financing receivable is also presented below.

	Three Months Ended March 31, 2024						
	Principal Forgiveness	Payment Delay	Term Extension	Interest Rate Reduction	Combination Term Extension and Principal Forgiveness	Combination Term Extension and Interest Rate Reduction	Total Class of Financing Receivables
	(Dollars in thousands)						
Commercial	$ —	$ —	$ 33	$ —	$ —	$ —	0.01 %
Total	$ —	$ —	$ 33	$ —	$ —	$ —	0.01 %

	Three Months Ended March 31, 2023						
	Principal Forgiveness	Payment Delay	Term Extension	Interest Rate Reduction	Combination Term Extension and Principal Forgiveness	Combination Term Extension and Interest Rate Reduction	Total Class of Financing Receivables
	(Dollars in thousands)						
Commercial	$ 6	$ 88	$ 36	$ —	$ —	$ —	0.03 %
Total	$ 6	$ 88	$ 36	$ —	$ —	$ —	0.03 %

The Company has committed to lend no additional amounts to the borrowers included in the previous tables.

The Company closely monitors the performance of the loans that are modified to borrowers experiencing financial difficulty to understand the effectiveness of its modification efforts. The following tables present the performance of such loans that have been modified for the periods indicated.

	Three Months Ended March 31, 2024			
	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or Greater Past Due	Total Past Due
	(Dollars in thousands)			
Commercial	$ —	$ —	$ —	$ —
Total	$ —	$ —	$ —	$ —

	Three Months Ended March 31, 2023			
	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or Greater Past Due	Total Past Due
	(Dollars in thousands)			
Commercial	$ —	$ 36	$ 6	$ 42
Total	$ —	$ 36	$ 6	$ 42

The following tables present the financial effect of the loan modification presented above to borrowers experiencing financial difficulty for the periods indicated:

	Three Months Ended March 31, 2024		
	Principal Forgiveness	Weighted Average Interest Rate Reduction	Weighted Average Term Extension (Months)
	(Dollars in thousands)		
Commercial	$ —	— %	10
Total	$ —	— %	10

	Three Months Ended March 31, 2023		
	Principal Forgiveness	Weighted Average Interest Rate Reduction	Weighted Average Term Extension (Months)
	(Dollars in thousands)		
Commercial	$ 3	— %	9
Total	$ 3	— %	9

There were no payment defaults for loans modified for the three months ended March 31, 2024 and March 31, 2023.

6) Goodwill and Other Intangible Assets

Goodwill

At March 31, 2024, the carrying value of goodwill was $ 167,631,000, which included $13,044,000 of goodwill related to the acquisition of Bay View Funding, $32,619,000 from the acquisition of Focus Business Bank, $ 13,819,000 from the acquisition of Tri-Valley Bank, $24,271,000 from the acquisition of United American Bank and $ 83,878,000 from its acquisition of Presidio Bank.

ASC 350-20 outlines the methodology used to determine if goodwill has been impaired and to measure any loss resulting from an impairment. Goodwill impairment exists when a reporting unit’s carrying value exceeds its fair value, which is determined through a qualitative assessment whether it is more likely than not that the fair value of equity of the reporting unit exceeds the carrying value. If the qualitative assessment indicates it is more likely than not that the fair value of equity of a reporting unit is less than book value, then a quantitative impairment test is required. The quantitative assessment identifies if a reporting unit’s fair value is less than its carrying value. If it is, then the Company will recognize goodwill impairment equal to the difference between the carrying amount of the reporting unit and its fair value, not to exceed the carrying amount of goodwill.

The Company's policy is to test goodwill for impairment annually as of November 30, or on an interim basis if an event triggering impairment assessment may have occurred. The Company completed its annual goodwill impairment analysis as of November 30, 2023 with the assistance of an independent valuation firm. The goodwill related to the acquisition of Bay View Funding was tested separately for impairment under this analysis. The qualitative assessment indicated that it was more likely than not that the fair value of the reporting units exceeded the carry value. No events or circumstances since the November 30, 2023 annual impairment test were noted that would indicate it was more likely than not a goodwill impairment exists.

The following table summarizes the carrying amount of goodwill by segment for the periods indicated:

	March 31, 2024	December 31, 2023
	(Dollars in thousands)	
Banking	$ 154,587	$ 154,587
Factoring	13,044	13,044
Total Goodwill	$ 167,631	$ 167,631

Other Intangible Assets

The Company's intangible assets are summarized as follows for the periods indicated:

	March 31, 2024		
	Gross Carrying Amount	Accumulated Amortization	Total
	(Dollars in thousands)		
Core deposit intangibles	$ 25,023	(17,152)	$ 7,871
Customer relationship and brokered relationship intangibles	1,900	(1,788)	112
Below market leases	110	(19)	91
Total	$ 27,033	$ (18,959)	$ 8,074

	December 31, 2023		
	Gross Carrying Amount	Accumulated Amortization	Total
	(Dollars in thousands)		
Core deposit intangibles	$ 25,023	(16,646)	$ 8,377
Customer relationship and brokered relationship intangibles	1,900	(1,741)	159
Below market leases	110	(19)	91
Total	$ 27,033	$ (18,406)	$ 8,627

As of March 31, 2024, the estimated amortization expense for future periods is as follows:

Year	Core Deposit Intangible	Customer & Brokered Relationship Intangible	Below/ (Above) Market Lease	Total Amortization Expense
	(Dollars in thousands)			
2024 remaining	$ 1,517	$ 112	$ 5	$ 1,634
2025	1,795	—	18	1,813
2026	1,512	—	18	1,530
2027	1,438	—	18	1,456
2028	999	—	18	1,017
2029	610	—	14	624
	$ 7,871	$ 112	$ 91	$ 8,074

Impairment testing of the intangible assets is performed at the individual asset level. Impairment exists if the carrying amount of the asset is not recoverable and exceeds its fair value at the date of the impairment test. For intangible assets, estimates of expected future cash flows (cash inflows less cash outflows) that are directly associated with an intangible asset are used to determine the fair value of that asset. Management makes certain estimates and assumptions in determining the expected future cash flows from core deposit and customer relationship intangibles including account attrition, expected lives, discount rates, interest rates, servicing costs and other factors. Significant changes in these estimates and assumptions could adversely impact the valuation of these intangible assets. If an impairment loss exists, the carrying amount of the intangible asset is adjusted to a new cost basis. The new cost basis is then amortized over the remaining useful life of the asset. Based on its assessment, management concluded that there was no impairment of intangible assets at March 31, 2024 and December 31, 2023.

7) Income Taxes

Some items of income and expense are recognized in one year for tax purposes, and another when applying generally accepted accounting principles, which leads to timing differences between the Company's actual current tax liability and the amount accrued for this liability based on book income. These temporary differences comprise the "deferred" portion of the Company's tax expense or benefit, which is accumulated on the Company's books as a deferred tax asset or deferred tax liability until such time as they reverse.

Under generally accepted accounting principles, a valuation allowance is required if it is "more likely than not" that a deferred tax asset will not be realized. The determination of the realizability of the deferred tax assets is highly subjective and dependent upon judgment concerning management's evaluation of both positive and negative evidence, including forecasts of future income, cumulative losses, applicable tax planning strategies, and assessments of current and future economic and business conditions.

The Company had net deferred tax assets of $ 27,513,000 and $29,765,000, at March 31, 2024 and December 31, 2023, respectively. After consideration of the matters in the preceding paragraph, the Company determined that it is more likely than not that the net deferred tax assets at March 31, 2024 and December 31, 2023 will be fully realized in future years.

The following table reflects the carrying amounts of the low income housing investments included in accrued interest receivable and other assets, and the future commitments included in accrued interest payable and other liabilities for the periods indicated:

	March 31, 2024	December 31, 2023
	(Dollars in thousands)	
Low income housing investments	$ 2,615	$ 2,794
Future commitments	$ 494	$ 494

The Company expects $14,000 of the future commitments to be paid in 2024, and $ 480,000 in 2025 through 2027.

For tax purposes, the Company had low income housing tax credits of $ 141,000 and $180,000 for the three months ended March 31, 2024 and 2023, respectively, and low income housing investment expense of $148,000 and $186,000, respectively. The Company recognized low income housing investment expense as a component of income tax expense.

8) Benefit Plans

Supplemental Retirement Plan

The Company has a supplemental retirement plan (the "Plan") covering some current and some former key employees and directors. The Plan is a nonqualified defined benefit plan. Benefits are unsecured as there are no Plan assets. The following table presents the amount of periodic cost recognized for the periods indicated:

	Three Months Ended March 31,	
	2024	2023
	(Dollars in thousands)	
Components of net periodic benefit cost:		
Service cost	$ 50	$ 48
Interest cost	318	324
Amortization of net actuarial loss	27	13
Net periodic benefit cost	$ 395	$ 385
Amount recognized in other comprehensive income	$ 18	$ 8

The components of net periodic benefit cost other than the service cost component are included in the line item "other noninterest expense" in the Consolidated Statements of Income.

Split-Dollar Life Insurance Benefit Plan

The Company maintains life insurance policies for some current and former directors and officers that are subject to split-dollar life insurance agreements. The following table sets forth the funded status of the split-dollar life insurance benefits for the periods indicated:

	March 31, 2024	December 31, 2023
	(Dollars in thousands)	
Change in projected benefit obligation:		
Projected benefit obligation at beginning of year	$ 6,951	$ 7,060
Interest cost	86	365
Actuarial loss	—	(474)
Projected benefit obligation at end of period	$ 7,037	$ 6,951

	March 31, 2024	December 31, 2023
	(Dollars in thousands)	
Net actuarial loss	$ 2,183	$ 2,108
Prior transition obligation	678	701
Accumulated other comprehensive loss	$ 2,861	$ 2,809

	Three Months Ended March 31, 2024	Three Months Ended March 31, 2023
	(Dollars in thousands)	
Amortization of prior transition obligation and actuarial losses	$ (52)	$ (47)
Interest cost	86	91
Net periodic benefit cost	$ 34	$ 44
Amount recognized in other comprehensive income	$ (52)	$ (48)

9) Fair Value

Accounting guidance establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

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

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical assets or liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data (for example, interest rates and yield curves observable at commonly quoted intervals, prepayment speeds, credit risks, and default rates).

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

Financial Assets and Liabilities Measured on a Recurring Basis

The fair values of securities available-for-sale are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs).

The fair value of interest-only ("I/O") strip receivable assets is based on a valuation model used by a third party. The Company is able to compare the valuation model inputs and results to widely available published industry data for reasonableness (Level 2 inputs).

		Fair Value Measurements Using		
	Balance	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(Dollars in thousands)		
Assets at March 31, 2024				
Available-for-sale securities:				
U.S. Treasury	$ 347,453	$ 347,453	$ —	$ —
Agency mortgage-backed securities	57,021	—	57,021	—
I/O strip receivables	110	—	110	—
Assets at December 31, 2023				
Available-for-sale securities:				
U.S. Treasury	$ 382,369	$ 382,369	$ —	$ —
Agency mortgage-backed securities	60,267	—	60,267	—
I/O strip receivables	117	—	117	—

There were no transfers between Level 1 and Level 2 during the period for assets measured at fair value on a recurring basis.

Assets and Liabilities Measured on a Non-Recurring Basis

The fair value of collateral dependent loans individually evaluated with specific allocations of the allowance for credit losses on loans is generally based on recent real estate appraisals. The 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 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. There were no material collateral dependent loans carried at fair value on a non-recurring basis at March 31, 2024 or December 31, 2023.

Foreclosed assets are valued at the time the loan is foreclosed upon and the asset is transferred to foreclosed assets. The fair value is based primarily on third party appraisals, less costs to sell. The appraisals may utilize a single valuation approach or a combination of approaches including the comparable sales and income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a Level 3 classification of the inputs for determining fair value. At March 31, 2024 and December 31, 2023, there were no foreclosed assets on the balance sheet.

The carrying amounts and estimated fair values of financial instruments at March 31, 2024 are as follows:

	Carrying Amounts	Estimated Fair Value: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(Dollars in thousands)				
Assets:					
Cash and cash equivalents	$ 541,359	$ 541,359	$ —	$ —	$ 541,359
Securities available-for-sale	404,474	347,453	57,021	—	404,474
Securities held-to-maturity	636,249	—	542,858	—	542,858
Loans (including loans held-for-sale)	3,338,048 (1)	—	1,946	3,142,873	3,144,819
FHLB stock, FRB stock, and other investments	32,544	—	—	—	N/A
Accrued interest receivable	16,246	1,592	2,482	12,172	16,246
I/O strips receivables	110	—	110	—	110
Liabilities:					
Time deposits	$ 488,112	$ —	$ 491,943	$ —	$ 491,943
Other deposits	3,956,548	—	3,956,548	—	3,956,548
Subordinated debt	39,539	—	32,339	—	32,339
Accrued interest payable	5,296	—	5,296	—	5,296

(1) Before allowance for credit losses on loans of $ 47,888,000.

The carrying amounts and estimated fair values of the Company's financial instruments at December 31, 2023:

	Carrying Amounts	Estimated Fair Value: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(Dollars in thousands)				
Assets:					
Cash and cash equivalents	$ 408,129	$ 408,129	$ —	$ —	$ 408,129
Securities available-for-sale	442,636	382,369	60,267	—	442,636
Securities held-to-maturity	650,565	—	564,127	—	564,127
Loans (including loans held-for-sale)	3,352,583 (1)	—	2,205	3,172,512	3,174,717
FHLB stock, FRB stock, and other investments	32,540	—	—	—	N/A
Accrued interest receivable	14,959	1,255	1,764	11,940	14,959
I/O strips receivables	117	—	117	—	117
Liabilities:					
Time deposits	$ 469,472	$ —	$ 471,693	$ —	$ 471,693
Other deposits	3,908,986	—	3,908,986	—	3,908,986
Subordinated debt	39,502	—	31,902	—	31,902
Accrued interest payable	4,688	—	4,698	—	4,698

(1) Before allowance for credit losses on loans of $ 47,958,000.

10) Equity Plan

The Company maintained an Amended and Restated 2004 Equity Plan (the “2004 Plan”) for directors, officers, and key employees. The 2004 Plan was terminated on May 23, 2013. On May 23, 2013, the Company’s shareholders approved the 2013 Equity Incentive Plan (the “2013 Plan”). On May 21, 2020, the shareholders approved an amendment to the 2013 Plan to increase the number of shares available from 3,000,000 to 5,000,000 shares. The 2013 Plan was terminated on May 25, 2023. The shareholders approved the 2023 Equity Incentive Plan (the “2023 Plan”) on May 25, 2023, which reserved for issuance 600,000 shares, plus the number of shares available for issuance under the 2013 Plan that had not been made subject to outstanding awards as of the effective date of the 2023 Plan. These plans are collectively referred to as “Equity Plans.” The Equity Plans provide for the grant of incentive and nonqualified stock options, restricted stock, restricted stock units (“RSUs”) and performance-based restricted stock units (“PRSUs”). The Equity Plans provide that the option price for both incentive and nonqualified stock options will be determined by the Board of Directors at no less than the fair value at the date of grant. Options granted vest on a schedule determined by the Board of Directors at the time of grant. Generally, options vest over four years. All options expire no later than ten years from the date of grant. There were 946,954 shares available for the issuance of equity awards under the 2023 Plan as of March 31, 2024.

Each RSU will vest ratably over three years. For the three months ended March 31, 2024, the Company granted 239,531 of RSUs.

The Company’s Executive Officer Cash Incentive Plan is comprised of formula-based financial measure. The executive officers that participate in the plan have 50% of their award value are PRSUs contingent on relative return on average tangible common equity (“ROATCE”) performance compared to a peer group at the end of a three year performance period. PRSUs are subject to cliff vesting after a three year performance period commencing in the initial year of grant. The earned PRSUs, if any, shall vest on the date on which the Board of Directors certifies whether and to what extent the performance goal has been achieved following the end of the performance period. For the three months ended March 31, 2024, the Company granted 149,923 shares of PRSUs.

Restricted stock is subject to time vesting. Restricted stock granted to the Board of Directors vest in one year. For the three months ended March 31, 2024, the Company granted 57,123 shares of restricted stock.

Stock option activity under the Equity Plans is as follows:

Total Stock Options	**Number of Shares**	**Weighted Average Exercise Price**	**Weighted Average Remaining Contractual Life (Years)**	**Aggregate Intrinsic Value**
Outstanding at January 1, 2024	2,637,356	$ 10.40		
Exercised	(72,882)	$ 5.29		
Forfeited or expired	(112,482)	$ 9.85		
Outstanding at March 31, 2024	2,451,992	$ 10.58	5.61	$ 1,086,661
Vested or expected to vest	2,304,872		5.61	$ 1,021,461
Exercisable at March 31, 2024	1,869,398		4.71	$ 748,468

Information related to the Equity Plans for the periods indicated:

	March 31,	
	2024	**2023**
Intrinsic value of options exercised	$ 268,715	$ 466,308
Cash received from option exercise	$ 385,219	$ 682,825
Tax (expense) benefit realized from option exercises	$ (22,452)	$ 3,968

As of March 31, 2024, there was $ 1,014,000 of total unrecognized compensation cost related to unvested stock options granted under the Equity Plans. That cost is expected to be recognized over a weighted-average period of approximately 2.48 years.

Restricted stock activity under the Equity Plans is as follows:

Total Restricted Stock Award	Number of Shares	Weighted Average Grant Date Fair Value
Nonvested shares at January 1, 2024	185,413	$ 10.87
Granted	57,123	$ 8.49
Forfeited or expired	(23,215)	$ 11.36
Nonvested shares at March 31, 2024	219,321	$ 9.34

As of March 31, 2024, there was $1,056,000 of total unrecognized compensation cost related to unvested restricted stock awards granted under the Equity Plans. The cost is expected to be recognized over a weighted-average period of approximately 1.09 years.

RSU activity under the Equity Plans is as follows:

Total RSUs	Number of Shares	Weighted Average Grant Date Fair Value
Nonvested shares at January 1, 2024	119,362	$ 7.41
Granted	239,531	$ 8.49
Forfeited or expired	(18,355)	$ 7.41
Nonvested shares at March 31, 2024	340,538	$ 8.17

As of March 31, 2024, there were $2,508,000 of total unrecognized compensation cost related to unvested RSUs granted under the Equity Plans. The cost is expected to be recognized over a weighted average period of 2.69 years.

PRSU activity under the Equity Plans is as follows:

Total PRSUs	Number of Shares	Weighted Average Grant Date Fair Value
Nonvested shares at January 1, 2024	119,358	$ 7.41
Granted	149,923	$ 8.49
Forfeited or expired	(18,355)	$ 7.41
Nonvested shares at March 31, 2024	250,926	$ 8.06

As of March 31, 2024, there were $1,764,000 of total unrecognized compensation cost related to unvested PRSUs granted under the Equity Plans. The cost is expected to be recognized over a weighted average period of 2.60 years.

11) Borrowing Arrangements

Federal Home Loan Bank Borrowings, Federal Reserve Bank Borrowings, and Available Lines of Credit

HBC has off-balance sheet liquidity in the form of federal funds purchase arrangements with correspondent banks, and lines of credit from the FHLB and FRB. HBC maintains a collateralized line of credit with the FHLB of San Francisco. Under this line, the Company can borrow from the FHLB on a short-term (typically overnight) or long-term (over one year) basis. HBC can also borrow from the FRB discount window. The following table shows the collateral value of loans and securities pledged for the lines of credit (if collateralized), total available lines of credit, the amounts outstanding, and the remaining available for the periods indicated:

	March 31, 2024			
	Collateral Value	Total Available	Outstanding	Remaining Available
	(Dollars in thousands)			
FHLB collateralized borrowing capacity	$ 1,569,070	$ 1,097,518	$ —	$ 1,097,518
FRB discount window collateralized line of credit	1,639,038	1,245,362	—	1,245,362
Federal funds purchase arrangements	N/A	90,000	—	90,000
Holding company line of credit	N/A	20,000	—	20,000
	$ 3,208,108	$ 2,452,880	$ —	$ 2,452,880

	December 31, 2023			
	Collateral Value	Total Available	Outstanding	Remaining Available
	(Dollars in thousands)			
FHLB collateralized borrowing capacity	$ 1,600,371	$ 1,100,931	$ —	$ 1,100,931
FRB discount window collateralized line of credit	1,658,642	1,235,573	—	1,235,573
Federal funds purchase arrangements	N/A	90,000	—	90,000
Holding company line of credit	N/A	20,000	—	20,000
Total	$ 3,259,013	$ 2,446,504	$ —	$ 2,446,504

HBC may also utilize securities sold under repurchase agreements to manage its liquidity position. There were no securities sold under agreements to repurchase at March 31, 2024 and December 31, 2023.

Subordinated Debt

On May 11, 2022, the Company completed a private placement offering of $ 40,000,000 aggregate principal amount of its 5.00% fixed-to-floating rate subordinated notes due May 15, 2032 (“Sub Debt due 2032”). The Company used the net proceeds of the Sub Debt due 2032 for general corporate purposes, including the repayment on June 1, 2022 of the Company’s $40,000,000 aggregate principal amount of 5.25% fixed-to-floating rate subordinated notes due June 1, 2027. The Sub Debt due 2032, net of unamortized issuance costs of $461,000, totaled $39,539,000 at March 31, 2024, and qualifies as Tier 2 capital for the Company under the guidelines established by the Federal Reserve Board.

12) Capital Requirements

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

The Company’s consolidated capital ratios and the HBC’s capital ratios exceeded the regulatory guidelines for a well-capitalized financial institution under the Basel III regulatory requirements at March 31, 2024. There are no conditions or events since March 31, 2024, that management believes have changed the categorization of the Company or HBC as "well-capitalized."

Quantitative measures established by regulation to help ensure capital adequacy require the Company and HBC to maintain minimum amounts and ratios (set forth in the tables below) of total, Tier 1 capital, and common equity Tier 1 capital (as defined in the regulations) to risk weighted assets (as defined), and of Tier 1 capital to average assets (as defined). Management believes that, as of March 31, 2024 and December 31, 2023, the Company and HBC met all capital adequacy guidelines to which they were subject.

The Company's consolidated capital amounts and ratios are presented in the following table, together with capital adequacy requirements, under the Basel III regulatory requirements for the periods indicated:

	Actual		Required For Capital Adequacy Purposes Under Basel III	
	Amount	Ratio	Amount	Ratio [1]
	(Dollars in thousands)			
As of March 31, 2024				
Total Capital (to risk-weighted assets)	$ 598,795	15.6 %	$ 402,267	10.5 %
Tier 1 Capital (to risk-weighted assets)	$ 513,473	13.4 %	$ 325,644	8.5 %
Common Equity Tier 1 Capital (to risk-weighted assets)	$ 513,473	13.4 %	$ 268,178	7.0 %
Tier 1 Capital (to average assets)	$ 513,473	10.2 %	$ 200,413	4.0 %

(1) Includes 2.5% capital conservation buffer, except the Tier 1 Capital to average assets ratio.

	Actual		Required For Capital Adequacy Purposes Under Basel III	
	Amount	Ratio	Amount	Ratio [1]
	(Dollars in thousands)			
As of December 31, 2023				
Total Capital (to risk-weighted assets)	$ 594,371	15.5 %	$ 403,060	10.5 %
Tier 1 Capital (to risk-weighted assets)	$ 511,799	13.3 %	$ 326,287	8.5 %
Common Equity Tier 1 Capital (to risk-weighted assets)	$ 511,799	13.3 %	$ 268,707	7.0 %
Tier 1 Capital (to average assets)	$ 511,799	10.0 %	$ 204,024	4.0 %

(1) Includes 2.5% capital conservation buffer, except the Tier 1 Capital to average assets ratio.

HBC's actual capital amounts and ratios are presented in the following table, together with capital adequacy requirements, under the Basel III regulatory requirements for the periods indicated:

	Actual		To Be Well-Capitalized Under PCA Regulatory Guidelines		Required For Capital Adequacy Purposes Under Basel III	
	Amount	Ratio	Amount	Ratio	Amount	Ratio [1]
	(Dollars in thousands)					
As of March 31, 2024						
Total Capital (to risk-weighted assets)	$ 577,519	15.1 %	$ 382,910	10.0 %	$ 402,055	10.5 %
Tier 1 Capital (to risk-weighted assets)	$ 531,736	13.9 %	$ 306,328	8.0 %	$ 325,473	8.5 %
Common Equity Tier 1 Capital (to risk-weighted assets)	$ 531,736	13.9 %	$ 248,891	6.5 %	$ 268,037	7.0 %
Tier 1 Capital (to average assets)	$ 531,736	10.6 %	$ 250,346	5.0 %	$ 200,277	4.0 %

(1) Includes 2.5% capital conservation buffer, except the Tier 1 Capital to average assets ratio.

	Actual		To Be Well-Capitalized Under Basel III PCA Regulatory Requirements		Required For Capital Adequacy Purposes Under Basel III	
	Amount	Ratio	Amount	Ratio	Amount	Ratio [1]
	(Dollars in thousands)					
As of December 31, 2023						
Total Capital (to risk-weighted assets)	$ 572,907	14.9 %	$ 383,542	10.0 %	$ 402,719	10.5 %
Tier 1 Capital (to risk-weighted assets)	$ 529,836	13.8 %	$ 306,834	8.0 %	$ 326,011	8.5 %
Common Equity Tier 1 Capital (to risk-weighted assets)	$ 529,836	13.8 %	$ 249,302	6.5 %	$ 268,479	7.0 %
Tier 1 Capital (to average assets)	$ 529,836	10.4 %	$ 254,869	5.0 %	$ 203,895	4.0 %

(1) Includes 2.5% capital conservation buffer, except the Tier 1 Capital to average assets ratio.

The Subordinated Debt, net of unamortized issuance costs, totaled $ 39,539,000 at March 31, 2024, and qualifies as Tier 2 capital for the Company under the guidelines established by the Federal Reserve Board.

Under California General Corporation Law, the holders of common stock are entitled to receive dividends when and as declared by the Board of Directors, out of funds legally available. The California Financial Code provides that a state licensed bank may not make a cash distribution to its shareholders in excess of the lesser of the following: (i) the bank's retained earnings; or (ii) the bank's net income for its last three fiscal years, less the amount of any distributions made by the bank to its shareholders during such period. However, a bank, with the prior approval of the Commissioner of the California Department of Financial Protection and Innovation ("DFPI") may make a distribution to its shareholders of an amount not to exceed the greater of (i) a bank's retained earnings; (ii) its net income for its last fiscal year; or (iii) its net income for the current fiscal year. Also with the prior approval of the Commissioner of the DFPI and the shareholders of the bank, the bank may make a distribution to its shareholders, as a reduction in capital of the bank. In the event that the Commissioner determines that the shareholders' equity of a bank is inadequate or that the making of a distribution by a bank would be unsafe or unsound, the Commissioner may order a bank to refrain from making such a proposed distribution. As of March 31, 2024, HBC would not be required to obtain regulatory approval, and the amount available for cash dividends is $87,477,000. HBC distributed to HCC dividends of $8,000,000 during the first quarter of 2024.

13) Commitments and Loss Contingencies

Loss Contingencies

Within the ordinary course of our business, we are subject to private lawsuits, government audits and examinations, administrative proceedings and other claims, and from time to time we may be subjected to increased risk associated with the acts or omissions of our customers (such as customers who, unbeknownst to the Bank or the Company, engage in or are associated with fraudulent or unlawful transactions, Ponzi schemes, money laundering, and similar unlawful acts). A number of these claims may exist at any given time, and some of the claims may be pled as class actions. We could be affected by adverse publicity and litigation costs resulting from such allegations, regardless of whether they are valid or whether we are legally determined to be liable.

At March 31, 2024, the Company was the subject of three pending legal proceedings (excluding pending and potential litigation arising in the ordinary course of business). All three such claims are employment-related. Between November 2020 and October 2021, three employees filed employment-related lawsuits against the Bank. The claims purport to be class actions on behalf of other employees and seek unspecified damages, penalties and attorney fees under the California Labor Code, the California Business and Professions Code, and the California Private Attorneys General Act ("PAGA"). The claimants allege various instances of disability, race and gender discrimination, wage-and-hour violations, retaliation, and related claims. Those cases remain pending in Alameda County Superior Court following a series of motions and interlocutory appeals. The Company believes the underlying claims are without merit and intend to defend them vigorously.

The Company makes a provision for a liability relating to legal matters when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. These provisions are reviewed at least quarterly and adjusted to reflect the impacts of negotiations, estimated settlements, legal rulings, advice of legal counsel and other information and events pertaining to a particular matter. The outcomes of legal proceedings and other contingencies are, however, inherently unpredictable and subject to significant uncertainties. As a result, the Company cannot reasonably estimate the amount or range of possible losses, including losses that could arise as a result of application of non-monetary remedies, with respect to the contingencies it faces, and the Company's estimates may not prove to be accurate.

At this time, we believe that the amount of reasonably possible losses resulting from final disposition of any pending lawsuits, audits, proceedings and claims will not have a material adverse effect individually or in the aggregate on our financial position, results of operations or liquidity. It is possible, however, that our future results of operations for a particular quarter or fiscal year could be impacted by changes in circumstances relating to lawsuits, proceedings or claims. Legal costs related to such claims are expensed as incurred.

Off-Balance Sheet Arrangements

In the normal course of business the Company makes commitments to extend credit to its customers as long as there are no violations of any conditions established in the contractual arrangements. These commitments are obligations that represent a potential credit risk to the Company, but are not reflected on the Company's consolidated balance sheets. Total unused commitments to extend credit were $1,156,000,000 at March 31, 2024, and $1,149,056,000 at December 31, 2023. Unused commitments represented 35% and 34% of outstanding gross loans at March 31, 2024 and December 31, 2023, respectively.

The effect on the Company's revenues, expenses, cash flows and liquidity from the unused portion of the commitments to provide credit cannot be reasonably predicted because there is no certainty that lines of credit and letters of credit will ever be fully utilized. The following table presents the Company's commitments to extend credit for the periods indicated:

	March 31, 2024			December 31, 2023		
	Fixed Rate	Variable Rate	Total	Fixed Rate	Variable Rate	Total
	(Dollars in thousands)					
Unused lines of credit and commitments to make loans	$ 73,278	$ 1,068,636	$ 1,141,914	$ 96,166	$ 1,041,608	$ 1,137,774
Standby letters of credit	6,101	7,985	14,086	4,283	6,999	11,282
	$ 79,379	$ 1,076,621	$ 1,156,000	$ 100,449	$ 1,048,607	$ 1,149,056

For the three months ended March 31, 2024, there was a decrease of ($ 44,000) to the allowance for credit losses on the Company's off-balance sheet credit exposures. The decrease in the allowance for credit losses for off-balance sheet credit exposures in the first three months of 2024 was driven by a decline in the loss factor in the commercial and industrial and land and construction loan segments. The allowance for credit losses on the Company's off-balance sheet credit exposures was $723,000 at March 31, 2024 and $ 767,000 at December 31, 2023.

14) Revenue Recognition

Service charges and fees on deposit accounts consist of account analysis fees (i.e., net fees earned on analyzed business and public checking accounts), monthly service fees, check orders, and other deposit account related fees. We sometimes charge customers fees that are not specifically related to the customer accessing its funds, such as account maintenance or dormancy fees. The amount of deposit fees assessed varies based on a number of factors, such as the type of customer and account, the quantity of transactions, and the size of the deposit balance. We charge, and in some circumstances do not charge, fees to earn additional revenue and influence certain customer behavior. An example would be where we do not charge a monthly service fee, or do not charge for certain transactions, for customers that have a high deposit balance. Deposit fees are considered either transactional in nature (such as wire transfers, nonsufficient fund fees, and stop payment orders) or non-transactional (such as account maintenance and dormancy fees). These fees are recognized as earned or as transactions occur and services are provided. Check orders and other deposit account related fees are largely transactional based and, therefore, the Company's performance obligation is satisfied, and related revenue recognized, at a point in time. Payment for service charges on deposit accounts is primarily received immediately or in the following month through a direct charge to customers' accounts.

The Company currently accounts for sales of foreclosed assets in accordance with Topic 360-20. In most cases the Company will seek to engage a real estate agent for the sale of foreclosed assets immediately upon foreclosure. However, in some cases, where there is clear demand for the property in question, the Company may elect to allow for a marketing period of no more than six months to attempt a direct sale of the property. We generally recognize the sale, and any associated gain or loss, of a real estate property when control of the property transfers. Any gains or losses from the sale are recorded to noninterest income/expense.

The following presents noninterest income, segregated by revenue streams in-scope and out-of-scope of Topic 606, for the periods indicated:

	Three Months Ended March 31,	
	2024	2023
	(Dollars in thousands)	
Noninterest Income In-scope of Topic 606:		
Service charges and fees on deposit accounts	$ 877	$ 1,743
Total noninterest income in-scope of Topic 606	877	1,743
Noninterest Income Out-of-scope of Topic 606	1,170	1,023
Total noninterest income	$ 2,047	$ 2,766

15) Noninterest Expense

The following table sets forth the various components of the Company’s noninterest expense for the periods indicated:

	Three Months Ended March 31,	
	2024	2023
	(Dollars in thousands)	
Salaries and employee benefits	$ 15,509	$ 14,809
Occupancy and equipment	2,443	2,400
Insurance expense	1,634	1,520
Professional fees	1,327	1,399
Data processing	840	774
Client services	782	445
Federal Deposit Insurance Corporation ("FDIC") assessments	670	417
Other	4,331	3,637
Total noninterest expense	$ 27,536	$ 25,401

16) Leases

The Company recognizes the following for all leases, at the commencement date: (1) a lease liability, which is a lessee’s obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) a right-of-use (“ROU”) 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. The Company is impacted as a lessee of the offices and real estate used for operations. The Company's lease agreements include options to renew at the Company's option. No lease extensions are reasonably certain to be exercised, therefore it was not considered in the calculation of the ROU asset and lease liability. As of March 31, 2024, operating lease ROU assets, included in other assets, and lease liabilities, included in other liabilities, totaled $30,726,000.

The following table presents the quantitative information for the Company’s leases for the periods indicated:

	Three Months Ended March 31,	
	2024	2023
	(Dollars in thousands)	
Operating Lease Cost (Cost resulting from lease payments)	$ 1,676	$ 1,701
Operating Lease - Operating Cash Flows (Fixed Payments)	$ 1,684	$ 1,645
Operating Lease - ROU assets	$ 30,726	$ 32,123
Operating Lease - Liabilities	$ 30,726	$ 32,123
Weighted Average Lease Term - Operating Leases	5.65 years	6.44 years
Weighted Average Discount Rate - Operating Leases	5.03%	4.54%

The following maturity analysis shows the undiscounted cash flows due on the Company’s operating lease liabilities as of March 31, 2024:

	(Dollars in thousands)
2024 remaining	$ 5,085
2025	6,412
2026	5,835
2027	5,575
2028	4,971
Thereafter	7,532
Total undiscounted cash flows	35,410
Discount on cash flows	(4,684)
Total lease liability	$ 30,726

17) Business Segment Information

The following presents the Company's operating segments. The Company operates through two business segments: Banking segment and Factoring segment. Transactions between segments consist primarily of borrowed funds. Intersegment interest expense is allocated to the Factoring segment based on the Company's prime rate and funding costs. The provision for credit losses on loans is allocated based on the segment's allowance for credit loss determination which considers the effects of charge-offs. Noninterest income and expense directly attributable to a segment are assigned to it. Taxes are paid on a consolidated basis and allocated for segment purposes. The Factoring segment includes only factoring originated by Bay View Funding.

	Three Months Ended March 31, 2024		
	Banking [1]	Factoring	Consolidated
	(Dollars in thousands)		
Interest income	$ 54,713	$ 2,838	$ 57,551
Intersegment interest allocations	423	(423)	—
Total interest expense	17,458	—	17,458
Net interest income	37,678	2,415	40,093
Provision for (recapture of) credit losses on loans	285	(101)	184
Net interest income after provision	37,393	2,516	39,909
Noninterest income	1,959	88	2,047
Noninterest expense	26,089	1,447	27,536
Intersegment expense allocations	128	(128)	—
Income before income taxes	13,391	1,029	14,420
Income tax expense	3,950	304	4,254
Net income	$ 9,441	$ 725	$ 10,166
Total assets	$ 5,172,553	$ 83,521	$ 5,256,074
Loans, net of deferred fees	$ 3,280,404	$ 55,698	$ 3,336,102
Goodwill	$ 154,587	$ 13,044	$ 167,631

	Three Months Ended March 31, 2023		
	Banking [1]	Factoring	Consolidated
	(Dollars in thousands)		
Interest income	$ 52,273	$ 4,001	$ 56,274
Intersegment interest allocations	705	(705)	—
Total interest expense	7,016	—	7,016
Net interest income	45,962	3,296	49,258
Provision for (recapture of) credit losses on loans	144	(112)	32
Net interest income after provision	45,818	3,408	49,226
Noninterest income	2,682	84	2,766
Noninterest expense	23,728	1,673	25,401
Intersegment expense allocations	174	(174)	—
Income before income taxes	24,946	1,645	26,591
Income tax expense	7,188	486	7,674
Net income	$ 17,758	$ 1,159	$ 18,917
Total assets	$ 5,453,352	$ 83,188	$ 5,536,540
Loans, net of deferred fees	$ 3,192,491	$ 69,424	$ 3,261,915
Goodwill	$ 154,587	$ 13,044	$ 167,631

(1) Includes the holding company's results of operations

18) Subsequent Events

On April 25, 2024, the Company announced that its Board of Directors declared a $ 0.13 per share quarterly cash dividend to holders of common stock. The dividend will be payable on May 23, 2024, to shareholders of record at the close of the business day on May 9, 2024.

ITEM 2—MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion provides information about the results of operations, financial condition, liquidity, and capital resources of Heritage Commerce Corp (the "Company" or "HCC"), its wholly-owned subsidiary, Heritage Bank of Commerce (the "Bank" or "HBC"), and HBC's wholly-owned subsidiary, CSNK Working Capital Finance Corp, a California Corporation, dba Bay View Funding. This information is intended to facilitate the understanding and assessment of significant changes and trends related to our financial condition and the results of operations. This discussion and analysis should be read in conjunction with our consolidated financial statements and the accompanying notes presented elsewhere in this Quarterly Report on Form 10-Q (this "Report"). Unless we state otherwise or the context indicates otherwise, references to the "Company," "Heritage," "we," "us," and "our," in this Report refer to Heritage Commerce Corp and its subsidiaries.

Financial results are presented in accordance with accounting principles generally accepted in the United States of America ("GAAP") and with reference to certain non-GAAP financial measures. Management believes that the presentation of certain non-GAAP financial measures provide useful supplemental information to investors as these financial measures are commonly used in the banking industry. A reconciliation of GAAP to non-GAAP financial measures are presented in the tables under *"Reconciliation of Non-GAAP Financial Measures."*

CRITICAL ACCOUNTING POLICIES

Critical accounting policies are discussed in our Form 10-K for the year ended December 31, 2023 under the heading "*Item 7—Management's Discussion and Analysis of Financial Condition and Results of Operations.* " There have been no changes in the Company's application of critical accounting policies since December 31, 2023.

EXECUTIVE SUMMARY

This summary is intended to identify the most important matters on which management focuses when it evaluates the financial condition and performance of the Company. When evaluating financial condition and performance, management looks at certain key metrics and measures. The Company's evaluation includes comparisons with peer group financial institutions and its own performance objectives established in the internal planning process.

The primary activity of the Company is commercial banking. The Company's commercial banking operations are located in the general San Francisco Bay Area of California in the counties of Alameda, Contra Costa, Marin, San Benito, San Francisco, San Mateo, and Santa Clara. The Company's market includes the cities of Oakland, San Francisco, and San Jose, the headquarters of a number of technology based companies in the region known commonly as Silicon Valley. The Company's customers are primarily closely held businesses and professionals.

Performance Overview

For the three months ended March 31, 2024, net income was $10.2 million, or $0.17 per average diluted common share, compared to $18.9 million, or $0.31 per average diluted common share, for the three months ended March 31, 2023. The Company's annualized return on average assets was 0.79% and annualized return on average equity was 6.08% for the three months ended March 31, 2024, compared to 1.47% and 12.03%, respectively, for the three months ended March 31, 2023. The Company's annualized return on average tangible assets was 0.82% and annualized return on average tangible common equity was 8.24% for the three months ended March 31, 2024, compared to 1.52% and 16.71%, respectively, for the three months ended March 31, 2023. The annualized return on average tangible assets and annualized return on average tangible common equity are non-GAAP financial measures.

First Quarter 2024 Highlights

Results of Operations:

- Net interest income decreased (19%) to $40.1 million for the first quarter of 2024, compared to $49.3 million for the first quarter of 2023. The fully tax equivalent ("FTE") net interest margin contracted (75 basis points) to 3.34% for the first quarter of 2024, from 4.09% for the first quarter of 2023, primarily due to higher rates paid on customer deposits, a decrease in the average balances of noninterest-bearing demand deposits, a decrease in average interest earning assets, and decreases in average balances of higher yielding asset-based loans and Bay View Funding factored receivables, partially offset by an increase in the rate on overnight funds. The FTE net interest margin is a non-GAAP financial measure.

- The average yield on the total loan portfolio decreased to 5.44% for the first quarter of 2024, compared to 5.46% for the first quarter of 2023, primarily due to lower average balances of higher yielding asset-based lending loans and Bay View Funding factored receivables, a decrease in the accretion of loan purchase discount into interest income from acquired loans, and lower prepayment fees, partially offset by increases in the prime rate.

- In aggregate, the unamortized net purchase discount on total loans acquired was $3.0 million at March 31, 2024.

- The average cost of total deposits increased to 1.56% for the first quarter of 2024, compared to 0.54% for the first quarter of 2023. The average cost of funds increased to 1.60% for the first quarter of 2024, compared to 0.63% for the first quarter of 2023.

- The increase in the average cost of total deposits and the average cost of funds for the first quarter of 2024 was primarily due to clients seeking higher yields and moving noninterest-bearing deposits to the Bank’s interest-bearing and Insured Cash Sweep (“ICS”)/Certificate of Deposit Account Registry Service (“CDARS”) deposits and interest-bearing money market accounts.

- During the first quarter of 2024, we recorded a provision for credit losses on loans of $184,000, compared to a $32,000 provision for credit losses on loans for the first quarter of 2023.

- Total noninterest income decreased (26%) to $2.0 million for the first quarter of 2024, compared to $2.8 million for the first quarter of 2023, primarily due to lower service charges and fees on deposit accounts during the first quarter of 2024.

- Total noninterest expense for the first quarter of 2024 increased to $27.5 million, compared to $25.4 million for the first quarter of 2023, primarily due to higher salaries and employee benefits which are seasonal in nature, and higher marketing related expenses, insurance costs, regulatory assessments, information technology related expenses, and ICS/CDARS fee expense included in other noninterest expense.

- The efficiency ratio increased to 65.34% for the first quarter of 2024, compared to 48.83% for the first quarter of 2023, primarily due to lower total revenue and higher noninterest expense during the first quarter of 2024. The efficiency ratio is a non-GAAP financial measure.

- Income tax expense was $4.3 million for the first quarter of 2024, compared to $7.7 million for the first quarter of 2023. The effective tax rate for the first quarter of 2024 was 29.5%, compared to 28.9% for the first quarter of 2023.

Current Financial Condition and Liquidity Position:

- Our liquidity, including cash on hand, undrawn lines of credit, and other sources of liquidity, totaled $3.00 billion, or 67% of the Company’s total deposits and approximately 149% of the Bank’s estimated uninsured deposits, at March 31, 2024. The Bank’s uninsured deposits were approximately $2.02 billion, or 45% of the Company’s total deposits, at March 31, 2024. The following table shows our liquidity, available lines of credit and the amounts outstanding at March 31, 2024:

	Total Available	Outstanding	Remaining Available
	(Dollars in thousands)		
Excess funds at the Federal Reserve Bank ("FRB")	$ 490,000	$ —	$ 490,000
FRB discount window collateralized line of credit	1,245,362	—	1,245,362
Federal Home Loan Bank ("FHLB") collateralized borrowing capacity	1,097,518	—	1,097,518
Unpledged investment securities (at fair value)	55,358	—	55,358
Federal funds purchase arrangements	90,000	—	90,000
Holding company line of credit	20,000	—	20,000
Total	$ 2,998,238	$ —	$ 2,998,238

- Cash, interest-bearing deposits in other financial institutions and securities available-for-sale, at fair value, decreased (23%) to $945.8 million at March 31, 2024, from $1.23 billion at March 31, 2023, and increased 11% from $850.8 million at December 31, 2023.

- Securities held-to-maturity, at amortized cost, totaled $636.3 million at March 31, 2024, compared to $698.2 million at March 31, 2023, and $650.6 million, at December 31, 2023.

- The pre-tax unrealized loss on the securities available-for-sale portfolio was ($9.7) million, or ($6.9) million net of taxes, which was 1.0% of total shareholders' equity at March 31, 2024. The pre-tax unrealized loss on the securities held-to-maturity portfolio was ($93.4) million at March 31, 2024, or ($65.8) million net of taxes, which was 9.7% of total shareholders' equity at March 31, 2024. The fair value is expected to recover as the securities approach their maturity date and/or interest rates decline.

- The weighted average life of the securities available-for-sale portfolio was 1.15 years, the weighted average life of the securities held-to-maturity portfolio was 6.59 years, and the average life of the total investment securities portfolio was 4.44 years at March 31, 2024.

- The following are the projected cash flows from paydowns and maturities in the investment securities portfolio for the periods indicated based on the current interest rate environment:

	U.S. Treasury	Agency Mortgage-backed and Municipal Securities	Total
	(Dollars in thousands)		
Second quarter of 2024	$ 131,000	$ 22,245	$ 153,245
Third quarter of 2024	37,500	21,031	58,531
Fourth quarter of 2024	9,000	19,442	28,442
First quarter of 2025	35,000	18,851	53,851
Second quarter of 2025	118,000	18,381	136,381
Third quarter of 2025	25,500	19,583	45,083
Fourth quarter of 2025	—	18,035	18,035
First quarter of 2026	—	17,136	17,136
Total	$ 356,000	$ 154,704	$ 510,704

- Loans, excluding loans held-for-sale, increased $74.2 million, or 2%, to $3.34 billion at March 31, 2024, compared to $3.26 billion at March 31, 2023, and decreased ($14.3) million from $3.35 billion at December 31, 2023. Core loans, excluding residential mortgages, increased $112.8 million, or 4%, to $2.85 billion at March 31, 2024, compared to $2.73 billion at March 31, 2023, and relatively flat from $2.85 billion at December 31, 2023.

- There were 13 borrowers included in nonperforming assets (“NPAs”) totaling $7.9 million, or 0.15% of total assets, at March 31, 2024, compared to 8 borrowers totaling $2.2 million, or 0.04% of total assets, at March 31, 2023, and 12 borrowers totaling $7.7 million, or 0.15% of total assets at December 31, 2023.

- Classified assets totaled $35.4 million, or 0.67% of total assets, at March 31, 2024, compared to $26.8 million, or 0.48% of total assets, at March 31, 2023, and $31.8 million, or 0.61% of total assets, at December 31, 2023. The increase in classified assets during the first quarter of 2024 was primarily due to the downgrade of one commercial real estate (“CRE”) investor loan, which is well collateralized,, fully leased, cash-flowing, and personally guaranteed by the principals.

- Net charge-offs totaled $254,000 for the first quarter of 2024, compared to net charge-offs of $271,000 for the first quarter of 2023, and net charge-offs of $33,000 for the fourth quarter of 2023.

- The allowance for credit losses on loans (“ACLL”) at March 31, 2024 was $47.9 million, or 1.44% of total loans, representing 608% of total nonperforming loans. The ACLL at March 31, 2023 was $47.3 million, or 1.45% of total loans, representing 2,110% of total nonperforming loans. The ACLL at December 31, 2023 was $48.0 million, or 1.43% of total loans, representing 622% of total nonperforming loans.

- Total deposits were relatively flat at $4.44 billion at both March 31, 2024 and March 31, 2023. Total deposits increased $66.2 million, or 2%, from $4.38 billion at December 31, 2023.

- Migration of client deposits into interest-bearing and insured accounts and resulted in an increase in ICS/CDARS deposits to $913.8 million at March 31, 2024, compared to $304.1 million at March 31, 2023, and increased $59.7 million from $854.1 million at December 31, 2023.

- Noninterest-bearing demand deposits decreased ($227.0) million, or (15%), to $1.24 billion at March 31, 2024 from $1.47 billion at March 31, 2023, largely in response to the increasing interest rate environment. Noninterest-bearing demand deposits decreased ($50.4) million, or (4%), from $1.29 billion at December 31, 2023.

- The ratio of noncore funding (which consists of time deposits of $250,000 and over, brokered deposits, securities under an agreement to repurchase, subordinated debt, and short-term borrowings) to total assets was 4.57% at March 31, 2024, compared to 9.24% at March 31, 2023, and 4.46% at December 31, 2023.

- The loan to deposit ratio was 75.06% at March 31, 2024, compared to 73.39% at March 31, 2023, and 76.52% at December 31, 2023.

Capital Adequacy:

- The Company's consolidated capital ratios exceeded regulatory guidelines and the HBC's capital ratios exceeded the prompt corrective action ("PCA") regulatory guidelines for a well-capitalized financial institution, and the Basel III minimum regulatory requirements at March 31 2024, as reflected in the following table:

Capital Ratios	Heritage Commerce Corp	Heritage Bank of Commerce	Well-capitalized Financial Institution PCA Regulatory Guidelines	Basel III Minimum Regulatory Requirements(1)
Total Capital	15.6 %	15.1 %	10.0 %	10.5 %
Tier 1 Capital	13.4 %	13.9 %	8.0 %	8.5 %
Common Equity Tier 1 Capital	13.4 %	13.9 %	6.5 %	7.0 %
Tier 1 Leverage	10.2 %	10.6 %	5.0 %	4.0 %
Tangible common equity / tangible assets [2]	9.9 %	10.2 %	N/A	N/A

(1) Basel III minimum regulatory requirements for both HCC and HBC include a 2.5% capital conservation buffer, except the Tier 1 Leverage ratio.
(2) This is a non-GAAP financial measure that represents shareholders' equity minus goodwill and other intangible assets divided by total assets minus goodwill and other intangible assets.

RESULTS OF OPERATIONS

The Company earns income from two primary sources. The first is net interest income, which is interest income generated by earning assets less interest expense on interest-bearing liabilities. The second is noninterest income, which primarily consists of gains on the sale of loans, loan servicing fees, customer service charges and fees, the increase in cash surrender value of life insurance, and gains on the sale of securities. The majority of the Company's noninterest expenses are operating costs that relate to providing banking services to our customers.

Net Interest Income and Net Interest Margin

The level of net interest income depends on several factors in combination, including growth in earning assets, yields on earning assets, the cost of interest-bearing liabilities, the relative volumes of earning assets and interest-bearing liabilities, and the mix of products that comprise the Company's earning assets, deposits, and other interest-bearing liabilities. Net interest income can also be impacted by the reversal of interest on loans placed on nonaccrual status, and recovery of interest on loans that have been on nonaccrual and are either sold or returned to accrual status. To maintain its net interest margin, the Company must manage the relationship between interest earned and interest paid.

The following Distribution, Rate and Yield table presents for each of the past three years, the average amounts outstanding for the major categories of the Company's balance sheet, the average interest rates earned or paid thereon, and the resulting net interest margin on average interest earning assets for the periods indicated. Average balances are based on daily averages.

Distribution, Rate and Yield

	Three Months Ended March 31, 2024			Three Months Ended March 31, 2023		
	Average Balance	Interest Income / Expense	Average Yield / Rate	Average Balance	Interest Income / Expense	Average Yield / Rate
	(Dollars in thousands)					
Assets:						
Loans, gross [1][2]	$ 3,299,989	$ 44,600	5.44 %	$ 3,277,525	$ 44,112	5.46 %
Securities — taxable	1,042,484	6,183	2.39 %	1,161,021	7,056	2.46 %
Securities — exempt from Federal tax [3]	31,939	286	3.60 %	36,012	313	3.52 %
Other investments, interest-bearing deposits in other financial institutions and Federal funds sold	467,867	6,542	5.62 %	420,451	4,859	4.69 %
Total interest earning assets	4,842,279	57,611	4.79 %	4,895,009	56,340	4.67 %
Cash and due from banks	33,214			37,563		
Premises and equipment, net	10,015			9,269		
Goodwill and other intangible assets	176,039			178,443		
Other assets	117,089			115,222		
Total assets	$ 5,178,636			$ 5,235,506		
Liabilities and shareholders' equity:						
Deposits:						
Demand, noninterest-bearing	$ 1,177,078			$ 1,667,260		
Demand, interest-bearing	920,048	1,554	0.68 %	1,217,731	1,476	0.49 %
Savings and money market	1,067,581	6,649	2.50 %	1,285,173	3,489	1.10 %
Time deposits — under $100	10,945	42	1.54 %	12,280	10	0.33 %
Time deposits — $100 and over	221,211	2,064	3.75 %	163,047	845	2.10 %
ICS/CDARS — interest-bearing demand, money market and time deposits	963,287	6,611	2.76 %	70,461	81	0.47 %
Total interest-bearing deposits	3,183,072	16,920	2.14 %	2,748,692	5,901	0.87 %
Total deposits	4,360,150	16,920	1.56 %	4,415,952	5,901	0.54 %
Short-term borrowings	15	—	0.00 %	46,677	578	5.02 %
Subordinated debt, net of issuance costs	39,516	538	5.48 %	39,363	537	5.53 %
Total interest-bearing liabilities	3,222,603	17,458	2.18 %	2,834,732	7,016	1.00 %
Total interest-bearing liabilities and demand, noninterest-bearing / cost of funds	4,399,681	17,458	1.60 %	4,501,992	7,016	0.63 %
Other liabilities	106,663			95,917		
Total liabilities	4,506,344			4,597,909		
Shareholders' equity	672,292			637,597		
Total liabilities and shareholders' equity	$ 5,178,636			$ 5,235,506		
Net interest income / margin		40,153	3.34 %		49,324	4.09 %
Less tax equivalent adjustment		(60)			(66)	
Net interest income		$ 40,093			$ 49,258	

(1) Includes loans held-for-sale. Nonaccrual loans are included in average balance.
(2) Yield amounts earned on loans include fees and costs. The accretion of net deferred loan fees into loan interest income was $160,000 for the first quarter of 2024, compared to $300,000 for the first quarter of 2023. Prepayment fees totaled $24,000 for the first quarter of 2024, compared to $138,000 for the first quarter of 2023.
(3) Reflects the non-GAAP fully tax equivalent adjustment for Federal tax-exempt income based on a 21% tax rate.

Volume and Rate Variances

The Volume and Rate Variances table below sets forth the dollar difference in interest earned and paid for each major category of interest-earning assets and interest-bearing liabilities for the noted periods, and the amount of such change attributable to changes in average balances (volume) or changes in average interest rates. Volume variances are equal to the increase or decrease in the average balance multiplied by prior period rates and rate variances are equal to the increase or decrease in the average rate multiplied by the prior period average balance. Variances attributable to both rate and volume changes are equal to the change in rate multiplied by the change in average balance and are included below in the average volume column.

	Three Months Ended March 31, 2024 vs. 2023 Increase (Decrease) Due to Change in:		
	Average Volume	Average Rate	Net Change
	(Dollars in thousands)		
Income from the interest earning assets:			
Loans, gross	$ 269	$ 219	$ 488
Securities — taxable	(716)	(157)	(873)
Securities — exempt from Federal tax (1)	(36)	9	(27)
Other investments, interest-bearing deposits in other financial institutions and Federal funds sold	667	1,016	1,683
Total interest income on interest-earning assets	184	1,087	1,271
Expense from the interest-bearing liabilities:			
Demand, interest-bearing	(505)	583	78
Savings and money market	(1,339)	4,499	3,160
Time deposits — under $100	(5)	37	32
Time deposits — $100 and over	544	675	1,219
CDARS — interest-bearing demand, money market and time deposits	6,127	403	6,530
Short-term borrowings	—	(578)	(578)
Subordinated debt, net of issuance costs	2	(1)	1
Total interest expense on interest-bearing liabilities	4,824	5,618	10,442
Net interest income	$ (4,640)	$ (4,531)	(9,171)
Less tax equivalent adjustment			6
Net interest income			$ (9,165)

(1) Reflects the non-GAAP fully tax equivalent adjustment for Federal tax-exempt income based on a 21% tax rate.

Net interest income decreased (19%) to $40.1 million for the first quarter of 2024, compared to $49.3 million for the first quarter of 2023. The non-GAAP FTE net interest margin contracted (75 basis points) to 3.34% for the first quarter of 2024, from 4.09% for the first quarter of 2023, primarily due to higher rates paid on customer deposits, a decrease in the average balances of noninterest-bearing demand deposits, a decrease in average interest earnings assets, and decreases in average balances of higher yielding asset-based loans and Bay View Funding factored receivables, partially offset by an increase in the rate on overnight funds.

The following tables present the average balance of loans outstanding, interest income, and the average yield for the periods indicated:

	For the Quarter Ended March 31, 2024			For the Quarter Ended March 31, 2023		
	Average Balance	Interest Income	Average Yield	Average Balance	Interest Income	Average Yield
			(Dollars in thousands)			
Loans, core bank	$ 2,779,487	$ 37,339	5.40 %	$ 2,688,800	$ 34,967	5.27 %
Prepayment fees	—	24	0.00 %	—	138	0.02 %
Asset-based lending	15,864	382	9.68 %	27,550	627	9.23 %
Bay View Funding factored receivables	53,511	2,838	21.33 %	77,755	4,001	20.87 %
Purchased residential mortgages	454,240	3,788	3.35 %	487,780	3,857	3.21 %
Loan fair value mark / accretion	(3,113)	229	0.03 %	(4,360)	522	0.08 %
Total loans (includes loans held-for-sale)	$ 3,299,989	$ 44,600	5.44 %	$ 3,277,525	$ 44,112	5.46 %

The average yield on the total loan portfolio decreased to 5.44% for the first quarter of 2024, compared to 5.46% for the first quarter of 2023, primarily due to lower average balances of higher yielding asset-based lending loans and Bay View Funding factored receivables, a decrease in the accretion of loan purchase discount into interest income from acquired loans, and lower prepayment fees, partially offset by increases in the prime rate.

In aggregate, the remaining net purchase discount on total loans acquired was $3.0 million at March 31, 2024.

The average cost of total deposits increased to 1.56% for the first quarter of 2024, compared to 0.54% for the first quarter of 2023. The average cost of funds increased to 1.60% for the first quarter of 2024, compared to 0.63% for the first quarter of 2023.

The increase in the average cost of total deposits and the average cost of funds for the first quarter of 2024 was primarily due to clients seeking higher yields and moving noninterest-bearing deposits to the Bank's interest-bearing and ICS/CDARS deposits and to interest-bearing money market accounts.

Provision for Credit Losses on Loans

Credit risk is inherent in the business of making loans. The Company establishes an allowance for credit losses on loans through charges to earnings, which are presented in the statements of income as the provision for credit losses on loans. Specifically identifiable and quantifiable known losses are promptly charged off against the allowance. The provision for credit losses on loans is determined by conducting a quarterly evaluation of the adequacy of the Company's allowance for credit losses on loans and charging the shortfall or excess, if any, to the current quarter's expense. This has the effect of creating variability in the amount and frequency of charges to the Company's earnings. The provision for credit losses on loans and level of allowance for each period are dependent upon many factors, including loan growth, net charge-offs, changes in the composition of the loan portfolio, delinquencies, management's assessment of the quality of the loan portfolio, the valuation of problem loans and the general economic conditions in the Company's market area. The provision for credit losses on loans and level of allowance for each period are also dependent on forecast data for the state of California including GDP and unemployment rate projections.

There was a provision for credit losses on loans of $184,000 for the first quarter of 2024, compared to a provision for credit losses on loans of $32,000 for the first quarter of 2023. Provisions for credit losses on loans are charged to operations to bring the allowance for credit losses on loans to a level deemed appropriate by the Company based on the factors discussed under *"Credit Quality and Allowance for Credit Losses on Loans."*

Noninterest Income

	Three Months Ended March 31,		Increase (decrease) 2024 versus 2023	
	2024	2023	Amount	Percent
	(Dollars in thousands)			
Service charges and fees on deposit accounts	$ 877	$ 1,743	$ (866)	(50)%
Increase in cash surrender value of life insurance	518	493	25	5 %
Gain on sales of SBA loans	178	76	102	134 %
Servicing income	90	131	(41)	(31)%
Termination fees	13	11	2	18 %
Other	371	312	59	19 %
Total	$ 2,047	$ 2,766	$ (719)	(26)%

Total noninterest income decreased (26%) to $2.0 million for the first quarter of 2024, compared to $2.8 million for the first quarter of 2023, primarily due to lower service charges and fees on deposit accounts during the first quarter of 2024.

A portion of the Company's noninterest income is associated with its Small Business Administration ("SBA") lending activity, as gain on the sales of loans sold in the secondary market and servicing income from loans sold with servicing rights retained. For the first quarter of 2024, SBA loan sales resulted in an $178,000 gain, compared to a $76,000 gain on sales of SBA loans for the first quarter of 2023.

The servicing assets that result from the sales of SBA loans with servicing retained are amortized over the expected term of the loans using a method approximating the interest method. Servicing income generally declines as the respective loans are repaid.

Noninterest Expense

The following table sets forth the various components of the Company's noninterest expense:

	Three Months Ended March 31,		Increase (Decrease) 2024 versus 2023	
	2024	2023	Amount	Percent
	(Dollars in thousands)			
Salaries and employee benefits	$ 15,509	$ 14,809	$ 700	5 %
Occupancy and equipment	2,443	2,400	43	2 %
Insurance expense	1,634	1,520	114	8 %
Professional fees	1,327	1,399	(72)	(5)%
Data processing	840	774	66	9 %
Client services	782	445	337	76 %
Federal Deposit Insurance Corporation ("FDIC") assessments	670	417	253	61 %
Other	4,331	3,637	694	19 %
Total noninterest expense	$ 27,536	$ 25,401	$ 2,135	8 %

The following table indicates the percentage of noninterest expense in each category for the periods indicated:

	Three Months Ended March 31,			
	2024	Percent of Total	2023	Percent of Total
	(Dollars in thousands)			
Salaries and employee benefits	$ 15,509	56 %	$ 14,809	58 %
Occupancy and equipment	2,443	9 %	2,400	9 %
Insurance expense	1,634	6 %	1,520	6 %
Professional fees	1,327	5 %	1,399	6 %
Data processing	840	3 %	774	3 %
Client services	782	3 %	445	2 %
FDIC assessments	670	2 %	417	2 %
Other	4,331	16 %	3,637	14 %
Total noninterest expense	$ 27,536	100 %	$ 25,401	100 %

Total noninterest expense for the first quarter of 2024 increased to $27.5 million, compared to $25.4 million for the first quarter of 2023, primarily due to higher salaries and employee benefits, higher marketing related expenses, insurance costs, regulatory assessments, information technology related expenses, and ICS/CDARS fee expense included in other noninterest expense.

Full time equivalent employees were 351 at March 31, 2024, compared to 339 at March 31, 2023, and 349 and at December 31, 2023.

Income Tax Expense

The Company computes its provision for income taxes on a monthly basis. The effective tax rate is determined by applying the Company's statutory income tax rates to pre-tax book income as adjusted for permanent differences between pre-tax book income and actual taxable income. These permanent differences include, but are not limited to, increases in the cash surrender value of life insurance policies, interest on tax-exempt securities, certain expenses that are not allowed as tax deductions, and tax credits.

The following table shows the Company's effective income tax rates for the periods indicated:

	March 31,	
	2024	2023
Effective income tax rate	29.5 %	28.9 %

The Company's Federal and state income tax expense for the first quarter of 2024 was $4.3 million, compared to $7.7 million for the first quarter of 2023.

Some items of income and expense are recognized in different years for tax purposes than when applying generally accepted accounting principles leading to timing differences between the Company's actual tax liability, and the amount accrued for this liability based on book income. These temporary differences comprise the "deferred" portion of the Company's tax expense or benefit, which is accumulated on the Company's books as a deferred tax asset or deferred tax liability until such time as they reverse.

Realization of the Company's deferred tax assets is primarily dependent upon the Company generating sufficient future taxable income to obtain benefit from the reversal of net deductible temporary differences and the utilization of tax credit carryforwards and the net operating loss carryforwards for Federal and state income tax purposes. The amount of deferred tax assets considered realizable is subject to adjustment in future periods based on estimates of future taxable income. Under generally accepted accounting principles a valuation allowance is required to be recognized if it is "more likely than not" that the deferred tax assets will not be realized. The determination of the realizability of the deferred tax assets is highly subjective and dependent upon judgment concerning management's evaluation of both positive and negative evidence, including forecasts of future income, cumulative losses, applicable tax planning strategies, and assessments of current and future economic and business conditions.

The Company had net deferred tax assets of $27.5 million at March 31, 2024, and $29.8 million at both March 31, 2023 and December 31, 2023. After consideration of the matters in the preceding paragraph, the Company determined that it is more likely than not that the net deferred tax assets at March 31, 2024, March 31, 2023, and December 31, 2023 will be fully realized in future years.

FINANCIAL CONDITION

At March 31, 2024, total assets decreased (5%) to $5.26 billion, compared to $5.54 billion at March 31, 2023, and increased 1% from $5.19 billion at December 31, 2023.

Securities available-for-sale, at fair value, were $404.5 million at March 31, 2024, a decrease of (18%) from $491.8 million at March 31, 2023, and decreased (9%) from $442.6 million at December 31, 2023. Securities held-to-maturity, at amortized cost, were $636.2 million at March 31, 2024, a decrease of (9%) from $698.2 million at March 31, 2023, and a decrease of (2%) from $650.6 million at December 31, 2023.

Loans, excluding loans held-for-sale, increased $74.2 million, or 2%, to $3.34 billion at March 31, 2024, compared to $3.26 billion at March 31, 2023, and decreased ($14.3) million from $3.35 billion at December 31, 2023. Core loans, excluding residential mortgages, increased $112.8 million, or 4%, to $2.85 billion at March 31, 2024, compared to $2.73 billion at March 31, 2023, and remained relatively flat from $2.85 billion at December 31, 2023.

Total deposits were relatively flat at $4.44 billion at both March 31, 2024 and March 31, 2023. Total deposits increased $66.2 million, or 2%, from $4.38 billion at December 31, 2023.

Securities Portfolio

The following table reflects the balances for each category of securities at the dates indicated:

	March 31,		December 31,
	2024	2023	2023
	(Dollars in thousands)		
Securities available-for-sale (at fair value):			
U.S. Treasury	$ 347,453	$ 422,903	$ 382,369
Agency mortgage-backed securities	57,021	68,848	60,267
Total	$ 404,474	$ 491,751	$ 442,636
Securities held-to-maturity (at amortized cost):			
Agency mortgage-backed securities	$ 604,458	$ 663,481	$ 618,374
Municipals — exempt from Federal tax (1)	31,803	34,764	32,203
Total (1)	$ 636,261	$ 698,245	$ 650,577

(1) Gross of the allowance for credit losses of ($12,000) at both March 31, 2024 and December 31, 2023, and ($14,000) at March 31, 2023.

The following table summarizes the weighted average life and weighted average yields of securities at March 31, 2024:

	Weighted Average Life									
	Within One Year or Less		After One and Within Five Years		After Five and Within Ten Years		After Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
	(Dollars in thousands)									
Securities available-for-sale (at fair value):										
U.S. Treasury	$ 210,042	2.86 %	$ 137,411	2.99 %	$ —	— %	$ —	— %	$ 347,453	2.91 %
Agency mortgage-backed securities	68	3.20 %	47,232	2.52 %	9,721	2.67 %	—	— %	57,021	2.55 %
Total	$ 210,110	2.86 %	$ 184,643	2.87 %	$ 9,721	2.67 %	$ —	— %	$ 404,474	2.86 %
Securities held-to-maturity (at amortized cost):										
Agency mortgage-backed securities	$ 1,300	1.93 %	$ 61,579	2.13 %	$ 459,258	1.80 %	$ 82,321	2.85 %	$ 604,458	1.98 %
Municipals — exempt from Federal tax (1) (2)	1,925	4.37 %	8,017	3.43 %	21,861	3.57 %	—	0.00 %	31,803	3.58 %
Total (2)	$ 3,225	3.39 %	$ 69,596	2.27 %	$ 481,119	1.88 %	$ 82,321	2.85 %	$ 636,261	2.06 %

(1) Reflects tax equivalent adjustment for Federal tax exempt income based on a 21% tax rate.
(2) Gross of the allowance for credit losses of ($12,000) at March 31, 2024.

The securities portfolio serves the following purposes: (i) it provides a source of pledged assets for securing certain deposits and borrowed funds, as may be required by law or by specific agreement with a depositor or lender; (ii) it provides liquidity to even out cash flows from the loan and deposit activities of customers; (iii) it can be used as an interest rate risk management tool, since it provides a large base of assets, the maturity and interest rate characteristics of which can be changed more readily than the loan portfolio to better match changes in the deposit base and other funding sources of the Company; and (iv) it is an alternative interest-earning use of funds when loan demand is weak or when deposits grow more rapidly than loans.

The Company's portfolio may include: (i) U.S. Treasury securities and U.S. Government sponsored entities' debt securities for liquidity and pledging; (ii) mortgage-backed securities, which in many instances can also be used for pledging, and which generally enhance the yield of the portfolio; (iii) municipal obligations, which provide tax free income and limited pledging potential; (iv) single entity issue trust preferred securities, which generally enhance the yield on the portfolio; (v) corporate bonds, which also enhance the yield on the portfolio; (vi) money market mutual funds; (vii) certificates of deposit; (viii) commercial paper; (ix) bankers acceptances; (x) repurchase agreements; (xi) collateralized mortgage obligations; and (xii) asset-backed securities.

The Company classifies its securities as either available-for-sale or held-to-maturity at the time of purchase. Accounting guidance requires available-for-sale securities to be marked to fair value with an offset to accumulated other comprehensive income (loss), a component of shareholders' equity. Monthly adjustments are made to reflect changes in the fair value of the Company's available-for-sale securities.

The following table shows the net pre-tax unrealized and unrecognized (loss) on securities available-for-sale and securities held-to-maturity and the allowance for credit losses for the periods indicated:

	March 31,		December 31,
	2024	2023	2023
	(Dollars in thousands)		
Securities available-for-sale pre-tax unrealized (loss):			
U.S. Treasury	$ (4,784)	$ (7,510)	$ (5,621)
Agency mortgage-backed securities	(4,895)	(4,969)	(4,313)
Total	$ (9,679)	$ (12,479)	$ (9,934)
Securities held-to-maturity pre-tax unrecognized (loss):			
Agency mortgage-backed securities	$ (92,332)	$ (89,962)	$ (85,729)
Municipals — exempt from Federal tax	(1,071)	(297)	(721)
Total	$ (93,403)	$ (90,259)	$ (86,450)
Allowance for credit losses on municipal securities	$ (12)	$ (14)	$ (12)

The net pre-tax unrealized loss on the securities available-for-sale was ($9.7) million, or ($6.9) million net of taxes, which was 1.0% of total shareholders' equity at March 31, 2024. The net pre-tax unrecognized loss on the securities held-to-maturity at March 31, 2024 was ($93.4) million, or ($65.8) million net of taxes, which was 9.7% of total shareholders' equity at March 31, 2024. The unrealized and unrecognized losses in both the available-for-sale and held-to-maturity portfolios were due to higher interest rates at March 31, 2024 compared to when the securities were purchased. The issuers are of high credit quality and all principal amounts are expected to be repaid when the securities mature. The fair value is expected to recover as the securities approach their maturity date and/or interest rates decline.

Loans

The Company's loans represent the largest portion of earning assets, substantially greater than the securities portfolio or any other asset category, and the quality and diversification of the loan portfolio is an important consideration when reviewing the Company's financial condition. Gross loans, excluding loans held-for-sale, represented 63% of total assets at March 31, 2024, compared to 59% at March 31, 2023, and 65% at December 31, 2023. The loan to deposit ratio was 75.06% at March 31, 2024, compared to 73.39% at March 31, 2023, and 76.52% at December 31, 2023.

Loan Distribution

The Loan Distribution table that follows sets forth the Company's gross loans, excluding loans held-for-sale, outstanding and the percentage distribution in each category at the dates indicated:

	March 31, 2024		March 31, 2023		December 31, 2023	
	Balance	% to Total	Balance	% to Total	Balance	% to Total
	(Dollars in thousands)					
Commercial	$ 452,231	14 %	$ 506,602	16 %	$ 463,778	14 %
Real estate:						
CRE - owner occupied	585,031	17 %	603,298	18 %	583,253	17 %
CRE - non-owner occupied	1,271,184	38 %	1,083,852	33 %	1,256,590	37 %
Land and construction	129,712	4 %	166,408	5 %	140,513	4 %
Home equity	122,794	4 %	124,481	4 %	119,125	4 %
Multifamily	269,263	8 %	231,242	7 %	269,734	8 %
Residential mortgages	490,035	15 %	528,639	16 %	496,961	15 %
Consumer and other	16,439	< 1 %	17,905	1 %	20,919	1 %
Total Loans	3,336,689	100 %	3,262,427	100 %	3,350,873	100 %
Deferred loan fees, net	(587)	—	(512)	—	(495)	—
Loans, net of deferred fees	3,336,102	100 %	3,261,915	100 %	3,350,378	100 %
Allowance for credit losses on loans	(47,888)		(47,273)		(47,958)	
Loans, net	$ 3,288,214		$ 3,214,642		$ 3,302,420	

The Company's loan portfolio is concentrated in commercial loans, (primarily manufacturing, wholesale, and services oriented entities), and CRE, with the remaining balance in land development and construction, home equity, purchased residential mortgages, and consumer loans. The Company does not have any concentrations by industry or group of industries in its loan portfolio, however, 86% of its gross loans were secured by real property at March 31, 2024, compared to 83% at March 31, 2023, and 85% at December 31, 2023. While no specific industry concentration is considered significant, the Company's bank lending operations are substantially located in areas that are dependent on the technology and real estate industries and their supporting companies.

The Company has established concentration limits in its loan portfolio for commercial real estate loans, commercial loans, construction loans and unsecured lending, among others. All loan types are within established limits. The Company uses underwriting guidelines to assess the borrowers' historical cash flow to determine debt service, and we further stress test the debt service under higher interest rate scenarios. Financial and performance covenants are used in commercial lending to allow the Company to react to a borrower's deteriorating financial condition, should that occur. Stress testing and debt service on commercial real estate loans are reviewed quarterly.

The Company's commercial loans are made for working capital, financing the purchase of equipment or for other business purposes. Commercial loans include loans with maturities ranging from thirty days to two years and "term loans" with maturities normally ranging from one to five years. Short-term business loans are generally intended to finance current transactions and typically provide for periodic principal payments, with interest payable monthly. Term loans normally provide for floating interest rates, with monthly payments of both principal and interest.

The Company is an active participant in the SBA and U.S. Department of Agriculture guaranteed lending programs, and has been approved by the SBA as a lender under the Preferred Lender Program. The Company regularly makes such loans conditionally guaranteed by the SBA (collectively referred to as "SBA loans"). The guaranteed portion of these loans is typically sold in the secondary market depending on market conditions. When the guaranteed portion of an SBA loan is sold, the Company retains the servicing rights for the sold portion. During the three months ended March 31, 2024 and 2023, loans were sold resulting in a gain on sales of SBA loans of $178,000 and $76,000, respectively.

The Company's factoring receivables are from the operations of Bay View Funding, whose primary business is purchasing and collecting factored receivables on a nation-wide basis. Factored receivables are receivables that have been transferred by the originating organization and typically have not been subject to previous collection efforts. These receivables are acquired from a variety of companies, including but not limited to service providers, transportation companies, manufacturers, distributors, wholesalers, apparel companies, advertisers, and temporary staffing companies. The portfolio of factored receivables is included in the Company's commercial loan portfolio. The average life of the factored receivables was 35 days for the first three months of 2024, compared to 39 days for the first three months of 2023.

The following table shows the balance of factored receivables at period end, average balances during the period, and full time equivalent employees of Bay View Funding at period end:

	March 31, 2024	March 31, 2023
	(Dollars in thousands)	
Total factored receivables at period-end	$ 55,698	$ 69,424
Average factored receivables:		
For the three months ended	53,511	77,754
Total full time equivalent employees at period-end	30	26

The commercial loan portfolio decreased ($54.4) million, or (11%), to $452.2 million at March 31, 2024, from $506.6 million at March 31, 2023, and decreased ($11.6) million, or (2%), from $463.8 million at December 31, 2023. Commercial and industrial line usage was 28% at March 31, 2024, compared to 31% at March 31, 2023 and 29% at December 31, 2023.

The Company's CRE loans consist primarily of loans based on the borrower's cash flow and are secured by deeds of trust on commercial property to provide a secondary source of repayment. The Company generally restricts real estate term loans to no more than 75% of the property's appraised value or the purchase price of the property depending on the type of property and its utilization. For each category of CRE, the Company has set its requirements for loan to appraised value or purchase price to a level that is below supervisory limits. The Company offers both fixed and floating rate loans. Maturities for CRE loans are generally between five and ten years (with amortization ranging from fifteen to twenty five years and a balloon payment due at maturity), however, SBA and certain other real estate loans that can be sold in the secondary market may be granted for longer maturities.

The CRE owner occupied loan portfolio decreased ($18.3) million, or (3%), to $585.0 million at March 31, 2024, from $603.3 million at March 31, 2023, and increased $1.7 million from $583.3 million at December 31, 2023. CRE non-owner occupied loans increased $187.3 million, or 17%, to $1.27 billion at March 31, 2024, compared to $1.08 billion at March 31, 2023, and increased $14.6 million, or 1%, from $1.26 billion at December 31, 2023. At both March 31, 2024 and December 31, 2023, there was 32% of the CRE loan portfolio was secured by owner-occupied real estate, compared to 36% at March 31, 2023.

During the first quarter of 2024, there were 23 new CRE loans originated totaling $40 million with a weighted average loan-to-value ("LTV") and debt-service coverage ratio ("DSCR") for the non-owner occupied portfolio of 51% and 1.84 times, respectively. The average loan size for all CRE loans at March 31, 2024 was $1.6 million, which was the same as the average loan size for office CRE loans at this date. The Company has personal guarantees on 92% of its CRE portfolio. A substantial portion of the unguaranteed CRE loans were made to credit-worthy non-profit organizations.

Total office exposure (excluding medical/dental offices) in the CRE portfolio was $398 million, including 29 loans totaling approximately $74 million, in San Jose, 17 loans totaling approximately $26 million in San Francisco, and eight loans totaling approximately $16 million, in Oakland, at March 31, 2024. Non-owner occupied CRE with office exposure totaled $311 million at March 31, 2024.

At March 31, 2024, the weighted average LTV and DSCR for the entire non-owner occupied office portfolio were 42.6% and 1.83 times, respectively.

Total medical/dental office exposure in the non-owner occupied CRE portfolio consisted of 14 loans totaling $16.8 million, with a weighted average LTV and DSCR ratio of 46.1% and 2.02 times, respectively, at March 31, 2024.

The following table presents the weighted average LTV and DSCR by collateral type for CRE loans at March 31, 2024:

	CRE - Non-owner Occupied			CRE - Owner Occupied		Total CRE	
Collateral Type	**Outstanding**	**LTV**	**DSCR**	**Outstanding**	**LTV**	**Outstanding**	**LTV**
Industrial	19 %	40.7 %	2.40	33 %	43.7 %	23 %	41.8 %
Retail	25 %	38.8 %	1.99	16 %	47.3 %	23 %	40.3 %
Mixed-Use, Special Purpose and Other	18 %	42.5 %	1.98	35 %	41.1 %	22 %	41.9 %
Office	20 %	42.6 %	1.83	16 %	41.9 %	19 %	42.4 %
Multifamily	18 %	42.8 %	1.93	0 %	0.0 %	13 %	42.8 %
Hotel/Motel	< 1 %	19.7 %	1.88	0 %	0.0 %	< 1 %	19.7 %
Total	100 %	41.2 %	2.03	100 %	43.0 %	100 %	41.7 %

The following table presents the weighted average LTV and DSCR by county for CRE loans at March 31, 2024:

	CRE - Non-owner Occupied			CRE - Owner Occupied		Total CRE	
County	**Outstanding**	**LTV**	**DSCR**	**Outstanding**	**LTV**	**Outstanding**	**LTV**
Alameda	25 %	45.1 %	1.92	18 %	45.0 %	23 %	45.1 %
Contra Costa	7 %	42.5 %	1.76	8 %	48.5 %	7 %	44.3 %
Marin	7 %	46.8 %	1.95	2 %	52.8 %	5 %	47.4 %
Monterey	2 %	44.4 %	1.78	2 %	45.9 %	2 %	44.8 %
Napa	1 %	29.6 %	2.44	1 %	52.7 %	1 %	37.6 %
Out of Area	9 %	43.0 %	2.11	9 %	51.6 %	9 %	45.4 %
San Benito	1 %	35.3 %	2.13	2 %	40.7 %	1 %	37.5 %
San Francisco	9 %	39.0 %	1.75	4 %	38.6 %	8 %	38.9 %
San Mateo	10 %	37.4 %	2.14	15 %	40.1 %	12 %	38.4 %
Santa Clara	24 %	38.2 %	2.25	36 %	40.2 %	27 %	38.9 %
Santa Cruz	2 %	35.7 %	1.87	1 %	46.1 %	2 %	37.5 %
Solano	1 %	32.8 %	2.33	1 %	35.9 %	1 %	33.5 %
Sonoma	2 %	41.3 %	2.23	1 %	38.5 %	2 %	40.8 %
Total	100 %	41.2 %	2.03	100 %	43.0 %	100 %	41.7 %

The Company's land and construction loans are primarily to finance the development and construction of commercial and single family residential properties. The Company utilizes underwriting guidelines to assess the likelihood of repayment from sources such as sale of the property or availability of permanent mortgage financing prior to making the construction loan. Construction loans are provided primarily in our market area, and we have extensive controls for the disbursement process. Land and construction loans decreased ($36.7) million, or (22%), to $129.7 million at March 31, 2024, compared to $166.4 million at March 31, 2023, and decreased ($10.8) million, or (8%), from $140.5 million at December 31, 2023.

The Company makes home equity lines of credit available to its existing customers. Home equity lines of credit are underwritten initially with a maximum 75% loan to value ratio. Home equity lines of credit decreased ($1.7) million, or (1%), to $122.8 million at March 31, 2024, compared to $124.5 million at March 31, 2023, and increased $3.7 million, or 3%, from $119.1 million at December 31, 2023.

Multifamily loans increased $38.1 million, or 16%, to $269.3 million at March 31, 2024, compared to $231.2 million at March 31, 2023, and remained relatively flat from $269.7 million at December 31, 2023.

From time to time the Company has purchased single family residential mortgage loans. Purchases of residential loans have been an attractive alternative for replacing mortgage-backed security paydowns in the investment securities portfolio. Residential mortgage loans decreased ($38.6) million, or (7%), to $490.0 million at March 31, 2024, compared to $528.6 million at March 31, 2023, and decreased ($7.0) million, or (1%) from $497.0 million at December 31, 2023.

Additionally, the Company makes consumer loans for the purpose of financing automobiles, various types of consumer goods, and other personal purposes. Consumer loans generally provide for the monthly payment of principal and interest. Most of the Company's consumer loans are secured by the personal property being purchased or, in the instances of home equity loans or lines of credit, real property. Consumer and other loans decreased ($1.5) million, or (8%), to $16.4 million at March 31, 2024, compared to $17.9 million at March 31, 2023, and decreased ($4.5) million, or (21%) from $20.9 million at December 31, 2023.

With certain exceptions, state chartered banks are permitted to make extensions of credit to any one borrowing entity totaling up to 15% of the bank's capital and reserves for unsecured loans and up to 25% of the bank's capital and reserves for secured loans. For HBC, these lending limits were $111.4 million and $185.6 million at March 31, 2024, respectively.

Loan Maturities

The following table presents the maturity distribution of the Company's loans (excluding loans held-for-sale) as of March 31, 2024. The table shows the distribution of such loans between those loans with predetermined (fixed) interest rates and those with variable (floating) interest rates. Floating rates generally fluctuate with changes in the prime rate as reflected in the Western Edition of The Wall Street Journal. As of March 31, 2024, approximately 26% of the Company's loan portfolio consisted of floating interest rate loans.

	Due in One Year or Less	Over One Year But Less than Five Years	Over Five Years	Total
		(Dollars in thousands)		
Commercial	$ 220,789	$ 188,135	$ 43,307	$ 452,231
Real estate:				
CRE - owner occupied	21,791	158,399	404,841	585,031
CRE - non-owner occupied	19,602	392,488	859,094	1,271,184
Land and construction	102,159	22,040	5,513	129,712
Home equity	7,092	27,146	88,556	122,794
Multifamily	22,560	99,401	147,302	269,263
Residential mortgages	2,128	20,017	467,890	490,035
Consumer and other	10,722	5,570	147	16,439
Loans	$ 406,843	$ 913,196	$ 2,016,650	$ 3,336,689
Loans with variable interest rates	$ 328,683	281,761	272,620	$ 883,064
Loans with fixed interest rates	78,160	631,435	1,744,030	2,453,625
Loans	$ 406,843	$ 913,196	$ 2,016,650	$ 3,336,689

Loan Servicing

As of March 31, 2024 and 2023, SBA loans were serviced by the Company for others totaled $52.9 million and $61.7 million, respectively. Activity for loan servicing rights was as follows:

	Three Months Ended March 31, 2024	Three Months Ended March 31, 2023
	(Dollars in thousands)	
Beginning of period balance	$ 415	$ 549
Additions	41	18
Amortization	(64)	(45)
End of period balance	$ 392	$ 522

Loan servicing rights are included in accrued interest receivable and other assets on the unaudited consolidated balance sheets and reported net of amortization. There was no valuation allowance as of March 31, 2024 and 2023, as the fair value of the assets was greater than the carrying value.

Activity for the I/O strip receivable was as follows:

	Three Months Ended March 31, 2024	Three Months Ended March 31, 2023
	(Dollars in thousands)	
Beginning of period balance	$ 117	$ 152
Unrealized holding loss	(7)	(7)
End of period balance	$ 110	$ 145

Credit Quality and Allowance for Credit Losses on Loans

Like all financial institutions, HBC has exposure to credit quality risk, which generally arises because we could potentially receive less than a full return of principal and interest if a debtor becomes unable or unwilling to repay. Since loans are the Company's most significant assets and generate the largest portion of its revenues, the Company's management of credit quality risk is focused primarily on loan quality. Banks have generally suffered their most severe earnings declines as a result of customers' inability to generate sufficient cash flow to service their debts and/or downturns in national and regional economies and declines in overall asset values, including real estate. In addition, certain debt securities that the Company may purchase have the potential of declining in value if the obligor's financial capacity to repay deteriorates.

The Company's policies and procedures identify market segments, set goals for portfolio growth or contraction, and establish limits on industry and geographic credit concentrations. In addition, these policies establish the Company's underwriting standards and the methods of monitoring ongoing credit quality. The Company's internal credit risk controls are centered in underwriting practices, credit granting procedures, training, risk management techniques, and familiarity with loan customers as well as the relative diversity and geographic concentration of our loan portfolio.

The Company's credit risk also may be affected by external factors such as the level of interest rates, employment, general economic conditions, real estate values, and trends in particular industries or geographic markets. As an independent community bank serving a specific geographic area, the Company must contend with the unpredictable changes in the general California market and, particularly, primary local markets. The Company's asset quality has suffered in the past from the impact of national and regional economic recessions, consumer bankruptcies, and depressed real estate values.

Nonperforming assets are comprised of the following: loans for which the Company is no longer accruing interest; restructured loans which have been current under six months; loans 90 days or more past due and still accruing interest (although they are generally placed on nonaccrual when they become 90 days past due, unless they are both well-secured and in the process of collection); and foreclosed assets. The following tables present the aging of past due loans by class for the periods indicated:

	March 31, 2024					
	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total
	(Dollars in thousands)					
Commercial	$ 3,522	$ 1,180	$ 1,955	$ 6,657	$ 445,574	$ 452,231
Real estate:						
CRE - Owner Occupied	—	—	—	—	585,031	585,031
CRE - Non-Owner Occupied	5,662	—	—	5,662	1,265,522	1,271,184
Land and construction	3,550	—	4,672	8,222	121,490	129,712
Home equity	441	—	—	441	122,353	122,794
Multifamily	—	—	—	—	269,263	269,263
Residential mortgages	—	—	508	508	489,527	490,035
Consumer and other	—	—	—	—	16,439	16,439
Total	$ 13,175	$ 1,180	$ 7,135	$ 21,490	$ 3,315,199	$ 3,336,689

	December 31, 2023					
	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Current	Total
	(Dollars in thousands)					
Commercial	$ 6,688	$ 2,030	$ 1,264	$ 9,982	$ 453,796	$ 463,778
Real estate:						
CRE - Owner Occupied	—	—	—	—	583,253	583,253
CRE - Non-Owner Occupied	1,289	—	—	1,289	1,255,301	1,256,590
Land and construction	955	—	3,706	4,661	135,852	140,513
Home equity	—	—	142	142	118,983	119,125
Multifamily	—	—	—	—	269,734	269,734
Residential mortgages	3,794	510	779	5,083	491,878	496,961
Consumer and other	—	—	—	—	20,919	20,919
Total	$ 12,726	$ 2,540	$ 5,891	$ 21,157	$ 3,329,716	$ 3,350,873

The following table presents the past due loans on nonaccrual and current loans on nonaccrual for the periods indicated:

	March 31, 2024	December 31, 2023
	(Dollars in thousands)	
Past due nonaccrual loans	$ 5,184	$ 12,200
Current nonaccrual loans	736	718
Total nonaccrual loans	$ 5,920	$ 12,918

Management's classification of a loan as "nonaccrual" is an indication that there is reasonable doubt as to the full recovery of principal or interest on the loan. At that point, the Company stops accruing interest income, and reverses any uncollected interest that had been accrued as income. The Company resumes recognizing interest income only as cash interest payments are received and it has been determined the collection of all outstanding principal is not in doubt. The loans may or may not be collateralized, and collection efforts are pursued. Loans may be restructured by management when a borrower has experienced some change in financial status causing an inability to meet the original repayment terms and where the Company believes the borrower will eventually overcome those circumstances and make full restitution. Foreclosed assets consist of properties and other assets acquired by foreclosure or similar means that management is offering or will offer for sale.

There were no foreclosed assets on the balance sheet at March 31, 2024, March 31, 2023, or December 31, 2023. There were no CRE loans, Shared National Credits ("SNCs") or material purchased participations included in NPAs or total loans at March 31, 2024, March 31, 2023, or December 31, 2023.

The following table summarizes the Company's nonperforming assets at the dates indicated:

	March 31, 2024	March 31, 2023	December 31, 2023
	(Dollars in thousands)		
Nonaccrual loans — held-for-investment	$ 5,920	$ 781	$ 6,818
Loans 90 days past due and still accruing	1,951	1,459	889
Total nonperforming loans	7,871	2,240	7,707
Foreclosed assets	—	—	—
Total nonperforming assets	$ 7,871	$ 2,240	$ 7,707
Nonperforming assets as a percentage of loans plus foreclosed assets	0.24 %	0.07 %	0.23 %
Nonperforming assets as a percentage of total assets	0.15 %	0.04 %	0.15 %

The following table presents the amortized cost basis of nonperforming loans and loans past due over 90 days and still accruing at the periods indicated:

	March 31, 2024			
	Nonaccrual with no Special Allowance for Credit Losses	Nonaccrual with Special Allowance for Credit Losses	Loans over 90 Days Past Due and Still Accruing	Total
	(Dollars in thousands)			
Commercial	$ 924	$ 203	$ 1,443	$ 2,570
Real estate:				
CRE - Owner Occupied	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—
Land and construction	4,673	—	—	4,673
Home equity	120	—	—	120
Residential mortgages	—	—	508	508
Total	$ 5,717	$ 203	$ 1,951	$ 7,871

	December 31, 2023			
	Nonaccrual with no Special Allowance for Credit Losses	Nonaccrual with Special Allowance for Credit Losses	Loans over 90 Days Past Due and Still Accruing	Total
	(Dollars in thousands)			
Commercial	$ 946	$ 290	$ 889	$ 2,125
Real estate:				
CRE - Owner Occupied	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—
Land and construction	4,661	—	—	4,661
Home equity	142	—	—	142
Residential mortgages	779	—	—	779
Total	$ 6,528	$ 290	$ 889	$ 7,707

Loans with a well-defined weakness, which are characterized by the distinct possibility that the Company will sustain a loss if the deficiencies are not corrected, are categorized as “classified.” Classified loans include all loans considered as substandard, substandard-nonaccrual, and doubtful and may result from problems specific to a borrower’s business or from economic downturns that affect the borrower’s ability to repay or that cause a decline in the value of the underlying collateral (particularly real estate). Loans held-for-sale are carried at the lower of cost or estimated fair value, and are not allocated an allowance for credit losses.

The amortized cost basis of collateral-dependent commercial loans collateralized by business assets totaled $203,000 and $290,000 at March 31, 2024 and December 31, 2023, respectively.

When management determines that foreclosures are probable, expected credit losses for collateral-dependent loans are based on the fair value of the collateral at the reporting date, adjusted for selling costs as appropriate. For loans for which foreclosure is not probable, but for which repayment is expected to be provided substantially through the operation or sale of the collateral and the borrower is experiencing financial difficulty, management has elected the practical expedient under ASC 326 to estimate expected credit losses based on the fair value of collateral, adjusted for selling costs as appropriate. The class of loan represents the primary collateral type associated with the loan. Significant quarter over quarter changes are reflective of changes in nonaccrual status and not necessarily associated with credit quality indicators like appraisal value.

Classified loans were $35.4 million, or 0.67% of total assets, at March 31, 2024, compared to $26.8 million, or 0.48% of total assets, at March 31, 2023, and $31.8 million, or 0.61% of total assets at December 31, 2023.

In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed in accordance with the Company’s underwriting policy.

The ACLL is calculated by using the current expected credit loss (“CECL”) methodology. The ACLL estimation process involves procedures to appropriately consider the unique characteristics of loan portfolio segments. These segments are further disaggregated into loan classes, the level at which credit risk is monitored. When computing the level of expected credit losses, credit loss assumptions are estimated using a model that categorizes loan pools based on loss history, delinquency status, and other credit trends and risk characteristics, including current conditions and reasonable and supportable forecasts about the future. Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. In future periods, evaluations of the overall loan portfolio in light of the factors and forecasts then prevailing, may result in significant changes in the allowance and credit loss expense in those future periods.

The allowance level is influenced by loan volumes, loan risk rating migration or delinquency status, changes in historical loss experience, and other conditions influencing loss expectations, such as reasonable and supportable forecasts of economic conditions. The methodology for estimating the amount of expected credit losses reported in the allowance for credit losses has two basic components: first, an asset-specific component involving individual loans that do not share risk characteristics with other loans and the measurement of expected credit losses for such individual loans; and second, a pooled component for estimated expected credit losses for pools of loans that share similar risk characteristics.

Loans are charged-off against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance for credit losses on loans.

The following provides a summary of the risks associated with various segments of the Company’s loan portfolio, which are factors management regularly considers when evaluating the adequacy of the allowance:

Commercial

Commercial loans rely primarily on the identified cash flows of the borrower for repayment and secondarily on the value of underlying collateral provided by the borrower. However, the cash flows of the borrowers may not be as expected and the collateral securing these loans may vary in value. Most commercial loans are secured by the assets being financed or on other business assets such as accounts receivable, inventory or equipment and may incorporate a personal guarantee; however, some loans may be unsecured.

CRE

CRE loans rely primarily on the cash flows of the properties securing the loan and secondarily on the value of the property that is securing the loan. CRE loans comprise two segments differentiated by owner occupied CRE and non-owner occupied CRE. Owner occupied CRE loans are secured by commercial properties that are at least 50% occupied by the borrower or borrower affiliate. Although CRE loans often incorporate a personal guarantee, the commercial property collateral is typically sufficient and reliance on personal guarantees is minimal. Non-owner occupied CRE loans are secured by commercial properties that are less than 50% occupied by the borrower or a borrower affiliate. CRE loans may be adversely affected by conditions in the real estate markets or in the general economy.

Land and Construction

Land and construction loans are generally based on estimates of costs and value associated with the complete project. Construction loans usually involve the disbursement of funds with repayment substantially dependent on the success of the completion of the project. Sources of repayment for these loans may be permanent loans from HBC or other lenders, or proceeds from the sales of the completed project. These loans are monitored through on-site inspections and are considered to have higher risk than other real estate loans due to the final repayment dependent on numerous factors including general economic conditions.

Home Equity

Home equity loans are secured by 1-4 family residences that are generally owner occupied. Repayment of these loans depends primarily on the personal income of the borrower and secondarily on the value of the property securing the loan which can be impacted by changes in economic conditions such as the unemployment rate and property values.

Multifamily

Multifamily loans are loans on residential properties with five or more units. These loans rely primarily on the cash flows of the properties securing the loan for repayment and secondarily on the value of the properties securing the loan. The cash flows of these borrowers can fluctuate along with the values of the underlying property depending on general economic conditions.

Residential Mortgages

Residential mortgage loans are secured by 1-4 family residences which are generally owner-occupied. Repayment of these loans depends primarily on the personal income of the borrower and secondarily on the value of the property securing the loan which can be impacted by changes in economic conditions such as the unemployment rate and property values.

Consumer and Other

Consumer and other loans are secured by personal property or are unsecured and rely primarily on the income of the borrower for repayment and secondarily on the collateral value for secured loans. Borrower income and collateral value can vary dependent on economic conditions.

Allocation of Allowance for Credit Losses on Loans

As a result of the matters mentioned above, changes in the financial condition of individual borrowers, economic conditions, historical loss experience and the condition of the various markets in which collateral may be sold may all affect the required level of the allowance for credit losses on loans and the associated provision for credit losses on loans.

On an ongoing basis, we have engaged an outside firm to perform independent credit reviews of our loan portfolio on a sample basis, subject to review by the Federal Reserve Board and the California Department of Financial Protection and Innovation. Based on information currently available, management believes that the allowance for credit losses on loans is adequate. However, the loan portfolio can be adversely affected if economic conditions in general, and the real estate market in the San Francisco Bay Area market in particular, were to weaken further. Also, any weakness of a prolonged nature in the technology industry would have a negative impact on the local market. The effect of such events, although uncertain at this time, could result in an increase in the level of nonperforming loans and increased loan losses, which could adversely affect the Company’s future growth and profitability. No assurance of the ultimate level of credit losses can be given with any certainty.

Changes in the allowance for credit losses on loans were as follows for the periods indicated:

	Three Months Ended March 31, 2024								
	Commercial	CRE Owner Occupied	CRE Non-owner Occupied	Land & Construction	Home Equity	Multi-Family	Residential Mortgages	Consumer and Other	Total
	(Dollars in thousands)								
Beginning of period balance	$ 5,853	$ 5,121	$ 25,323	$ 2,352	$ 644	$ 5,053	$ 3,425	$ 187	$ 47,958
Charge-offs	(358)	—	—	—	—	—	—	—	(358)
Recoveries	82	4	—	—	18	—	—	—	104
Net (charge-offs) recoveries	(276)	4	—	—	18	—	—	—	(254)
Provision for (recapture of) credit losses on loans	(548)	16	1,086	(470)	91	(744)	774	(21)	184
End of period balance	$ 5,029	$ 5,141	$ 26,409	$ 1,882	$ 753	$ 4,309	$ 4,199	$ 166	$ 47,888
Percent of ACLL to Total ACLL at end of period	10%	11%	55%	4%	2%	9%	9%	< 1%	100%

	Three Months Ended March 31, 2023								
	Commercial	CRE Owner Occupied	CRE Non-owner Occupied	Land & Construction	Home Equity	Multi-Family	Residential Mortgages	Consumer and Other	Total
	(Dollars in thousands)								
Beginning of period balance	$ 6,617	$ 5,751	$ 22,135	$ 2,941	$ 666	$ 3,366	$ 5,907	$ 129	$ 47,512
Charge-offs	(134)	—	—	—	(246)	—	—	—	(380)
Recoveries	80	4	—	—	25	—	—	—	109
Net (charge-offs) recoveries	(54)	4	—	—	(221)	—	—	—	(271)
Provision for (recapture of) credit losses on loans	(29)	(302)	542	235	243	1,026	(1,711)	28	32
End of period balance	$ 6,534	$ 5,453	$ 22,677	$ 3,176	$ 688	$ 4,392	$ 4,196	$ 157	$ 47,273
Percent of ACLL to Total ACLL at end of period	14%	12%	48%	7%	1%	9%	9%	< 1%	100%

The following table provides a summary of the allocation of the allowance for credit losses on loans by class at the dates indicated. The allocation presented should not be interpreted as an indication that charges to the allowance for credit losses on loans will be incurred in these amounts or proportions, or that the portion of the allowance allocated to each category represents the total amount available for charge-offs that may occur within these classes.

	March 31, 2024		March 31, 2023		December 31, 2023	
	Allowance	Percent of Loans in each category to total loans	Allowance	Percent of Loans in each category to total loans	Allowance	Percent of Loans in each category to total loans
	(Dollars in thousands)					
Commercial	$ 5,029	14 %	$ 6,534	16 %	$ 5,853	14 %
Real estate:						
CRE - owner occupied	5,141	17 %	5,453	18 %	5,121	17 %
CRE - non-owner occupied	26,409	38 %	22,677	33 %	25,323	37 %
Land and construction	1,882	4 %	3,176	5 %	2,352	4 %
Home equity	753	4 %	688	4 %	644	4 %
Multifamily	4,309	8 %	4,392	7 %	5,053	8 %
Residential mortgages	4,199	15 %	4,196	16 %	3,425	15 %
Consumer and other	166	< 1 %	157	1 %	187	1 %
Total	$ 47,888	100 %	$ 47,273	100 %	$ 47,958	100 %

The ACLL totaled $47.9 million, or 1.44% of total loans at March 31, 2024, compared to $47.3 million, or 1.45% of total loans at March 31, 2023, and $48.0 million, or 1.43% of total loans at December 31, 2023. The decrease in the allowance for credit losses on loans of ($70,000) for the three months ended March 31, 2024, compared to December 31, 2023, was primarily attributed to an increase of $9,000 in the reserve for pooled loans, and a decrease of ($79,000) in specific reserves for individually evaluated loans.

The ACLL was 608.41% of nonperforming loans at March 31, 2024, compared to 2,110.40% of nonperforming loans at March 31, 2023, and 622.27% of nonperforming loans at December 31, 2023. The Company had net charge-offs of $254,000, or 0.03% of average loans, for the first quarter of 2024, compared to net charge-offs of $271,000, or 0.03% of average loans, for the first quarter of 2023, and net charge-offs of $33,000, or less than 0.01% of average loans, for the fourth quarter of 2023.

The following table shows the drivers of change in ACLL for the first quarter of 2024:

	(Dollars in thousands)
ACLL at December 31, 2023	$ 47,958
Portfolio changes during the first quarter of 2024	(234)
Qualitative and quantitative changes during the first quarter of 2024 including changes in economic forecasts	164
ACLL at March 31, 2024	$ 47,888

Leases

The Company recognizes the following for all leases, at the commencement date: (1) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) a right-of-use ("ROU") 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. The Company's lease agreements include options to renew at the Company's discretion. The extensions are not reasonably certain to be exercised, therefore it was not considered in the calculation of the ROU asset and lease liability. Total assets and total liabilities were $30.7 million on its consolidated statement of financial condition at March 31, 2024, as a result of recognizing right-of-use assets, included in other assets, and lease liabilities, included in other liabilities, related to non-cancelable operating lease agreements for office space.

Deposits

The composition and cost of the Company's deposit base are important components in analyzing the Company's net interest margin and balance sheet liquidity characteristics, both of which are discussed in greater detail in other sections herein. The Company's liquidity is impacted by the volatility of deposits from the propensity of that money to leave the institution for rate-related or other reasons. Deposits can be adversely affected if economic conditions weaken in California, and the Company's market area in particular. Potentially, the most volatile deposits in a financial institution are jumbo certificates of deposit, meaning time deposits with balances that equal or exceed $250,000, as customers with balances of that magnitude are typically more rate-sensitive than customers with smaller balances.

The following table summarizes the distribution of deposits and the percentage of distribution in each category of deposits for the periods indicated:

	March 31, 2024		March 31, 2023		December 31, 2023	
	Balance	% to Total	Balance	% to Total	Balance	% to Total
	(Dollars in thousands)					
Demand, noninterest-bearing	$ 1,242,059	28 %	$ 1,469,081	33 %	$ 1,292,486	30 %
Demand, interest-bearing	925,100	21 %	1,196,789	27 %	914,066	21 %
Savings and money market	1,124,900	25 %	1,264,567	28 %	1,087,518	25 %
Time deposits — under $250	38,105	1 %	37,884	1 %	38,055	1 %
Time deposits — $250 and over	200,739	4 %	172,070	4 %	192,228	4 %
ICS/CDARS — interest-bearing demand, money market and time deposits	913,757	21 %	304,147	7 %	854,105	19 %
Total deposits	$ 4,444,660	100 %	$ 4,444,538	100 %	$ 4,378,458	100 %

The Company obtains deposits from a cross-section of the communities it serves. The Company's business is not generally seasonal in nature. Public funds were less than 1% of deposits at March 31, 2024, March 31, 2023, and December 31, 2023.

Total deposits were relatively flat at $4.44 billion at both March 31, 2024 and March 31, 2023. Total deposits increased $66.2 million, or 2%, from $4.38 billion at December 31, 2023. Migration of customer deposits resulted in an increase in ICS/CDARS deposits to $913.8 million at March 31, 2024, compared to $304.1 million at March 31, 2023, and increased $59.7 million from $854.1 million at December 31, 2023. Noninterest-bearing demand deposits decreased ($227.0) million, or (15%), to $1.24 billion at March 31, 2024, compared to $1.47 billion at March 31, 2023, largely in response to the increasing interest rate environment. Noninterest-bearing demand deposits decreased ($50.4) million, or (4%), from $1.29 billion at December 31, 2023.

The Bank had 24,730 deposits accounts at March 31, 2024, with an average balance of $180,000, compared to 24,103 deposit accounts at March 31, 2023, with an average balance of $184,000. At December 31, 2023, the Bank had 24,737 deposit accounts, with an average balance of $177,000.

Deposits from the Bank's top 100 client relationships, representing 22% of total deposits, totaled $2.05 billion, representing 46% of total deposits, with an average account size of $384,000 at March 31, 2024. At March 31, 2023, deposits from the Bank's top 100 client relationships, representing 21% of the total number of accounts, totaled $2.20 billion, representing 50% of total deposits, with an average account size of $445,000. At December 31, 2023, deposits from the Bank's top 100 client relationships, representing 22% of the total number of accounts, totaled $1.96 billion, representing 45% of total deposits, with an average account size of $368,000.

The Bank's uninsured deposits were approximately $2.02 billion, or 45% of the Company's total deposits, at March 31, 2024, compared to $2.56 billion, or 58% of the Company's total deposits, at March 31, 2023, and $2.01 billion, or 46% of the Company's total deposits at December 31, 2023.

At March 31, 2024, the $913.8 million ICS/CDARS deposits comprised $435.7 million of interest-bearing demand deposits, $228.8 million of money market accounts and $249.3 million of time deposits. At March 31, 2023, the $304.1 million ICS/CDARS deposits comprised $241.3 million of interest-bearing demand deposits, $58.3 million of money market accounts and $4.5 million of time deposits. At December 31, 2023, the $854.1 million ICS/CDARS deposits comprised $425.0 million of interest-bearing demand deposits, $189.9 million of money market accounts and $239.2 million of time deposits.

The following table indicates the contractual maturity schedule of the Company's uninsured time deposits in excess of $250,000 as of March 31, 2024:

	Balance	% of Total
	(Dollars in thousands)	
Three months or less	$ 61,475	42 %
Over three months through six months	14,867	10 %
Over six months through twelve months	48,190	33 %
Over twelve months	21,207	15 %
Total	$ 145,739	100 %

The Company focuses primarily on providing and servicing business deposit accounts that are frequently over $250,000 in average balance per account. As a result, certain types of business clients that the Company serves typically carry average deposits in excess of $250,000. The account activity for some account types and client types necessitates appropriate liquidity management practices by the Company to help ensure its ability to fund deposit withdrawals.

Return on Equity and Assets

The following table indicates the ratios for return on average assets and average equity, and average equity to average assets for the periods indicated:

	Three Months Ended March 31,	
	2024	2023
Return on average assets	0.79 %	1.47 %
Return on average tangible assets [1]	0.82 %	1.52 %
Return on average equity	6.08 %	12.03 %
Return on average tangible common equity [1]	8.24 %	16.71 %
Average equity to average assets ratio	12.98 %	12.18 %

(1) This is a non-GAAP financial measure.

Liquidity, Asset/Liability Management and Available Lines of Credit

The Company's liquidity position supports its ability to maintain cash flows sufficient to fund operations, meet all of its financial obligations and commitments, and accommodate unexpected sudden changes in balances of loans and demand for deposits in a timely manner. At various times the Company requires funds to meet short term cash requirements brought about by loan growth or deposit outflows, the purchase of assets, or repayment of liabilities. An integral part of the Company's ability to manage its liquidity position appropriately is derived from its large base of core deposits which are generated by offering traditional banking services in its service area and which have historically been a stable source of funds.

The Company manages liquidity to be able to meet unexpected sudden changes in levels of its assets or deposit liabilities without maintaining excessive amounts of balance sheet liquidity. In order to meet short term liquidity needs the Company utilizes overnight Federal funds purchase arrangements and other borrowing arrangements with correspondent banks, solicits brokered deposits if cost effective deposits are not available from local sources, and maintains collateralized lines of credit with the FHLB and FRB.

The Company monitors its liquidity position and funding strategies on a daily basis, but recognizes that unexpected events, economic or market conditions, earnings issues or situations beyond its control could cause either a short or long term liquidity crisis. The Company has a detailed Contingency Funding Plan that will be used in the event of a "Liquidity Event" defined as a reduction in liquidity such that a normal deposit and liquidity environment cannot meet funding needs. In addition to other tools used to monitor liquidity and funding, the Company prepares liquidity stress scenarios that include lower-probability, higher impact scenarios, with various levels of severity. The liquidity stress scenarios incorporate the impact of moderate risk and higher risk situations, on a quarterly basis, or more often as circumstances require. The liquidity stress scenarios include a dashboard showing key liquidity ratios compared to established target limits and estimated cash flows for the next several quarters.

One of the measures of liquidity is the loan to deposit ratio. The loan to deposit ratio was 75.06% at March 31, 2024, compared to 73.39% at March 31, 2023, and 76.52% at December 31, 2023.

The Company's total liquidity and borrowing capacity was $3.00 billion, all of which remained available at March 31, 2024. The available liquidity and borrowing capacity was 67% of the Company's total deposits and approximately 149% of the Bank's estimated uninsured deposits at March 31, 2024.

HBC has off-balance sheet liquidity in the form of Federal funds purchase arrangements with correspondent banks, and lines of credit from the FHLB and FRB. HBC maintains a collateralized line of credit with the FHLB of San Francisco. Under this line, the Company can borrow from the FHLB on a short-term (typically overnight) or long-term (over one year) basis. HBC can also borrow from the FRB discount window. The following table shows the collateral value of loans and securities pledged for the lines of credit (if collateralized), total available lines of credit, the amounts outstanding, and the remaining available for the periods indicated:

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	March 31, 2024			
	Collateral Value	Total Available	Outstanding	Remaining Available
	(Dollars in thousands)			
FHLB collateralized borrowing capacity	$ 1,569,070	$ 1,097,518	$ —	$ 1,097,518
FRB discount window collateralized line of credit	1,639,038	1,245,362	—	1,245,362
Federal funds purchase arrangements	N/A	90,000	—	90,000
Holding company line of credit	N/A	20,000	—	20,000
	$ 3,208,108	$ 2,452,880	$ —	$ 2,452,880

	December 31, 2023			
	Collateral Value	Total Available	Outstanding	Remaining Available
	(Dollars in thousands)			
FHLB collateralized borrowing capacity	$ 1,600,371	$ 1,100,931	$ —	$ 1,100,931
FRB discount window collateralized line of credit	1,658,642	1,235,573	—	1,235,573
Federal funds purchase arrangements	N/A	90,000	—	90,000
Holding company line of credit	N/A	20,000	—	20,000
Total	$ 3,259,013	$ 2,446,504	$ —	$ 2,446,504

HBC may also utilize securities sold under repurchase agreements to manage our liquidity position. There were no securities sold under agreements to repurchase at March 31, 2024 and December 31, 2023.

Capital Resources

The Company uses a variety of measures to evaluate capital adequacy. Management reviews various capital measurements on a regular basis and takes appropriate action to ensure that such measurements are within established internal and external guidelines. The external guidelines, which are issued by the Federal Reserve and the FDIC, establish a risk adjusted ratio relating capital to different categories of assets and off balance sheet exposures.

On May 11, 2022, the Company completed a private placement offering of $40.0 million aggregate principal amount of its 5.00% fixed-to-floating rate subordinated notes due May 15, 2032 ("Sub Debt due 2032"). The Company used the net proceeds of the Sub Debt due 2032 for general corporate purposes, including the repayment on June 1, 2022 of the Company's $40.0 million aggregate principal amount of 5.25% fixed-to-floating rate subordinated notes due June 1, 2027. The Sub Debt due 2032, net of unamortized issuance costs of $461,000, totaled $39.5 million at March 31, 2024, and qualifies as Tier 2 capital for the Company under the guidelines established by the Federal Reserve Bank.

The following table summarizes risk-based capital, risk-weighted assets, and risk-based capital ratios of the consolidated Company under the Basel III requirements for the periods indicated:

	March 31, 2024	March 31, 2023	December 31, 2023
	(Dollars in thousands)		
Capital components:			
Common Equity Tier 1 capital	$ 513,473	$ 485,738	$ 511,799
Additional Tier 1 capital	—	—	—
Tier 1 Capital	513,473	485,738	511,799
Tier 2 Capital	85,322	81,824	82,572
Total Capital	$ 598,795	$ 567,562	$ 594,371
Risk-weighted assets	$ 3,831,110	$ 3,710,037	$ 3,838,667
Average assets for capital purposes	$ 5,010,331	$ 5,069,944	$ 5,100,600
Capital ratios:			
Total Capital	15.6 %	15.3 %	15.5 %
Tier 1 Capital	13.4 %	13.1 %	13.3 %
Common equity Tier 1 Capital	13.4 %	13.1 %	13.3 %
Tier 1 Leverage(1)	10.2 %	9.6 %	10.0 %

(1) Tier 1 capital divided by quarterly average assets (excluding intangible assets and disallowed deferred tax assets).

The following table summarizes risk based capital, risk-weighted assets, and risk-based capital ratios of HBC under the Basel III requirements for the periods indicated:

	March 31, 2024	March 31, 2023	December 31, 2023
	(Dollars in thousands)		
Capital components:			
Common Equity Tier 1 capital	$ 531,736	$ 502,735	$ 529,836
Additional Tier 1 capital	—	—	—
Tier 1 Capital	531,736	502,735	529,836
Tier 2 Capital	45,783	42,437	43,071
Total Capital	$ 577,519	$ 545,172	$ 572,907
Risk-weighted assets	$ 3,829,097	$ 3,712,417	$ 3,835,419
Average assets for capital purposes	$ 5,006,917	$ 5,068,039	$ 5,097,382
Capital ratios:			
Total Capital	15.1 %	14.7 %	14.9 %
Tier 1 Capital	13.9 %	13.5 %	13.8 %
Common Equity Tier 1 Capital	13.9 %	13.5 %	13.8 %
Tier 1 Leverage(1)	10.6 %	9.9 %	10.4 %

(1) Tier 1 capital divided by quarterly average assets (excluding intangible assets and disallowed deferred tax assets).

The following table presents the applicable well-capitalized regulatory guidelines and the standards for minimum capital adequacy requirements under Basel III and the regulatory guidelines for a “well–capitalized” financial institution under PCA:

	Minimum Regulatory Requirements(1)	Well-capitalized Financial Institution PCA Regulatory Guidelines
Capital ratios:		
Total Capital	10.5 %	10.0 %
Tier 1 Capital	8.5 %	8.0 %
Common equity Tier 1 Capital	7.0 %	6.5 %
Tier 1 Leverage	4.0 %	5.0 %

(1) Includes 2.5% capital conservation buffer, except the leverage capital ratio.

The Basel III capital rules introduced a “capital conservation 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.

At March 31, 2024, the Company’s consolidated capital ratio exceeded regulatory guidelines and HBC’s capital ratios exceed the highest regulatory capital requirement of “well-capitalized” under Basel III prompt corrective action provisions. Quantitative measures established by regulation to help ensure capital adequacy require the Company and HBC to maintain minimum amounts and ratios of total risk-based capital, Tier 1 capital, and common equity Tier 1 (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital to average assets (as defined). Management believes that, as of March 31, 2024, March 31, 2023, and December 31, 2023, the Company and HBC met all capital adequacy guidelines to which they were subject. There are no conditions or events since March 31, 2024, that management believes have changed the categorization of the Company or HBC as well-capitalized.

At March 31, 2024, the Company had total shareholders’ equity of $676.3 million, compared to $647.2 million at March 31, 2023, and $672.9 million at December 31, 2023. At March 31, 2024, total shareholders’ equity included $507.6 million in common stock, $181.3 million in retained earnings, and ($12.6) million of accumulated other comprehensive loss. The book value per share was $11.04 at March 31, 2024, compared to $10.62 at March 31, 2023, and $11.00 at December 31, 2023. The tangible book value per share was $8.17 at March 31, 2024, compared to $7.70 at March 31, 2023, and $8.12 at December 31, 2023. Tangible book value per share is a non-GAAP financial measure.

The following table reflects the components of accumulated other comprehensive loss, net of taxes, for the periods indicated:

Accumulated Other Comprehensive Loss	March 31, 2024	March 31, 2023	December 31, 2023
	(Dollars in thousands)		
Unrealized loss on securities available-for-sale	$ (6,936)	$ (8,924)	$ (7,116)
Split dollar insurance contracts liability	(2,861)	(3,139)	(2,809)
Supplemental executive retirement plan liability	(2,874)	(2,361)	(2,892)
Unrealized gain on interest-only strip from SBA loans	83	107	87
Total accumulated other comprehensive loss	$ (12,588)	$ (14,317)	$ (12,730)

Market Risk

Market risk is the risk of loss of future earnings, fair values, or future cash flows that may result from changes in the price of a financial instrument. The value of a financial instrument may change as a result of changes in interest rates, foreign currency exchange rates, commodity prices, equity prices and other market changes that affect market risk sensitive instruments. Market risk is attributed to all market risk sensitive financial instruments, including securities, loans, deposits and borrowings, as well as the Company’s role as a financial intermediary in customer-related transactions. The objective of market risk management is to avoid excessive exposure of the Company's earnings and equity to loss and to reduce the volatility inherent in certain financial instruments.

Interest Rate Management

The Company's market risk exposure is primarily that of interest rate risk, and it has established policies and procedures to monitor and limit earnings and balance sheet exposure to changes in interest rates. The Company does not engage in the trading of financial instruments, nor does the Company have exposure to currency exchange rates.

The principal objective of interest rate risk management (often referred to as "asset/liability management") is to manage the financial components of the Company in a manner that will optimize the risk/reward equation for earnings and capital in relation to changing interest rates. Interest rate risk is the potential of economic losses due to future interest rate changes. These economic losses can be reflected as a loss of future net interest income and/or a loss of current fair market values. The objective is to measure the effect on net interest income and to adjust the balance sheet to minimize the inherent risk while at the same time maximizing income. Management realizes certain risks are inherent, and that the goal is to identify and manage the risks. Management uses two methodologies to manage interest rate risk: (i) a standard GAP analysis; and (ii) an interest rate shock simulation model.

The planning of asset and liability maturities is an integral part of the management of an institution's net interest margin. To the extent maturities of assets and liabilities do not match in a changing interest rate environment, the net interest margin may change over time. Even with perfectly matched repricing of assets and liabilities, risks remain in the form of prepayment of loans or securities or in the form of delays in the adjustment of rates of interest applying to either earning assets with floating rates or to interest-bearing liabilities.

Interest rate changes do not affect all categories of assets and liabilities equally or at the same time. Varying interest rate environments can create unexpected changes in prepayment levels of assets and liabilities, which may have a significant effect on the net interest margin and are not reflected in the interest sensitivity analysis table. Because of these factors, an interest sensitivity GAP report may not provide a complete assessment of the exposure to changes in interest rates.

The Company uses modeling software for asset/liability management in order to simulate the effects of potential interest rate changes on the Company's net interest margin, and to calculate the estimated fair values of the Company's financial instruments under different interest rate scenarios. The program imports current balances, interest rates, maturity dates and repricing information for individual financial instruments, and incorporates assumptions on the characteristics of embedded options along with pricing and duration for new volumes to project the effects of a given interest rate change on the Company's interest income and interest expense. Rate scenarios consisting of key rate and yield curve projections are run against the Company's investment, loan, deposit and borrowed funds' portfolios. These rate projections can be shocked (an immediate and parallel change in all base rates, up or down) and ramped (an incremental increase or decrease in rates over a specified time period), based on current trends and econometric models or stable economic conditions (unchanged from current actual levels). Critical assumptions in the Company's interest rate risk model, like deposit betas, deposit rate change lags and decay rate assumptions, are reviewed and updated regularly to reflect current market conditions. In 2023, deposit beta assumptions in rising rate scenarios were increased and deposit cost lag assumptions were added.

The following tables set forth the estimated changes in the Company's annual net interest income and economic value of equity that would result from the designated instantaneous parallel shift in interest rates noted, and assuming a flat balance sheet with consistent product mix as of March 31, 2024:

Change in Interest Rates (basis points)	Increase/(Decrease) in Estimated Net Interest Income[1] Amount	Percent
	(Dollars in thousands)	
+400	$ 18,668	10.0 %
+300	$ 13,966	7.5 %
+200	$ 9,297	5.0 %
+100	$ 4,659	2.5 %
0	—	—
−100	$ (6,272)	(3.4)%
−200	$ (14,475)	(7.7)%
−300	$ (24,805)	(13.3)%
−400	$ (40,025)	(21.4)%

Change in Interest Rates (basis points)	Increase/(Decrease) in Estimated Economic Value of Equity[1] Amount	Percent
	(Dollars in thousands)	
+400	$ 104,038	8.6 %
+300	$ 88,095	7.3 %
+200	$ 66,340	5.5 %
+100	$ 37,610	3.1 %
0	—	—
−100	$ (61,930)	(5.1)%
−200	$ (151,250)	(12.5)%
−300	$ (268,857)	(22.2)%
−400	$ (418,343)	(34.5)%

(1) Computations of prospective effects of hypothetical interest rate changes are for illustrative purposes only, are based on numerous assumptions including relative levels of market interest rates, loan prepayments and deposit decay, and should not be relied upon as indicative of actual results. These projections are forward-looking and should be considered in light of the *Cautionary Note Regarding Forward-Looking Statements* on page 3. Actual rates paid on deposits may differ from the hypothetical interest rates modeled due to competitive or market factors, which could reduce any actual impact on net interest income.

As with any method of gauging interest rate risk, there are certain shortcomings inherent to the methodology noted above. The model assumes interest rate changes are instantaneous parallel shifts in the yield curve. In reality, rate changes are rarely instantaneous. The use of the simplifying assumption that short-term and long-term rates change by the same degree may also misstate historic rate patterns, which rarely show parallel yield curve shifts. Further, the model assumes that certain assets and liabilities of similar maturity or period to repricing will react in the same way to changes in rates. In reality, certain types of financial instruments may react in advance of changes in market rates, while the reaction of other types of financial instruments may lag behind the change in general market rates. Additionally, the methodology noted above does not reflect the full impact of annual and lifetime restrictions on changes in rates for certain assets, such as adjustable rate loans. When interest rates change, actual loan prepayments and actual early withdrawals from certificates may deviate significantly from the assumptions used in the model. Finally, this methodology does not measure or reflect the impact that higher rates may have on adjustable-rate loan clients' ability to service their debt. All of these factors are considered in monitoring the Company's exposure to interest rate risk.

RECONCILIATION OF NON-GAAP FINANCIAL MEASURES

The accounting and reporting policies of the Company conform to GAAP in the United States and prevailing practices in the banking industry. However, certain non-GAAP performance measures and ratios are used by management to evaluate and measure the Company's performance. The Company believes these non-GAAP financial measures are common in the banking industry, and may enhance comparability for peer comparison purposes. These non-GAAP financial measures should be supplemental to primary GAAP financial measures and should not be read in isolation or relied upon as a substitute for primary GAAP financial measures.

Management reviews yields on certain asset categories and the net interest margin of the Company on an FTE basis. In this non-GAAP presentation, net interest income is adjusted to reflect tax-exempt interest income on an equivalent before-tax basis using tax rates effective as of the end of the period. This measure ensures comparability of net interest income arising from both taxable and tax-exempt sources. The following table summarizes components of FTE net interest income of the Company for the periods indicated:

	March 31, 2024	March 31, 2023
	(Dollars in thousands)	
Net interest income (GAAP)	$ 40,093	$ 49,258
Tax-equivalent adjustment on securities - exempt from Federal tax	60	66
Net interest income, FTE (non-GAAP)	$ 40,153	$ 49,324
Average balance of total interest earning assets	$ 4,842,279	$ 4,895,009
Net interest margin (annualized net interest income divided by the average balance of total interest earnings assets) (GAAP)	3.33 %	4.08 %
Net interest margin, FTE (annualized net interest income, FTE, divided by the average balance of total interest earnings assets) (non-GAAP)	3.34 %	4.09 %

The efficiency ratio is a non-GAAP financial measure, which is calculated by dividing noninterest expense by total revenue (net interest income plus noninterest income), and measures how much it costs to produce one dollar of revenue. The following table summarizes components of the efficiency ratio of the Company for the periods indicated:

	March 31, 2024	March 31, 2023
	(Dollars in thousands)	
Noninterest expense	$ 27,536	$ 25,401
Net interest income	$ 40,093	$ 49,258
Noninterest income	2,047	2,766
Total revenue	$ 42,140	$ 52,024
Efficiency ratio (noninterest expense divided by total revenue) (non-GAAP)	65.34 %	48.83 %

Management considers the tangible common equity ratio and tangible book value per common share as useful measurements of the Company's equity. The Company references the return on average tangible common equity as a measurement of profitability.

The following table summarizes components of the annualized return on average tangible assets and the annualized return on average tangible common equity for the periods indicated:

	March 31, 2024	March 31, 2023
	(Dollars in thousands)	
Net income	$ 10,166	$ 18,917
Average tangible assets components:		
Average Assets (GAAP)	$ 5,178,636	$ 5,235,506
Less: Goodwill	(167,631)	(167,631)
Less: Other Intangible Assets	(8,408)	(10,812)
Total Average Tangible Assets (non-GAAP)	$ 5,002,597	$ 5,057,063
Annualized return on average tangible assets (non-GAAP)	0.82 %	1.52 %
Average tangible common equity components:		
Average Equity (GAAP)	$ 672,292	$ 637,597
Less: Goodwill	(167,631)	(167,631)
Less: Other Intangible Assets	(8,408)	(10,812)
Total Average Tangible Common Equity (non-GAAP)	$ 496,253	$ 459,154
Annualized return on average tangible common equity (non-GAAP)	8.24 %	16.71 %

The following table summarizes components of the tangible common equity to tangible assets ratio of the Company for the periods indicated:

	March 31, 2024	March 31, 2023	December 31, 2023
		(Dollars in thousands)	
Capital components:			
Total Equity (GAAP)	$ 676,296	$ 647,208	$ 672,901
Less: Preferred Stock	—	—	—
Total Common Equity	676,296	647,208	672,901
Less: Goodwill	(167,631)	(167,631)	(167,631)
Less: Other Intangible Assets	(8,074)	(10,431)	(8,627)
Total Tangible Common Equity (non-GAAP)	$ 500,591	$ 469,146	$ 496,643
Asset components:			
Total Assets (GAAP)	$ 5,256,074	$ 5,536,540	$ 5,194,095
Less: Goodwill	(167,631)	(167,631)	(167,631)
Less: Other Intangible Assets	(8,074)	(10,431)	(8,627)
Total Tangible Assets (non-GAAP)	$ 5,080,369	$ 5,358,478	$ 5,017,837
Tangible common equity / tangible assets (non-GAAP)	9.85 %	8.76 %	9.90 %

The following table summarizes components of the tangible common equity to tangible assets ratio of HBC for the periods indicated:

	March 31, 2024	March 31, 2023	December 31, 2023
		(Dollars in thousands)	
Capital components:			
Total Equity (GAAP)	$ 694,543	$ 664,163	$ 690,918
Less: Preferred Stock	—	—	—
Total Common Equity	694,543	664,163	690,918
Less: Goodwill	(167,631)	(167,631)	(167,631)
Less: Other Intangible Assets	(8,074)	(10,431)	(8,627)
Total Tangible Common Equity (non-GAAP)	$ 518,838	$ 486,101	$ 514,660
Asset components:			
Total Assets (GAAP)	$ 5,254,044	$ 5,538,878	$ 5,190,829
Less: Goodwill	(167,631)	(167,631)	(167,631)
Less: Other Intangible Assets	(8,074)	(10,431)	(8,627)
Total Tangible Assets (non-GAAP)	$ 5,078,339	$ 5,360,816	$ 5,014,571
Tangible common equity / tangible assets (non-GAAP)	10.22 %	9.07 %	10.26 %

The following table summarizes components of the tangible book value per share for the periods indicated:

	March 31, 2024	March 31, 2023	December 31, 2023
		(Dollars in thousands, except per share amounts)	
Capital components:			
Total Equity (GAAP)	$ 676,296	$ 647,208	$ 672,901
Less: Preferred Stock	—	—	—
Total Common Equity	676,296	647,208	672,901
Less: Goodwill	(167,631)	(167,631)	(167,631)
Less: Other Intangible Assets	(8,074)	(10,431)	(8,627)
Total Tangible Common Equity (non-GAAP)	$ 500,591	$ 469,146	$ 496,643
Common shares outstanding at period-end	61,253,625	60,948,607	61,146,835
Tangible book value per share (non-GAAP)	$ 8.17	$ 7.70	$ 8.12

ITEM 3—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information concerning quantitative and qualitative disclosure or market risk called for by Item 305 of Regulation S-K is included under "*Part I, Item 2—Management's Discussion and Analysis of Financial Condition and Results of Operations*" of this Report.

ITEM 4—CONTROLS AND PROCEDURES

Disclosure Control and Procedures

The Company has carried out an evaluation, under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of March 31, 2024. As defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), disclosure controls and procedures are controls and procedures designed to reasonably assure that information required to be disclosed in our reports filed or submitted under the Exchange Act are recorded, processed, summarized and reported on a timely basis. Disclosure controls are also designed to reasonably assure that such information is accumulated and communicated to our management, including the

Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Based upon their evaluation, our Chief Executive Officer and Chief Financial Officer concluded the Company's disclosure controls were effective at March 31, 2024, the period covered by this Report.

During the three months ended March 31, 2024, there were no changes in our internal controls over financial reporting that materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

Part II—OTHER INFORMATION

ITEM 1—LEGAL PROCEEDINGS

We evaluate all claims and lawsuits with respect to their potential merits, our potential defenses and counterclaims, settlement or litigation potential and the expected effect on us. The outcome of any claims or litigation, regardless of the merits, is inherently uncertain. Any claims and other lawsuits, and the disposition of such claims and lawsuits, whether through settlement or litigation, could be time-consuming and expensive to resolve, divert our attention from executing our business plan, result in efforts to enjoin our activities, and lead to attempts by third parties to seek similar claims.

For more information regarding legal proceedings, see Note 13 “Commitments and Loss Contingencies” to the consolidated financial statements.

ITEM 1A—RISK FACTORS

Our business, financial condition and results of operations are subject to various risks, including those discussed below. The risks discussed below are those that we believe are the most significant risks, although additional risks not presently known to us or that we currently deem less significant may also adversely affect our business, financial condition and results of operations, perhaps materially.

Risks Relating to Our Business

Our Business could be adversely affected by unfavorable economic and market conditions.

Our business and operations are sensitive to general business and economic conditions in the United States, generally, and particularly the state of California and our market area, which is situated primarily in the general San Francisco Bay Area. Unfavorable or uncertain economic and market conditions could lead to credit quality concerns related to borrower repayment ability and collateral protection as well as reduced demand for the products and services we offer. These economic conditions can arise suddenly, as did the conditions associated with the COVID-19 pandemic, and the full impact of such conditions can be difficult to predict. In addition, geopolitical and domestic political developments, such as existing and potential trade wars and other events beyond our control, can increase levels of political and economic unpredictability globally and increase the volatility of financial markets.

Concerns about the performance of international economies, especially in Europe and emerging markets, and economic conditions in Asia, can impact the economy and financial markets here in the United States. If the national, regional and local economies experience worsening economic conditions, including declining growth and high levels of unemployment, our growth and profitability could be constrained. Weak economic conditions are characterized by, among other indicators, deflation, inflation, elevated levels of unemployment, fluctuations in debt and equity capital markets, increased delinquencies on mortgage, commercial and consumer loans, residential and commercial real estate price declines, related vacancy rates, and lower home sales and commercial activity. Various market conditions may also negatively affect our operating results. Real estate market conditions directly affect performance of our loans secured by real estate. Debt markets affect the availability of credit, which affects the rates and terms at which we offer loans and leases. Stock market downturns affect businesses’ ability to raise capital and invest in business expansion. Stock market downturns often signal broader economic deterioration and/or a downward trend in business earnings, which adversely affects businesses’ ability to service their debts.

There can be no assurance that economic conditions will improve, and these conditions could worsen. Economic pressure on consumers and uncertainty regarding continuing economic improvement may result in changes in consumer and business spending, borrowing and saving habits. Such conditions could have a material adverse effect on the credit quality of our loans or our business, financial condition and results and operations.

An economic recession or a downturn in various markets could have one or more of the following adverse effects on our business:

- a decrease in the demand for our loan or other products and services offered by us;
- a decrease in our deposit balances due to an overall reduction in customer balances;
- a decrease in the value of our investment securities and loans;
- an increase in the level of nonperforming and classified loans;
- an increase in the provision for credit losses and loan charge-offs;
- a decrease in net interest income derived from our lending and deposit gathering activities;
- a decrease in the Company’s stock price;
- an increase in our operating expenses associated with attending to the effects of the above-listed circumstances; and/or
- a decrease in real estate values or a general decrease in capital available to finance real estate transactions, which could have a negative impact on borrowers’ ability to pay off their loans as they mature.

The COVID-19 pandemic has in the past negatively affected, and future pandemics, epidemics, disease outbreaks and other public health crises could negatively affect, the global and U.S. economies and could harm our business and results of operations, and such effects will depend on future developments, which are highly uncertain and are difficult to predict.

Pandemics, epidemics or disease outbreaks, such as the COVID-19 pandemic, in the U.S. or globally have in the past negatively affected, and could in the future negatively affect, the global and U.S. economies, including by increasing unemployment levels, disrupting supply chains and businesses in many industries, lowering equity market valuations, decreasing liquidity in fixed income markets, and creating significant volatility and disruption in financial markets. Social and governmental reactions to those events have from time to time affected, and may in the future continue to affect, customers’ banking patterns and preferences and their need for liquidity, particularly at times when layoffs, furloughs, and remote working requirements are in effect. The extent to which the COVID-19 pandemic or any future pandemic, epidemic, disease outbreak or other public health crisis could adversely affect our business, financial condition and results of operations, as well as our liquidity and capital profile, and provisions for credit losses, will depend on future developments, which are highly uncertain and cannot be predicted, including the scope and duration of the pandemic, the widespread availability, use and effectiveness of vaccines, actions taken by governmental authorities and other third parties in response to the pandemic and the direct and indirect impact of the pandemic on us, our clients and customers, our service providers and other market participants.

Our profitability is dependent upon the geographic concentration of the markets in which we operate.

We operate primarily in the general San Francisco Bay Area of California in the counties of Alameda, Contra Costa, Marin, San Benito, San Francisco, San Mateo, and Santa Clara and, as a result, our business, financial condition and results of operations are subject to the demand for our products in those areas and is also subject to changes in the economic conditions in those areas. Our success depends upon the business activity, population, income levels, deposits and real estate activity in these markets. Although our subsidiary’s, Bay View Funding, and our customers' business and financial interests may extend well beyond these market areas, adverse economic conditions that affect these market areas could reduce our growth rate, affect the ability of our customers to repay their loans to us and generally affect our business, financial condition and results of operations. Because of our geographic concentration, we are less able than regional or national financial institutions to diversify demand for our products or our credit risks across multiple markets.

Monetary policies and regulations of the Federal Reserve could adversely affect our business, financial condition and results of operations.

In addition to being affected by general economic conditions, our earnings and growth are affected by the policies of the Federal Reserve. An important function of the Federal Reserve is to regulate the money supply and credit conditions. Among the instruments used by the Federal Reserve to implement these objectives are open market purchases and sales of U.S. government securities, adjustments of the discount rate and changes in banks’ reserve requirements against bank deposits. These instruments are used in varying combinations to influence overall economic growth and the distribution of credit, bank loans, investments and deposits. Their use also affects interest rates charged on loans or paid on deposits. The monetary policies and regulations of the Federal Reserve have had a significant effect on the operating results of commercial banks in the past and are expected to continue to do so in the future.

Competition among U.S. banks for customer deposits is intense, may increase the cost of retaining current deposits or procuring new deposits, and may otherwise negatively affect our ability to grow our deposit base.

Competition among U.S. banks for customer deposits is intense, may increase the cost of retaining current deposits or procuring new deposits, and may otherwise negatively affect our ability to grow our deposit base. Maintaining and attracting new deposits is integral to our business and a major decline in deposits or failure to attract deposits in the future, including any such decline or failure related to an increase in interest rates paid by our competitors on interest-bearing accounts, could have an adverse effect on our business, financial conditions and results of operations. Interest-bearing accounts earn interest at rates established by management based on competitive market factors. The demand for the deposit products we offer may also be reduced due to a variety of factors, such as demographic patterns, changes in customer preferences, reductions in consumers' disposable income, regulatory actions that decrease customer access to particular products, or the availability of competing products.

We may not keep pace with the rapid technological developments in the financial services industry. Fraudulent and other illegal activity involving our products, services and systems could adversely affect our financial position and results of operations.

The financial services industry is subject to rapid technological changes, of which we cannot predict the effects on our business. We expect that new services and technologies applicable to our industry will continue to emerge, and these new services and technologies may be superior to, or render obsolete, the technologies we currently utilize in our products and services. These rapid changes increase cybersecurity risks to our Company and our third-party vendors and service providers, including the risk of security breaches, "denial of service" attacks, "hacking" and identity theft. Criminals are using increasingly sophisticated methods to engage in illegal activities, including through the use of deposit account products and customer information and may also see their effectiveness enhanced by the use of artificial intelligence. A single significant incident of fraud, or increases in the overall level of fraud, involving our products and services could result in reputational damage to us. Such damage could reduce the use and acceptance of our products and services or lead to greater regulation that would increase our compliance costs. Fraudulent activity could also result in the imposition of regulatory sanctions, including significant monetary fines, which could adversely affect our business, results of operations and financial condition. To address the challenges that we face with respect to fraudulent activity, we maintain certain risk control policies and procedures, both internally and with respect to our third-party vendors and service providers, that make it more difficult to fraudulently obtain and use our products and services. However, our inability to keep pace with technological changes, including our ability to identify and address cybersecurity risks, may significantly affect our financial position and results of operation.

Risks Related to Our Loans

Because a significant portion of our loan portfolio is comprised of real estate loans, negative changes in the economy affecting real estate values and liquidity could impair the value of collateral securing our real estate loans and result in loan and other losses.

Real estate lending (including commercial, land development and construction, home equity, multifamily, and residential mortgage loans) is a large portion of our loan portfolio. At March 31, 2024, approximately $2.87 billion, or 86% of our loan portfolio, was comprised of loans with real estate as a primary or secondary component of collateral. Included in CRE loans were owner occupied loans of $585.0 million, or 17% of total loans. The real estate securing our loan portfolio is concentrated in California. The market value of real estate can fluctuate significantly in a short period of time as a result of market conditions in the geographic area in which the real estate is located. Real estate values and real estate markets are generally affected by changes in national, regional or local economic conditions, the rate of unemployment, fluctuations in interest rates and the availability of loans to potential purchasers, fluctuations in vacancy rates, changes in tax laws and other governmental statutes, regulations and policies and acts of nature, such as earthquakes and other natural disasters. Adverse changes affecting real estate values and the liquidity of real estate in one or more of our markets could increase the credit risk associated with our loan portfolio, significantly impair the value of property pledged as collateral on loans and affect our ability to sell the collateral upon foreclosure without a loss or additional losses, which would adversely affect profitability. Such declines and losses would have a material adverse effect on our business, financial condition, and results of operations.

Our land and construction development loans are based upon estimates of costs and value associated with the complete project. These estimates may be inaccurate and we may be exposed to more losses on these projects than on other loans.

At March 31, 2024, land and construction loans, (including land acquisition and development loans) totaled $129.7 million or 4% of our portfolio. Of these loans, 16% were comprised of owner occupied and 84% non-owner occupied land and construction loans. These loans involve additional risks because funds are advanced upon the security of the project, which is of uncertain value prior to its completion, and costs may exceed realizable values in declining real estate markets. Because of the uncertainties inherent in estimating construction costs and the realizable market value of the completed project and the effects of governmental regulation of real property, it is relatively difficult to evaluate accurately the total funds required to complete a project and the related loan-to-value ratio. As a result, construction loans often involve the disbursement of substantial funds with repayment dependent, in part, on the success of the ultimate project and the ability of the borrower to sell or lease the property, rather than the ability of the borrower or guarantor to repay principal and interest. If our appraisal of the value of the completed project proves to be overstated or market values or rental rates decline, we may have inadequate security for the repayment of the loan upon completion of project construction. If we are forced to foreclose on a project prior to or at completion due to a default, we may not be able to recover all of the unpaid balance of, and accrued interest on, the loan as well as related foreclosure and holding costs. In addition, we may be required to fund additional amounts to complete the project and may have to hold the property for an unspecified period of time while we attempt to dispose of it.

Increased scrutiny by regulators of commercial real estate concentrations could restrict our activities and impose financial requirements or limits on the conduct of our business.

Banking regulators are giving commercial real estate lending greater scrutiny, and may require banks with higher levels of commercial real estate loans to implement improved underwriting, internal controls, risk management policies and portfolio stress testing, as well as possibly higher levels of allowances for credit losses on loans and capital levels as a result of commercial real estate lending growth and exposures. Therefore, we could be required to raise additional capital or restrict our future growth as a result of our higher level of commercial real estate loans.

Our use of appraisals in deciding whether to make a loan on or secured by real property does not ensure the value of the real property collateral.

In considering whether to make a loan secured by real property we generally require an appraisal of the property. However, an appraisal is only an estimate of the value of the property at the time the appraisal is conducted, and an error in fact or judgment could adversely affect the reliability of an appraisal. In addition, events occurring after the initial appraisal may cause the value of the real estate to decrease. As a result of any of these factors the value of collateral securing a loan may be less than estimated, and if a default occurs, we may not recover the outstanding balance of the loan.

Many of our loans are to commercial borrowers, which may have a higher degree of risk than other types of borrowers.

At March 31, 2024, commercial loans totaled $452.2 million or 14% of our loan portfolio (including SBA loans, SBA Paycheck Protection Program ("PPP") loans, asset-based lending, and factored receivables). Commercial loans represented 16% of our total loan portfolio at March 31, 2023. Commercial loans are often larger and involve greater risks than other types of lending. Because payments on such loans are often dependent on the successful operation or development of the property or business involved, repayment of such loans is often more sensitive than other types of loans to adverse conditions in the real estate market or the general business climate and economy. Accordingly, a downturn in the real estate market and a challenging business and economic environment may increase our risk related to commercial loans, particularly commercial real estate loans. Unlike home mortgage loans, which generally are made on the basis of the borrowers' ability to make repayment from their employment and other income and which are secured by real property whose value tends to be more easily ascertainable, commercial loans typically are made on the basis of the borrowers' ability to make repayment from the cash flow of the commercial venture. Our commercial and industrial loans are primarily made based on the identified cash flow of the borrower and secondarily on the collateral underlying the loans. Most often, collateral consists of accounts receivable, inventory and equipment and may incorporate a personal guarantee. Inventory and equipment may depreciate over time, may be difficult to appraise and may fluctuate in value based on the success of the business. Accounts receivable may be uncollectable. If the cash flow from business operations is reduced, the borrower's ability to repay the loan may be impaired. Vacancy rates can also negatively impact cash flows from business operations. Further, while no specific industry concentration is considered significant, the Company's lending operations are located in the Company's market areas that are dependent on the technology and real estate industries and their supporting companies. Thus, the Company's borrowers and their guarantors could be adversely impacted by a downturn in these sectors of the economy which could further impact the borrowers' ability to repay their loans. Due to the larger average size of each commercial loan as compared with other loans such as residential loans, as well as collateral that is generally less readily-marketable, losses incurred on a small number of commercial loans could have a material adverse effect on our business, financial condition and results of operations.

The small and medium-sized businesses that we lend to may have fewer resources to weather adverse business developments, which may impair a borrower's ability to repay a loan, and such impairment could adversely affect our business, financial condition and results of operation.

We target our business development and marketing strategy primarily to serve the banking and financial services needs of small to medium-sized businesses. These businesses generally have fewer financial resources in terms of capital or borrowing capacity than larger entities, frequently have smaller market shares than their competition, may be more vulnerable to economic downturns, often need substantial additional capital to expand or compete and may experience substantial volatility in operating results, any of which may impair a borrower's ability to repay a loan. In addition, the success of a small and medium-sized business often depends on the management talents and efforts of one or two people or a small group of people, and the death, disability or resignation of one or more of these people could have a material adverse impact on the business and its ability to repay its loan. Negative general economic conditions in our markets where we operate that adversely affect our medium-sized business borrowers may impair the borrower's ability to repay a loan and such impairment could have a material adverse effect on our business, financial condition and results of operation.

We may suffer losses in our loan portfolio despite our underwriting practices.

We mitigate the risks inherent in our loan portfolio by adhering to sound and proven underwriting practices, managed by experienced and knowledgeable credit professionals. These practices include analysis of a borrower's prior credit history, financial statements, tax returns, and cash flow projections, valuations of collateral based on reports of independent appraisers and verifications of liquid assets. Nonetheless, we may incur losses on loans that meet our underwriting criteria, and these losses may exceed the amounts set aside as reserves in our allowance for credit loss.

Risks Related to our SBA Loan Program

Small Business Administration lending is an important part of our business. Our SBA lending program is dependent upon the U.S. federal government, and we face specific risks associated with originating SBA loans.

At March 31, 2024, SBA loans totaled $32.9 million, which are included in the commercial loan portfolio. SBA loans held-for-sale totaled $1.9 million at March 31, 2024. In addition, the Company had $379,000 of SBA PPP loans at March 31, 2024. Our SBA lending program is dependent upon the U.S. federal government. As an approved participant in the SBA Preferred Lender's Program (an "SBA Preferred Lender"), we enable our clients to obtain SBA loans without being subject to the potentially lengthy SBA approval process necessary for lenders that are not SBA Preferred Lenders. The SBA periodically reviews the lending operations of participating lenders to assess, among other things, whether the lender exhibits prudent risk management. When weaknesses are identified, the SBA may request corrective actions or impose enforcement actions, including revocation of the lender's SBA Preferred Lender status. If we lose our status as an SBA Preferred Lender, we may lose some or all of our customers to lenders who are SBA Preferred Lenders, and as a result we could experience a material adverse effect to our financial results. Any changes to the SBA program, including but not limited to changes to the level of guarantee provided by the federal government on SBA loans, changes to program specific rules impacting volume eligibility under the guaranty program, as well as changes to the program amounts authorized by Congress may also have a material adverse effect on our business. In addition, any default by the U.S. government on its obligations or any prolonged government shutdown could, among other things, impede our ability to originate SBA loans or sell such loans in the secondary market, which could have a material adverse effect on our business, financial condition and results of operations.

The SBA's 7(a) Loan Program is the SBA's primary program for helping start-up and existing small businesses, with financing guaranteed for a variety of general business purposes. Generally, we sell the guaranteed portion of our SBA 7(a) loans in the secondary market. These sales result in premium income for us at the time of sale and create a stream of future servicing income, as we retain the servicing rights to these loans. For the reasons described above, we may not be able to continue originating these loans or sell them in the secondary market. Furthermore, even if we are able to continue to originate and sell SBA 7(a) loans in the secondary market, we might not continue to realize premiums upon the sale of the guaranteed portion of these loans or the premiums may decline due to economic and competitive factors. When we originate SBA loans, we incur credit risk on the non-guaranteed portion of the loans, and if a customer defaults on a loan, we share any loss and recovery related to the loan pro-rata with the SBA. If the SBA establishes that a loss on an SBA guaranteed loan is attributable to significant technical deficiencies in the manner in which the loan was originated, funded or serviced by us, the SBA may seek recovery of the principal loss related to the deficiency from us. Generally, we do not maintain reserves or loss allowances for such potential claims and any such claims could materially adversely affect our business, financial condition and results of operations.

In addition, the Company's SBA loans include loans under the U.S. Department of Agriculture guaranteed lending programs.

The laws, regulations and standard operating procedures that are applicable to SBA loan products may change in the future. We cannot predict the effects of these changes on our business and profitability. Because government regulation greatly affects the business and financial results of all commercial banks and bank holding companies and especially our organization, changes in the laws, regulations and procedures applicable to SBA loans could adversely affect our ability to operate profitably.

The recognition of gains on the sale of loans and servicing asset valuations reflect certain assumptions.

We expect that gains on the sale of U.S. government guaranteed loans will contribute to noninterest income. The gains on such sales recognized for the three months ended March 31, 2024 was $178,000. The determination of these gains is based on assumptions regarding the value of unguaranteed loans retained, servicing rights retained and deferred fees and costs, and net premiums paid by purchasers of the guaranteed portions of U.S. government guaranteed loans. The value of retained unguaranteed loans and servicing rights are determined based on market derived factors such as prepayment rates, current market conditions and recent loan sales. Deferred fees and costs are determined using internal analysis of the cost to originate loans. Significant errors in assumptions used to compute gains on sale of loans or servicing asset valuations could result in material revenue misstatements, which may have a material adverse effect on our business, financial condition and results of operations.

We originated $8.9 million of SBA loans for the three months ended March 31, 2024. We sold $1.8 million of the guaranteed portion of our SBA loans for the three months ended March 31, 2024. We generally retain the non-guaranteed portions of the SBA loans that we originate. Consequently, as of March 31, 2024, we held $34.8 million of SBA loans (including loans held-for-sale) on our balance sheet, $20.2 million of which consisted of the non-guaranteed portion of SBA loans, and $14.6 million of which consisted of the guaranteed portion of SBA loans. At March 31, 2024,

$1.9 million, or 5.6%, consisted of the guaranteed portion of SBA loans which we intend to sell in 2024. The non-guaranteed portion of SBA loans have a higher degree of credit risk and risk of loss as compared to the guaranteed portion of such loans and make up a substantial majority of our remaining SBA loans.

When we sell the guaranteed portion of SBA loans in the ordinary course of business, we are required to make certain representations and warranties to the purchaser about the SBA loans and the manner in which they were originated. Under these agreements, we may be required to repurchase the guaranteed portion of the SBA loan if we have breached any of these representations or warranties, in which case we may record a loss. In addition, if repurchase and indemnity demands increase on loans that we sell from our portfolios, our liquidity, results of operations and financial condition could be adversely affected. Further, we generally retain the non-guaranteed portions of the SBA loans that we originate and sell, and to the extent the borrowers of such loans experience financial difficulties, our financial condition and results of operations could be adversely impacted.

Risks Related to our Credit Quality

Our business depends on our ability to successfully manage credit risk.

The operation of our business requires us to manage credit risk. As a lender, we are exposed to the risk that our borrowers will be unable to repay their loans according to their terms, and that the collateral securing repayment of their loans, if any, may not be sufficient to ensure repayment. In addition, there are risks inherent in making any loan, including risks with respect to the period of time over which the loan may be repaid, risks relating to proper loan underwriting, risks resulting from changes in economic and industry conditions and risks inherent in dealing with individual borrowers. In order to successfully manage credit risk, we must, among other things, maintain disciplined and prudent underwriting standards and ensure that our bankers follow those standards. The weakening of these standards for any reason, a lack of discipline or diligence by our employees in underwriting and monitoring loans, the inability of our employees to adequately adapt policies and procedures to changes in economic or any other conditions affecting borrowers and the quality of our loan portfolio, may result in loan defaults, foreclosures and additional charge-offs and may necessitate that we significantly increase our allowance for credit losses on loans, each of which could adversely affect our net income. As a result, our inability to successfully manage credit risk could have a material adverse effect on our business, financial condition and results of operations.

Our allowance for credit losses on loans may prove to be insufficient to absorb potential losses in our loan portfolio.

We maintain an allowance for credit losses on loans to provide for loan defaults and non-performance. This allowance, expressed as a percentage of loans, was 1.44%, at March 31, 2024. Allowance for credit losses on loans is funded from a provision for credit losses on loans, which is a charge to our income statement. The Company had a provision for credit losses on loans of $184,000 for the first quarter ended March 31, 2024. The allowance for credit losses on loans reflects our estimate of the current expected credit losses in our loan portfolio at the relevant balance sheet date. Our allowance for credit losses on loans is based on our prior experience, as well as an evaluation of the known risks in the current portfolio, composition and growth of the loan portfolio and economic forecasts for correlated economic factors. The determination of an appropriate level of allowance for credit losses on loans is an inherently difficult and subjective process, requiring complex judgments, and is based on numerous analytical assumptions. The amount of future losses is susceptible to changes in economic and other conditions, including changes in interest rates, changes in economic forecasts, changes in the financial condition of borrowers, and deteriorating values of collateral that may be beyond our control, and these losses may exceed current estimates. The allowance is only an estimate of the probable incurred losses in the loan portfolio and may not represent actual over time, either of losses in excess of the allowance or of losses less than the allowance.

In addition, we evaluate all loans identified as individually evaluated loans and allocate an allowance based upon our estimation of the potential loss associated with those problem loans. While we strive to carefully manage and monitor credit quality and to identify loans that may be deteriorating, at any time there are loans included in the portfolio that may result in losses, but that have not yet been identified as nonperforming or potential problem loans. Through established credit practices, we attempt to identify deteriorating loans and adjust the allowance for credit losses on loans accordingly. However, because future events are uncertain and because we may not successfully identify all deteriorating loans in a timely manner, there may be loans that deteriorate in an accelerated time frame. We cannot be sure that we will be able to identify deteriorating loans before they become nonperforming assets, or that we will be able to limit losses on those loans that have been so identified.

Although management believes that the allowance for credit losses on loans is adequate to absorb losses on any existing loans that may become uncollectible, we may be required to take additional provisions for credit losses on loans in the future to further supplement the allowance for credit losses on loans, either due to management's decision to do so or because our banking regulators require us to do so. Our bank regulatory agencies will periodically review our allowance for credit losses on loans and the value attributed to nonaccrual loans or to real estate acquired through foreclosure and may require us to adjust our determination of the value for these items. If our allowance for credit losses on loans is inaccurate, for any of the reasons discussed above (or other reasons), and is inadequate to cover the loan losses that we actually experience, the resulting losses could have a material adverse effect on our business, financial condition and results of operations.

Nonperforming assets adversely affect our results of operations and financial condition, and take significant time to resolve.

As of March 31, 2024, our nonperforming loans (which consist of nonaccrual loans, loans past due 90 days or more and still accruing interest) totaled $7.9 million, or 0.24% of our loan portfolio, and our nonperforming assets (which include nonperforming loans plus other real estate owned) also totaled $7.9 million, or 0.15% of total assets.

Our nonperforming assets adversely affect our net income in various ways. We do not record interest income on nonaccrual loans or other real estate owned, thereby adversely affecting our net interest income, net income and returns on assets and equity, and our loan administration costs increase, which together with reduced interest income adversely affects our efficiency ratio. Further, when we place a loan on nonaccrual status, we reverse any accrued but unpaid interest receivable, which decreases interest income. Subsequently, we continue to have a cost to fund the loan, which is reflected as interest expense, without any interest income to offset the associated funding expense. When we take collateral in foreclosure and similar proceedings, we are required to mark the collateral to its then-fair market value, which may result in a loss. These nonperforming loans and other real estate owned also increase our risk profile and the level of capital our regulators believe is appropriate for us to maintain in light of such risks. The resolution of nonperforming assets requires significant time commitments from management and can be detrimental to the performance of their other responsibilities. If we experience increases in nonperforming loans and nonperforming assets, our net interest income may be negatively impacted and our loan administration costs could increase, each of which could have a material adverse effect on our business, financial condition and results of operations.

Real estate market volatility and future changes in our disposition strategies could result in net proceeds that differ significantly from our other real estate owned fair value appraisals.

As of March 31, 2024 we had no other real estate owned ("OREO") on our financial statements, but in the ordinary course of our business we expect to hold some level of OREO from time to time. OREO typically consists of properties that we obtain through foreclosure or through an in-substance foreclosure in satisfaction of an outstanding loan. OREO properties are valued on our books at the lesser of the recorded investment in the loan for which the property previously served as collateral or the property's "fair value," which represents the estimated sales price of the property on the date acquired less estimated selling costs. Generally, in determining "fair value," an orderly disposition of the property is assumed, unless a different disposition strategy is expected. Significant judgment is required in estimating the fair value of OREO property, and the period of time within which such estimates can be considered current is significantly shortened during periods of market volatility.

In response to market conditions and other economic factors, we may utilize alternative sale strategies other than orderly disposition as part of our OREO disposition strategy, such as immediate liquidation sales. In this event, as a result of the significant judgments required in estimating fair value and the variables involved in different methods of disposition, the net proceeds realized from such sales transactions could differ significantly from the appraisals, comparable sales and other estimates used to determine the fair value of our OREO properties.

We could be exposed to risk of environmental liabilities with respect to properties to which we take title.

In the course of our business, we may foreclose and take title to real estate, and could be subject to environmental liabilities with respect to these properties. We may be held liable to a governmental entity or to third-parties for property damage, personal injury, investigation and clean-up costs incurred by these parties in connection with environmental contamination, or may be required to investigate or clean up hazardous or toxic substances, or chemical releases at a property. The costs associated with investigation or remediation activities could be substantial. In addition, if we are the owner or former owner of a contaminated site, we may be subject to common law claims by third-parties based on damages and costs resulting from environmental contamination emanating from the property. Significant environmental liabilities could have a material adverse effect on our business, financial condition, and results of operations.

Risks Related to Our Growth Strategy

We face risks related to any future acquisitions we may make.

We plan to continue to grow our business organically. However, from time to time, we may consider opportunistic strategic acquisitions that we believe support our long-term business strategy. We face significant competition from numerous other financial services institutions, many of which will have greater financial resources than we do, when considering acquisition opportunities. Accordingly, attractive acquisition opportunities may not be available to us. We may not be successful in identifying or completing any future acquisitions, and we may incur expenses as a result of seeking these opportunities regardless of whether they are consummated. Acquisitions of financial institutions involve operational risks and uncertainties and acquired companies may have unforeseen liabilities, exposure to asset quality problems, key employee and customer retention problems and other problems that could negatively affect our organization.

If we complete any future acquisitions, we may not be able to successfully integrate the operations, management, products and services of the entities that we acquire and eliminate redundancies. The integration process could result in the loss of key employees or disruption of the combined entity's ongoing business or inconsistencies in standards, controls, procedures, and policies that adversely affect our ability to maintain relationships with customers and employees or achieve the anticipated benefits of the transaction. The integration process may also require significant time and attention from our management that they would otherwise direct at servicing existing business and developing new business. We may not be able to realize any projected cost savings, synergies or other benefits associated with any such acquisition we complete. We cannot determine all potential events, facts and circumstances that could result in loss and our investigation or mitigation efforts may be insufficient to protect against any such loss.

In addition, we must generally satisfy a number of meaningful conditions prior to completing any acquisition, including, in certain cases, federal and state bank regulatory approval. Bank regulators consider a number of factors when determining whether to approve a proposed transaction, including the effect of the transaction on financial stability and the ratings and compliance history of all institutions involved, including the Community Reinvestment Act, examination results and anti-money laundering and Bank Secrecy Act compliance records of all institutions involved. The process for obtaining required regulatory approvals has become substantially more difficult, which could affect our future business. We may fail to pursue, evaluate or complete strategic and competitively significant business opportunities as a result of our inability, or our perceived inability, to obtain any required regulatory approvals in a timely manner or at all.

Issuing additional shares of our common stock to acquire other banks and bank holding companies may result in dilution for existing shareholders and may adversely affect the market price of our stock.

In connection with our growth strategy, we have issued, and may issue in the future, shares of our common stock to acquire additional banks or bank holding companies that may complement our organizational structure. Resales of substantial amounts of common stock in the public market and the potential of such sales could adversely affect the prevailing market price of our common stock and impair our ability to raise additional capital through the sale of equity securities. We sometimes must pay an acquisition premium above the fair market value of acquired assets for the acquisition of banks or bank holding companies. Paying this acquisition premium, in addition to the dilutive effect of issuing additional shares, may also adversely affect the prevailing market price of our common stock.

If the goodwill that we recorded in connection with a business acquisition becomes impaired, it could require charges to earnings, which would have a negative impact on our financial condition and results of operations.

Goodwill represents the amount by which the cost of an acquisition exceeded the fair value of net assets we acquired in connection with the purchase. At March 31, 2024, our acquisition-related goodwill as reflected on our balance sheet was $167.6 million. We review goodwill for impairment at least annually, or more frequently if events or changes in circumstances indicate that the carrying value of the asset might be impaired. We determine impairment by comparing the implied fair value of the reporting unit goodwill with the carrying amount of that goodwill. Estimates of fair value are determined based on a complex model using cash flows, the fair value of our Company as determined by our stock price, and company comparisons. If management's estimates of future cash flows are inaccurate, fair value determined could be inaccurate and impairment may not be recognized in a timely manner. If the carrying amount of the reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. Any such adjustments are reflected in our results of operations in the periods in which they become known. There can be no assurance that our future evaluations of goodwill will not result in findings of impairment and related write-downs, which may have a material adverse effect on our financial condition and results of operations.

Our decisions regarding the fair value of assets acquired could be different than initially estimated, which could materially and adversely affect our business, financial condition and results of operations.

In business combinations, we acquire significant portfolios of loans that are marked to their estimated fair value. There is no assurance that the acquired loans will not suffer deterioration in value. The fluctuations in national, regional and local economic conditions, including those related to local residential, commercial real estate and construction markets, may increase the level of charge offs in the loan portfolio that we acquire and correspondingly reduce our net income. These fluctuations are not predictable, cannot be controlled and may have a material adverse effect on our business, financial condition, and results of operations.

We must effectively manage our branch growth strategy.

We seek to expand our franchise safely and consistently. A successful growth strategy requires us to manage multiple aspects of our business simultaneously, such as following adequate loan underwriting standards, balancing loan and deposit growth without increasing interest rate risk or compressing our net interest margin, maintaining sufficient capital, maintaining proper system and controls, and recruiting, training and retaining qualified professionals. We also may experience a lag in profitability associated with new branch openings. As part of our general growth strategy we may expand into additional communities or attempt to strengthen our position in our current markets by opening new offices, subject to any regulatory constraints on our ability to open new offices. To the extent that we are able to open additional offices, we are likely to experience the effects of higher operating expenses relative to operating income from the new operations for a period of time which could have a material adverse effect on our business, financial condition and results of operations.

New lines of business or new products and services may subject us to additional risks.

From time to time, we may implement or may acquire new lines of business or offer new products and services within existing lines of business. There are substantial risks and uncertainties associated with these efforts, particularly in instances where the markets are not fully developed. In developing and marketing new lines of business and new products and services we may invest significant time and resources. We may not achieve target timetables for the introduction and development of new lines of business and new products or services and price and profitability targets may not prove feasible. External factors, such as regulatory compliance obligations, competitive alternatives, and shifting market preferences, may also impact the successful implementation of a new line of business or a new product or service. Furthermore, any new line of business and/or new product or service could have a significant impact on the effectiveness of our system of internal controls. Failure to successfully manage these risks in the development and implementation of new lines of business or new products or services could have a material adverse effect on our business, financial condition and results of operations.

Risks Related to Our Financial Strength and Liquidity

An actual or perceived reduction in our financial strength may cause others to reduce or cease doing business with us, which could result in a decrease in our net interest income and fee revenues.

Our customers rely upon our financial strength and stability and evaluate the risks of doing business with us. If we experience diminished financial strength or stability, actual or perceived, including due to market or regulatory developments, announced or rumored business developments or results of operations, or a decline in stock price, customers may withdraw their deposits or otherwise seek services from other banking institutions and prospective customers may select other service providers. The risk that we may be perceived as less creditworthy relative to other market participants is increased in the current market environment, where the consolidation of financial institutions, including major global financial institutions, is resulting in a smaller number of much larger counterparties and competitors. If customers reduce their deposits with us or select other service providers for all or a portion of the services that we provide them, net interest income and fee revenues will decrease accordingly, and could have a material adverse effect on our results of operations.

Increasing challenges in credit markets and the effects on our current and future borrowers have adversely affected, and in the future may adversely affect, our loan portfolio and may result in losses or increasing provision expense.

From early-2022 to mid-2023, partially as a response to inflation in the U.S. and global economies, the Federal Reserve began tightening a years-long series of economic stimulus measures that had included historically low interest rates. As those measures were reversed, the Federal Reserve Open Markets committee increased benchmark interest rates from near zero to more than five percent in less than two years. These increases have had a variety of significant impacts, among them a substantial and rapid increase in the interest paid on variable-rate loans. These effects have included a significant reduction in borrowing on existing lines of credit by corporate and individual customers that have the ability to limit increasing indebtedness, and a reduction in the volume of new loans (each of which has the effect of reducing our interest-earning assets), as well as an increase in delinquencies and classified loans (which requires us to increase our reserves for loan and leases losses and increases our collection costs). These increases also effectively reduce demand for loans that we would typically originate and hold for resale, thus reducing our noninterest income. If rates continue increasing, or if they remain at relatively elevated levels for prolonged periods, our borrowers may experience increasing difficulty in repaying their loans.

If these trends continue, or if economic conditions affecting our borrowers worsen, our allowance for credit losses and related provision could be negatively impacted, which would result in a reduction in net income for the corresponding period, or in some cases we may experience losses in excess of established reserves, which would have a similar effect. These outcomes, alone or in combination with other factors, may have a material adverse effect on our results of operations.

Fluctuations in interest rates may reduce net interest income and otherwise negatively affect our business, financial condition and results of operations.

Shifts in short-term interest rates may reduce net interest income, which is the principal component of our earnings. Net interest income is the difference between the amounts received by us on our interest-earning assets and the interest paid by us on our interest-bearing liabilities. When interest rates rise, the rate of interest we receive on our assets, such as floating interest rate loans, rises more quickly than the rate of interest that we pay on our interest-bearing liabilities, such as deposits, which may cause our profits to increase. When interest rates decrease, the rate of interest we receive on our assets, such as floating interest rate loans, declines more quickly than the rate of interest that we pay on our interest-bearing liabilities, such as deposits, which may cause our profits to decrease.

Changes in interest rates could influence our ability to originate loans and deposits. Historically, there has been an inverse correlation between the demand for loans and interest rates. Loan origination volume usually declines during periods of rising or high interest rates and increases during periods of declining or low interest rates.

Changes in interest rates can also affect the level of loan refinancing activity, which impacts the amount of prepayment penalty income we receive on loans we hold. Because prepayment penalties are recorded as interest income when received, the extent to which they increase or decrease during any given period could have a significant impact on the level of net interest income and net income we generate during that time. A decrease in our prepayment penalty income resulting from any change in interest rates or as a result of regulatory limitations on our ability to charge prepayment penalties could therefore adversely affect our net interest income, net income or results of operations.

An increase in interest rates that adversely affects the ability of borrowers to pay the principal or interest on loans may lead to an increase in nonperforming assets and a reduction of income recognized, which could have a material adverse effect on our results of operations and cash flows. Further, when we place a loan on nonaccrual status, we reverse any accrued but unpaid interest receivable, which decreases interest income. Subsequently, we continue to have a cost to fund the loan, which is reflected as interest expense, without any interest income to offset the associated funding expense. Thus, an increase in the amount of nonperforming assets would have an adverse impact on net interest income.

Changes in interest rates also can affect the value of loans, securities and other assets. Rising interest rates will result in a decline in value of the fixed-rate debt securities we hold in our investment securities portfolio. The unrealized losses resulting from holding these securities would be recognized in accumulated other comprehensive income and reduce total shareholders' equity. Unrealized losses do not negatively impact our regulatory capital ratios. However, tangible common equity and the associated ratios would be reduced. If debt securities in an unrealized loss position are sold, such losses become realized and will reduce our regulatory capital ratios.

Rising interest rates have decreased the value of a portion of the Company's securities portfolio, and the Company would realize losses if it were required to sell such securities to meet liquidity needs.

As of March 31, 2024, the fair value of our securities portfolio was approximately $947.3 million. Fixed-rate securities acquired by us are generally subject to decreases in market value when interest rates rise. As a result of inflationary pressures and other general economic conditions, the Federal Open Market Committee of the Board of Governors of the Federal Reserve System has rapidly and significantly increased interest rates over the last two years. When interest rates increase, fixed-rate investment securities and loans held for sale tend to decline in value, because investors can often place funds in higher-yielding instruments rather than purchasing debt securities that have a yield that is lower than those earning at a newly-increased market interest rate. These fluctuations have in the past resulted in declines, and in the future may cause further declines, in the carrying value of our available-for-sale securities portfolio and our portfolio of fixed rate loans, as well as the value of securities pledged as collateral for certain borrowing lines. These trends can be exacerbated if the Company were required to sell such securities to meet liquidity needs, including in the event of deposit outflows or slower deposit growth.

Additional factors beyond our control can further significantly influence the fair value of securities in our portfolio and can cause potential adverse changes to the fair value of these securities. Additional factors include, but are not limited to, rating agency downgrades of the securities or our own analysis of the value of the security, defaults by the issuer or individual mortgagors with respect to the underlying securities, and continued instability in the credit markets. Any of the foregoing factors could cause credit-related impairment in future periods and result in realized losses. The process for determining whether impairment is credit related usually requires difficult, subjective judgments about the future financial performance of the issuer and any collateral underlying the security in order to assess the probability of receiving all contractual principal and interest payments on the security. Because of changing economic and market conditions affecting interest rates, we may recognize realized and/or unrealized losses in future periods, which could have a material adverse effect on our business, financial condition and results of operations.

Adverse changes to our credit ratings could limit our access to funding and increase our borrowing costs.

Credit ratings are subject to ongoing review by rating agencies, which consider a number of factors, including our financial strength, performance, prospects and operations as well as factors not under our control. Other factors that influence our credit ratings include changes to the rating agencies' methodologies for our industry or certain security types; the rating agencies' assessment of the general operating environment for financial services companies; our relative positions in the markets in which we compete; our various risk exposures and risk management policies and activities; pending litigation and other contingencies; our reputation; our liquidity position, diversity of funding sources and funding costs; the current and expected level and volatility of our earnings; our capital position and capital management practices; our corporate governance; current or future regulatory and legislative initiatives; and the agencies' views on whether the U.S. government would provide meaningful support to us or our subsidiaries in a crisis. Rating agencies could make adjustments to our credit ratings at any time, and there can be no assurance that they will maintain our ratings at current levels or that downgrades will not occur.

Any downgrade in our credit ratings could potentially adversely affect the cost and other terms upon which we are able to borrow or obtain funding, increase our cost of capital and/or limit our access to capital markets. Credit rating downgrades or negative watch warnings could negatively impact our reputation with lenders, investors and other third parties, which could also impair our ability to compete in certain markets or engage in certain transactions. In particular, holders of deposits may perceive such a downgrade or warning negatively and withdraw all or a portion of such deposits. While certain aspects of a credit rating downgrade are quantifiable, the impact that such a downgrade would have on our liquidity, business and results of operations in future periods is inherently uncertain and would depend on a number of interrelated factors, including, among other things, the magnitude of the downgrade, the rating relative to peers, the rating assigned by the relevant agency pre-downgrade, individual client behavior and future mitigating actions we might take.

Liquidity risks could affect operations and jeopardize our business, financial condition, and results of operations.

Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, the sale of loans and/or investment securities, and from other sources could have a substantial negative effect on our liquidity. Our most important source of funds consists of our customer deposits. The composition of our deposit base, and particularly the extent to which our deposits are not federally insured, may present a heightened risk of withdrawal. Such deposit balances can decrease during periods of economic uncertainty or when customers perceive alternative investments are providing a better risk/return tradeoff. Our measures to mitigate these risks, including correspondent deposit relationships, may not be completely effective in retaining and reassuring customers about their deposits and may increase the costs of maintaining those deposits. Further, significant economic fluctuations, or customers' expectations about such events (whether or not those expectations materialize) may exacerbate depositors' sensitivity to the availability of cash to fund immediate withdrawals. If customers move money out of bank deposits and into other investments, we could face a material decrease in the volume of our deposits and lose a relatively low cost source of funds, thereby increasing our funding costs and reducing net interest income and net income. We could have to raise interest rates to retain deposits, thereby increasing our funding costs and reducing net interest income and net income.

Additional liquidity is provided by our ability to borrow from the Federal Reserve Bank of San Francisco and the Federal Home Loan Bank of San Francisco. We also may borrow from third-party lenders from time to time. Our access to funding sources in amounts adequate to finance or capitalize our activities on terms that are acceptable to us could be impaired by factors that affect us directly or the financial services industry or economy in general, such as disruptions in the financial markets or negative views and expectations about the prospects for the financial services industry.

Any decline in available funding could adversely impact our ability to continue to implement our strategic plan, including our ability to originate loans, invest in securities, meet our expenses, or to fulfill obligations such as repaying our borrowings or meeting deposit withdrawal demands, any of which could have a material adverse effect on our liquidity, business, financial condition and results of operations.

Risks Related to Our Capital

We may be subject to more stringent capital requirements in the future.

We are subject to current and changing regulatory requirements specifying minimum amounts and types of capital that we must maintain. The failure to meet applicable regulatory capital requirements could result in one or more of our regulators placing limitations or conditions on our activities, including our growth initiatives, or restricting the commencement of new activities, and could affect customer and investor confidence, our costs of funds and Federal Deposit Insurance Corporation ("FDIC") insurance costs, our ability to pay dividends on our common stock, our ability to make acquisitions, and could materially adversely affect our business, financial condition and results of operations.

We may need to raise additional capital in the future, and if we fail to maintain sufficient capital, whether due to losses, an inability to raise additional capital or otherwise, our financial condition, liquidity and results of operations, as well as our ability to maintain regulatory compliance, would be adversely affected.

We face significant capital and other regulatory requirements as a financial institution. 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 needs, which could include the possibility of financing acquisitions. Our ability to raise additional capital depends on conditions in the capital markets, economic conditions and a number of other factors, including investor perceptions regarding the banking industry, market conditions and governmental activities, and on our financial condition and performance. 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. We, therefore, may not be able to raise additional capital if needed or on terms acceptable to us.

Risks Related to our Management

We are highly dependent on our management team, and the loss of our senior executive officers or other key employees could harm our ability to implement our strategic plan, impair our relationships with customers and adversely affect our business, financial condition and results of operations.

Our success depends, in large degree, on the skills of our management team and our ability to retain, recruit and motivate key officers and employees. Our senior management team has significant industry experience, and their knowledge and relationships would be difficult to replace. Leadership changes will occur from time to time, and we cannot predict whether significant resignations will occur or whether we will be able to recruit additional qualified personnel. Competition for senior executives and skilled personnel in the financial services and banking industry is intense, which means the cost of hiring, paying incentives and retaining skilled personnel may continue to increase. We need to continue to attract and retain key personnel and to recruit qualified individuals to succeed existing key personnel to ensure the continued growth and successful operation of our business. Our ability to effectively compete for senior executives and other qualified personnel by offering competitive compensation and benefit arrangements may increase our potential costs and may be restricted by applicable banking laws and regulations. The loss of the services of any senior executive or other key personnel, or the inability to recruit and retain qualified personnel in the future, could have a material adverse effect on our business, financial condition and results of operations.

Risks Related to Our Reputation and Operations

Our ability to maintain our reputation is critical to the success of our business, and the failure to do so may materially adversely affect our business, financial condition and results of operations.

We are a community bank, and our reputation is one of the most valuable components of our business. Threats to our reputation can come from many sources, including adverse sentiment about financial institutions generally, unethical practices, employee misconduct, failure to deliver minimum standards of service or quality, compliance deficiencies, and questionable or fraudulent activities of our customers. Negative publicity regarding our business, employees, or customers, with or without merit, may result in the loss of customers, investors and employees, costly litigation, a decline in revenues and increased governmental regulation and have a material adverse effect on business, financial condition and results of operations.

Adverse developments affecting the banking industry, and resulting media coverage, have eroded customer confidence in the banking system and could have a material effect on our operations and/or stock price.

The 2023 high-profile bank failures of Silicon Valley Bank, Signature Bank and First Republic Bank have generated significant market volatility among publicly traded bank holding companies. These market developments have negatively impacted customer confidence in the safety and soundness in the financial services industry, which has persisted into early 2024. We cannot offer assurances that the risks underlying negative publicity and public opinion have ameliorated or that adverse media stories, other bank failures, or geopolitical or market conditions will not exacerbate or continue these conditions. Partly as a result of these conditions, some community and regional bank depositors have chosen to place their deposits with larger financial institutions or to invest in higher yielding short-term fixed income securities, all of which have unfavorably affected, and may continue to materially adversely impact our liquidity, cost of funding, loan funding capacity, net interest margin, capital, and results of operations. In connection with high-profile bank failures, uncertainty and concern has been, and may be in the future, compounded by advances in technology that increase the speed at which deposits can be moved, as well as the speed and reach of media attention, including social media, and its ability to disseminate concerns or rumors, in each case potentially exacerbating liquidity concerns. Further, measures announced by the Department of the Treasury, the Federal Reserve, and the FDIC intended to reassure depositors of the availability of their deposits may not be successful in restoring customer confidence in the banking system.

In addition, the banking operating environment and public trading prices of banking institutions can be highly correlated, in particular during times of stress, which could adversely impact the trading prices of our common stock.

Further, recent experience has shown that the effects of these events on bank stock prices can cause a much more pronounced and widespread decline in trading values than might be expected based on an individual institution’s specific risk profile.

These recent events may also result in potentially adverse changes to laws or regulations governing banks and bank holding companies or result in the imposition of restrictions through supervisory or enforcement activities, including higher capital requirements, which could have a material impact on our business. The cost of resolving the recent bank failures may prompt the FDIC to increase its premiums above the recently increased levels or to issue additional special assessments.

Our risk management framework may not be effective in mitigating risks and/or losses to us.

Our risk management framework is comprised of various processes, systems and strategies, and is designed to manage the types of risk to which we are subject, including, among others, credit, market, liquidity, interest rate and compliance. Our risk management framework may not be effective under all circumstances and may not adequately mitigate any risk or loss to us. If our risk management framework is not effective, we could suffer unexpected losses and our business, financial condition and results of operations could be materially and adversely affected. We may also be subject to potentially adverse regulatory consequences.

Interruptions, cyber-attacks, fraudulent activity or other security breaches could have a material adverse effect on our business.

In the normal course of business, we directly or through third parties collect, store, share, process and retain sensitive and confidential information regarding our customers. We devote significant resources and management focus to ensuring the integrity of our systems, against damage from fires or other natural disasters; power or telecommunications failures; acts of terrorism or wars or other catastrophic events; breaches, physical break-ins or errors resulting in interruptions and unauthorized disclosure of confidential information, through information security and business continuity programs. Notwithstanding, our facilities and systems are vulnerable to interruptions, external or internal security breaches, acts of vandalism, computer viruses, misplaced or lost data, programming or human errors, force majeure events, or other similar events.

As a bank, we are susceptible to fraudulent activity 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's 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, phishing, social engineering and other dishonest acts. Reported incidents of fraud and other financial crimes have increased through the U.S. We have also experienced losses due to apparent fraud and other financial crimes. Increased use of the Internet and telecommunications technologies (including mobile devices) to conduct financial and other business transactions and operations, coupled with the increased sophistication and activities of organized crime, perpetrators of fraud, hackers, terrorists and others increases our security risks. In addition to cyber-attacks or other security breaches involving the theft of sensitive and confidential information, hackers continue to engage in attacks against large financial institutions. These attacks include denial of service attacks designed to disrupt external customer facing services, and ransomware attacks designed to deny organizations access to key internal resources or systems. While we have policies and procedures designed to prevent such losses, there can be no assurance that such losses will not occur. We are not able to anticipate or implement effective preventive measures against all security breaches of these types, especially because the techniques used change frequently and because attacks can originate from a wide variety of sources. We employ detection and response mechanisms designed to contain and mitigate security incidents, but early detection may be thwarted by sophisticated attacks and malware designed to avoid detection. The payment methods that we offer are subject to potential fraud and theft by criminals, who are becoming increasingly more sophisticated, seeking to obtain unauthorized access to or exploit weaknesses that may exist in the payment systems where we may be liable for losses. Breaches of information security also may occur through intentional or unintentional acts by those having access to our systems or our customers' or counterparties' confidential information, including employees.

The access by unauthorized persons to, or the improper disclosure by us of, confidential information regarding our customers or our own proprietary information, software, methodologies and business secrets, failures or disruptions in our communications, information and technology systems, or our failure to adequately address them, could negatively affect our customer relationship management, general ledger, deposit, loan or other systems. We cannot assure that such breaches, failures or interruptions will not occur or, if they do occur, that they will be adequately addressed by us or the third parties on which we rely. Our insurance may not fully cover all types of losses. The occurrence of any failures or interruptions of our communications, information and technology systems could damage our reputation, result in a loss of customer business, subject us to additional regulatory scrutiny or expose us to civil litigation and possible financial liability, any of which could have a material adverse effect on our business, financial condition or results of operations. We could be required to provide notices of security breaches. Such failures could result in increased regulatory scrutiny, legal liability, a loss of confidence in the security of our systems, our payment cards, products and services, and negative effects on our brand which could have a material adverse effect on our business, financial condition and results of operations.

Our operations could be interrupted by our third-party service providers experiencing difficulty in providing their services, terminating their services or failing to comply with banking regulations.

We depend to a significant extent on relationships with third-party service providers. Specifically, we utilize third-party core banking services and receive credit card and debit card services, branch capture services, Internet banking services and services complementary to our banking products from various third party service providers. These types of third-party relationships are subject to increasingly demanding regulatory requirements where we must maintain and continue to enhance our due diligence and ongoing monitoring and control over our third-party vendors. We may be required to renegotiate our agreements to meet these enhanced requirements, which could increase our costs. If our service providers experience difficulties or terminate their services and we are unable to replace them, our operations could be interrupted. It may be difficult for us to timely replace some of our service providers, which may be at a higher cost due to the unique services they provide. A third-party provider may fail to provide the services we require, or meet contractual requirements, comply with applicable laws and regulations, or suffer a cyber-attack or other security breach. We expect that our regulators will hold us responsible for deficiencies of our third-party relationships which could result in enforcement actions, including civil money penalties or other administrative or judicial penalties or fines, or customer remediation, any of which could have a material adverse effect on our business, financial condition and results of operations.

Employee misconduct could expose us to significant legal liability and reputational harm.

We are vulnerable to reputational harm because we operate in an industry in which integrity and the confidence of our customers are of critical importance. Our employees could engage in fraudulent, illegal, wrongful or suspicious activities, and/or activities resulting in consumer harm that adversely affects our customers and/or our business. The precautions we take to detect and prevent such misconduct may not always be effective and regulatory sanctions and/or penalties, serious harm to our reputation, financial condition, customer relationships and ability to attract new customers. In addition, improper use or disclosure of confidential information by our employees, even if inadvertent, could result in serious harm to our reputation, financial condition and current and future business relationships. If our internal controls against operational risks fail to prevent or detect an occurrence of such employee error or misconduct, or if any resulting loss is not insured or exceeds applicable insurance limits, it could have a material adverse effect on our business, financial condition and results of operations.

We depend on the accuracy and completeness of information provided by customers and counterparties and any misrepresented information could adversely affect our business, financial condition and results of operations.

In deciding whether to extend credit or to enter into other transactions with customers and counterparties, we may rely on information furnished to us by or on behalf of customers and counterparties, including financial statements and other financial information. Some of the information regarding customers provided to us is also used in our proprietary credit decision making and scoring models, which we use to determine whether to do business with customers and the risk profiles of such customers which are subsequently utilized by counterparties who lend us capital to fund our operations. We may also rely on representations of customers and counterparties as to the accuracy and completeness of that information. In deciding whether to extend credit, we may rely upon our customers' representations that their financial statements conform to Generally Accepted Accounting Principles and present fairly, in all material respects, the financial condition, results of operations and cash flows of the customer. We also may rely on customer representations and certifications, or other audit or accountants' reports, with respect to the business and financial condition of our customers. Whether a misrepresentation is made by the applicant, another third party or one of our employees, we generally bear the risk of loss associated with the misrepresentation. We may not detect all misrepresented information in our originations or from service providers we engage to assist in the approval process. Any such misrepresented information could have a material adverse effect on our business, financial condition and results of operations.

Increasing scrutiny and evolving expectations from customers, regulators, investors, and other stakeholders with respect to our environmental, social and governance practices may impose additional costs on us or expose us to new or additional risks.

Companies are facing increasing scrutiny from customers, regulators, investors, and other stakeholders related to their environmental, social and governance ("ESG") practices and disclosure. Investor advocacy groups, investment funds and influential investors are also increasingly focused on these practices, especially as they relate to the environment, health and safety, diversity, labor conditions and human rights. Increased ESG-related compliance costs for us as well as among our suppliers, vendors and various other parties within our supply chain could result in increases to our overall operational costs. New government regulations could also result in new or more stringent forms of ESG oversight and expanding mandatory and voluntary reporting, diligence, and disclosure. However, over the last few years there has been an increase in anti-ESG measures and proposals by investor advocacy groups, shareholders and policymakers. The potential impact of the 2024 presidential election on additional changes in agency personnel, policies and priorities on the financial services industry cannot be predicted at this time. Failure to adapt to or comply with evolving regulatory requirements or investor or stakeholder expectations and standards could negatively impact our reputation, ability to do business with certain partners, access to capital, and our stock price.

Risks from Competition

We face strong competition from financial services companies and other companies that offer commercial banking services, which could harm our business.

We face substantial competition in all phases of our operations from a variety of different competitors. Our competitors, including larger commercial banks, community banks, savings and loan associations, mutual savings banks, credit unions, consumer finance companies, insurance companies, securities dealers, brokers, mortgage bankers, investment advisors, money market mutual funds and other financial institutions, compete with lending and deposit gathering services offered by us. Many of these competing institutions have much greater financial and marketing resources than we have. Due to their size, many competitors can achieve larger economies of scale and may offer a broader range of products and services than we can. If we are unable to offer competitive products and services, our business may be negatively affected. Some of the financial services organizations with which we compete are not subject to the same degree of regulation as is imposed on bank holding companies and federally insured financial institutions or are not subject to increased supervisory oversight arising from regulatory examinations. As a result, these non-bank competitors have certain advantages over us in accessing funding and in providing various services.

We anticipate intense competition will continue for the coming year due to the recent consolidation of many financial institutions and more changes in legislation, regulation and technology. Further, we expect loan demand to continue to be challenging due to the uncertain economic climate and the intensifying competition for creditworthy borrowers, both of which could lead to loan rate concession pressure and could impact our ability to generate profitable loans. We expect we may see tighter competition in the industry as banks seek to take market share in the most profitable customer segments, particularly the small business segment and the mass affluent segment, which offers a rich source of deposits as well as more profitable and less risky customer relationships. Further, with the rebound of higher interest rates our deposit customers may perceive alternative investment opportunities as providing superior expected returns. Efforts and initiatives we undertake to retain and increase deposits, including deposit pricing, can increase our costs. When our customers move money into higher yielding deposits or in favor of alternative investments, we can lose a relatively inexpensive source of funds, thus increasing our funding costs.

New technology and other changes are allowing parties to effectuate financial transactions that previously required the involvement of banks. For example, consumers can maintain funds in brokerage accounts or mutual funds that would have historically been held as bank deposits. Consumers can also complete transactions such as paying bills and transferring funds directly without the assistance of banks. The process of eliminating banks as intermediaries, known as “disintermediation,” could result in the loss of fee income, as well as the loss of customer deposits and the related income generated from those deposits.

Increased competition in our markets may result in reduced loans, deposits, and fee income, as well as reduced net interest margin and profitability. If we are unable to attract and retain banking customers and expand our loan and deposit growth, then we may be unable to continue to grow our business which could have a material adverse effect on our financial condition and results of operations.

We have a continuing competitive need for technological change, and we may not have the resources to effectively implement new technology or we may experience operational challenges when implementing new technology.

The financial services industry is continually undergoing rapid technological change with frequent introductions of new, technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and to reduce costs. Our future success depends, in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies in our operations. Many of our competitors have substantially greater resources to invest in technological improvements than we do. As a result, they may be able to offer additional or superior products to those that we will be able to offer, which would put us at a competitive disadvantage. We may not be able to effectively implement new, technology-driven products and services or be successful in marketing these products and services to our customers. In addition, the implementation of technological changes and upgrades to maintain current systems and integrate new ones may also cause service interruptions, transaction processing errors and system conversion delays and may cause us to fail to comply with applicable laws. Failure to successfully keep pace with technological change affecting the financial services industry and avoid interruptions, errors and delays could have a material adverse effect on our business, financial condition and results of operations.

Risks Related to Other Business

The costs and effects of litigation, investigations or similar matters, or adverse facts and developments related thereto, could materially affect our business, financial condition and results of operations.

We are and will continue to be involved from time to time in a variety of litigation, investigations or similar matters arising out of our business. It is inherently difficult to assess the outcome of these matters, and we may not prevail in any proceedings or litigation. Any claims and lawsuits, and the disposition of such claims and lawsuits, whether through settlement, or litigation, could be time-consuming and expensive to resolve, divert management attention from executing our business plan, and lead to attempts on the part of other parties to pursue similar claims. Any claims asserted against us, regardless of merit or eventual outcome may harm our reputation. To mitigate the cost of some of these claims, we maintain insurance coverage in amounts and with deductibles that we believe are appropriate for our operations. However, our insurance coverage does not cover any civil monetary penalties or fines imposed by government authorities and may not cover all other claims that might be brought against us, including certain wage and hour class, collective and representative actions brought by customers, employees or former employees, and ponzi schemes. In addition, such insurance coverage may not continue to be available to us at a reasonable cost or at all. As a result, we may be exposed to substantial uninsured liabilities. Substantial legal liability or significant regulatory action against us could cause significant reputational harm to us and could have a material adverse impact on our business, financial condition, and results of operations.

Our ability to access markets for funding and acquire and retain customers could be adversely affected by the deterioration of other financial institutions or the financial service industry's reputation.

Our ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial services companies are interrelated as a result of trading, clearing, counterparty and other relationships. We have exposure to different industries and counterparties, and through transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, investment banks and other institutional clients. As a result, defaults by, or even rumors or questions about, one or more financial services companies, or the financial services industry generally, have led to market-wide liquidity problems and could lead to losses or defaults by us or by other institutions. These losses or defaults could have a material adverse effect on our business, financial condition and results of operations.

Severe weather, natural disasters, pandemics, acts of war or terrorism, social unrest and other external events could significantly impact our business.

Severe weather, natural disasters (including fires, earthquakes, and floods), wide spread disease or pandemics (such as COVID-19), acts of war or terrorism, social unrest and other adverse external events could have a significant impact on our ability to conduct business. Such events could affect the stability of our deposit base, impair the ability of borrowers to repay outstanding loans, impair the value of collateral securing loans, cause significant property damage, result in loss of revenue and/or cause us to incur additional expenses. The majority of our branches are located in the San Jose, San Francisco, Oakland areas, which in the past have experienced both severe earthquakes and wildfires. We do not carry earthquake insurance on our properties. Earthquakes, wildfires or other natural disasters could severely disrupt our operations. Operations in our market could be disrupted by both the evacuation of large portions of the population as well as damage to and/or lack of access to our banking and operation facilities. Although management has established disaster recovery policies and procedures, the occurrence of any such events could have a material adverse effect on our business, financial condition and results of operations.

In addition, our customers and loan collateral may be severely impacted by such events, resulting in losses. Physical risks related to discreet events such as flooding and wildfires, and extreme weather impacts and longer-term shifts in climate patterns, such as extreme heat, sea level rise and more frequent and prolonged droughts, which could impair our or our customers' property and/or result in financial losses that could impair asset values and the creditworthiness of our customers. Such events could disrupt our operations or those of our customers, including through direct damage to assets, reduced availability of and/or significant cost increases for insurance, unemployment and indirect impacts from supply chain disruption and market volatility.

Climate change could have a material negative impact on the Company and our customers.

The Company's business, as well as the operations and activities of our clients, could be negatively impacted by climate change. Climate change presents both immediate and long-term risks to the Company and its clients, and these risks are expected to increase over time. Climate change presents multi-faceted risks, including: operational risk from the physical effects of climate events on the Company and its clients' facilities and other assets; credit risk from borrowers with significant exposure to climate risk; transition risks associated with the transition to a less carbon-dependent economy; and reputational risk from stakeholder concerns about our practices related to climate change, the Company's carbon footprint, and the Company's business relationships with clients who operate in carbon-intensive industries.

Federal and state banking regulators and supervisory authorities, investors, and other stakeholders have increasingly viewed financial institutions as important in helping to address the risks related to climate change both directly and with respect to their clients, which may result in financial institutions coming under increased pressure regarding the disclosure and management of their climate risks and related lending and investment activities. Given that climate change could impose systemic risks upon the financial sector, either via disruptions in economic activity resulting from the physical impacts of climate change or changes in policies as the economy transitions to a less carbon-intensive environment, the Company may face regulatory risk of increasing focus on the Company's resilience to climate-related risks, including in the context of stress testing for various climate stress scenarios. Ongoing legislative or regulatory uncertainties and changes regarding climate risk management and practices may result in higher regulatory, compliance, credit, and reputational risks and costs.

With the increased importance and focus on climate change, we are making efforts to enhance our governance of climate change-related risks and integrate climate considerations into our risk governance framework. Nonetheless, the risks associated with climate change are rapidly changing and evolving in an escalating fashion, making them difficult to assess due to limited data and other uncertainties. We could experience increased expenses resulting from strategic planning, litigation, and technology and market changes, and reputational harm as a result of negative public sentiment, regulatory scrutiny, and reduced investor and stakeholder confidence due to our response to climate change and our climate change strategy, which, in turn, could have a material negative impact on our business, results of operations, and financial condition.

Risks Related to Finance and Accounting

Accounting estimates and risk management processes rely on analytical models that may prove inaccurate resulting in a material adverse effect on our business, financial condition and results of operations.

The processes we use to estimate the allowance for credit losses on loans and to measure the fair value of financial instruments, as well as the processes used to estimate the effects of changing interest rates and other market measures on our financial condition and results of operations, depends upon the use of analytical models. These models reflect assumptions that may not be accurate, particularly in times of market stress or other unforeseen circumstances. Even if these assumptions are adequate, the models using those assumptions may prove to be inadequate or inaccurate because of other flaws in their design or their implementation. If the models we use for interest rate risk and asset-liability management are inadequate, we may incur increased or unexpected losses upon changes in market interest rates or other market measures. If the models we use for determining the allowance for credit losses on loans are inadequate, the allowance for credit losses on loans may not be sufficient to support future charge-offs. If the models we use to measure the fair value of financial instruments are inadequate, the fair value of such financial instruments may fluctuate unexpectedly or may not accurately reflect what we could realize upon sale or settlement of such financial instruments. Any such failure in our analytical models could result in losses that could have a material adverse effect on our business, financial condition and results of operations.

Changes in accounting standards could materially impact our financial statements.

From time to time, the Financial Accounting Standards Board or the Securities and Exchange Commission ("SEC"), may change the financial accounting and reporting standards that govern the preparation of our financial statements. Such changes may result in us being subject to new or changing accounting and reporting standards. In addition, the bodies that interpret the accounting standards (such as banking regulators or outside auditors) may change their interpretations or positions on how these standards should be applied. These changes may be beyond our control, can be hard to predict and can materially impact how we record and report our financial condition and results of operations. In some cases, we could be required to apply a new or revised standard retrospectively, or apply an existing standard differently, also retrospectively, in each case resulting in our needing to revise or restate prior period financial statements. Restating or revising our financial statements may result in reputational harm or may have other adverse effects on us.

Failure to maintain effective internal controls over financial reporting could have a material adverse effect on our business and stock price.

We are required to comply with the SEC's rules implementing Section 302, Section 404, and Section 906 of the Sarbanes-Oxley Act, which will require management to certify financial and other information in our quarterly and annual reports and provide an annual management report as to the effectiveness of controls over financial reporting. In particular, we are required to certify our compliance with Section 404 of the Sarbanes-Oxley Act, which requires us to furnish annually a report by management on the effectiveness of our internal control over financial reporting and our independent registered public accounting firm is required to report on the effectiveness of our internal control over financial reporting.

If we identify any material weaknesses in our internal control over financial reporting or are unable to comply with the requirements of Section 404 in a timely manner or assert that our internal control over financial reporting is effective, or if our independent registered public accounting firm is unable to express an opinion as to the effectiveness of our internal control over financial reporting, investors, counterparties and customers may lose confidence in the accuracy and completeness of our financial statements and reports; our liquidity, access to capital markets and perceptions of our creditworthiness could be adversely affected; and the market price of our common stock could decline. In addition, we could become subject to investigations by the stock exchange on which our securities are listed, the SEC, the Federal Reserve, the FDIC, the Department of Financial Protection and Innovation ("DFPI") or other regulatory authorities, which could require additional financial and management resources. These events could have a material adverse effect on our business and stock price.

We have significant deferred tax assets and cannot assure that they will be fully realized.

Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between the carrying amounts and tax basis of assets and liabilities computed using enacted tax rates. We regularly assess available positive and negative evidence to determine whether it is more likely than not that our net deferred tax assets will be realized. Realization of a deferred tax asset requires us to apply significant judgment and is inherently speculative because it requires estimates that cannot be made with certainty. At March 31, 2024, we had a net deferred tax asset of $27.5 million. If we were to determine at some point in the future that we will not achieve sufficient future taxable income to realize our net deferred tax asset, we would be required, under generally accepted accounting principles, to establish a full or partial valuation allowance which would require us to incur a charge to income for the period in which the determination was made.

Risks Related to Legislative and Regulatory Developments

We are subject to extensive government regulation that could limit or restrict our activities, which in turn may adversely impact our ability to increase our assets and earnings.

We operate in a highly regulated environment and are subject to supervision and regulation by a number of governmental regulatory agencies, including the Federal Reserve, the DFPI and the FDIC. These bank regulators possess broad authority to prevent or remedy unsafe or unsound practices or violations of law. Regulations adopted by these agencies, which are generally intended to provide protection for depositors and customers rather than for the benefit of shareholders, govern a comprehensive range of matters relating to ownership and control of our shares, our acquisition of other companies and businesses, permissible activities for us to engage in, maintenance of adequate capital levels, and other aspects of our operations.

The potential impact of the 2024 presidential election and any changes in agency personnel, policies and priorities on the financial services industry cannot be predicted at this time. The laws and regulations applicable to the banking industry could change at any time and we cannot predict the effects of these changes on our business, profitability or growth strategy. Increased regulation could increase our cost of compliance and adversely affect profitability. Moreover, certain of these regulations contain significant punitive sanctions for violations, including monetary penalties and limitations on a bank's ability to implement components of its business plan, such as expansion through mergers and acquisitions or the opening of new branch offices. In addition, changes in regulatory requirements can significantly affect the services that we provide as well as the costs associated with compliance efforts. Furthermore, government policy and regulation, particularly as implemented through the Federal Reserve System, significantly affect credit conditions. Negative developments in the financial industry and the impact of new legislation and regulation in response to those developments could negatively impact our business operations and adversely impact our financial performance. In addition, adverse publicity and damage to our reputation arising from the failure or perceived failure to comply with legal, regulatory or contractual requirements could affect our ability to attract and retain customers.

Legislative and regulatory actions taken now or in the future may impact our business, governance structure, financial condition or results of operations. Proposed legislative and regulatory actions, including changes to financial regulation and the corporate tax law, may not occur on the timeframe that is expected, or at all, which could result in additional uncertainty for our business.

New proposals for legislation continue to be introduced in the U.S. Congress that could substantially increase regulation of the financial services industry, impose restrictions on the operations and general ability of firms within the industry to conduct business consistent with historical practices, including in the areas of compensation, interest rates, financial product offerings and disclosures, and have an effect on bankruptcy proceedings with respect to consumer residential real estate mortgages, among other things. Federal and state regulatory agencies also frequently adopt changes to their regulations or change the manner in which existing regulations are applied. Presently, in addition to refining existing regulations implemented after the 2008-2010 financial crisis, the banking regulators are also focusing their attention on certain policy areas, such as climate risk, capital requirements, digital currencies, and technological innovation and artificial intelligence. This new focus is on financial institutions of all sizes, but is expected to result in many smaller institutions facing regulatory standards that have typically been reserved for larger institutions and may require us to invest significant management attention and resources to evaluate and make any changes required by the legislation and accompanying rules.

Certain aspects of current or proposed regulatory or legislative changes, including to laws applicable to the financial industry, if enacted or adopted, may impact the profitability of our business activities, require more oversight or change certain of our business practices, including the ability to offer new products, obtain financing, attract deposits, make loans and achieve satisfactory interest spreads, and could expose us to additional costs, including increased compliance costs. These changes also may require us to invest significant management attention and resources to make any necessary changes to operations to comply and could have a material adverse effect on our business, financial condition and results of operations. In addition, any proposed legislative or regulatory changes, including those that could benefit our business, financial condition and results of operations, may not occur on the timeframe that is proposed, or at all, which could result in additional uncertainty for our business.

Federal and state regulators periodically examine our business, and we may be required to remediate adverse examination findings.

The Federal Reserve and the DFPI annually examine our business, including our compliance with laws and regulations. If, as a result of an examination, a banking agency were to determine that our financial condition, capital resources, asset quality, earnings prospects, management, liquidity or other aspects of any of our operations had become unsatisfactory, or that we were in violation of any law or regulation, they may take a number of different remedial actions as they deem appropriate. These actions 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 our capital, to restrict our growth, to assess civil money penalties, to fine or remove officers and directors and, if it is concluded that such conditions cannot be corrected or there is an imminent risk of loss to depositors, to terminate our deposit insurance and place us into receivership or conservatorship. Any regulatory action against us could have an adverse effect on our business, financial condition and results of operations.

We face a risk of noncompliance and enforcement action with the Bank Secrecy Act and other anti-money laundering statutes and regulations.

The Bank Secrecy Act, the USA Patriot Act and other laws and regulations require financial institutions, among other duties, to institute and maintain an effective anti-money laundering program and to file reports such as suspicious activity reports and currency transaction reports. We are required to comply with these and other anti-money laundering requirements. The federal banking agencies and Financial Crimes Enforcement Network are authorized to impose significant civil money penalties for violations of those requirements and have recently engaged in coordinated enforcement efforts against banks and other financial services providers with the U.S. Department of Justice, Drug Enforcement Administration and Internal Revenue Service. We are also subject to increased scrutiny of compliance with the rules enforced by the Office of Foreign Assets Control. If our policies, procedures and systems are deemed deficient, we would be subject to liability, including fines and regulatory actions, which may include restrictions on our ability to pay dividends and the necessity to obtain regulatory approvals to proceed with certain aspects of our business plan, including our acquisition plans. Failure to maintain and implement adequate programs to combat money laundering and terrorist financing could also have serious reputational consequences for us. Any of these results could have a material adverse effect on our business, financial condition and results of operations.

We are subject to numerous laws designed to protect consumers, including the Community Reinvestment Act and fair lending laws, and failure to comply with these laws could lead to a wide variety of sanctions.

The Community Reinvestment Act, the Equal Credit Opportunity Act, the Fair Housing Act and other fair lending laws and regulations impose non-discriminatory lending and other requirements on financial institutions. The U.S. Department of Justice and other federal agencies, including the FDIC and the Consumer Financial Protection Bureau, are responsible for enforcing these laws and regulations. A successful challenge to an institution’s performance under the Community Reinvestment Act, fair lending and other compliance laws and regulations could result in a wide variety of sanctions, including the required payment of damages and civil money penalties, injunctive relief, imposition of restrictions on mergers and acquisitions activity and restrictions on expansion. Private parties may also have the ability to challenge an institution’s performance under fair lending laws in private class action litigation. The costs of defending, and any adverse outcome from, any such challenge could damage our reputation or could have a material adverse effect on our business, financial condition and results of operations.

Regulations relating to privacy, information security, cybersecurity and data protection could increase our costs and affect or limit how we collect and use personal information.

We are subject to various privacy, information security, cybersecurity and data protection laws, including requirements concerning security breach notification, and we could be negatively impacted by these laws. For example, our business is subject to the Gramm-Leach-Bliley Act of 1999 which, among other things: (i) imposes certain limitations on our ability to share nonpublic personal information about our customers with nonaffiliated third parties; (ii) requires that we provide certain disclosures to customers about our information collection, sharing and security practices and afford customers the right to “opt out” of any information sharing by us with nonaffiliated third parties (with certain exceptions); and (iii) requires that we develop, implement and maintain a written comprehensive information security program containing safeguards appropriate based on our size and complexity, the nature and scope of our activities, and the sensitivity of customer information we process, as well as plans for responding to data security breaches. Various state and federal banking regulators and states have also enacted data security breach notification requirements with varying levels of individual, consumer, regulatory or law enforcement notification in certain circumstances in the event of a security breach. As a public company, we are subject to the SEC’s rules requiring disclosure of material cybersecurity incidents, as well as cybersecurity governance and risk management. Moreover, legislators and regulators in the United States are increasingly adopting or revising privacy, information security and data protection laws that potentially could have a significant impact on our current and planned privacy, data protection and information security-related practices, our collection, use, sharing, retention and safeguarding of consumer or employee information.

Compliance with current or future privacy, data protection and information security laws (including those regarding security breach notification) affecting customer or employee data to which we are subject could result in higher compliance and technology costs and could restrict our ability to provide certain products and services, which could have a material adverse effect on our business, financial condition and results of operations. Our failure to comply with privacy, data protection and information security laws could result in potentially significant regulatory or governmental investigations or actions, litigation, fines, sanctions and damage to our reputation, which could have a material adverse effect on our business, financial condition and results of operations.

Risks Related to Our Common Stock

An investment in our common stock is not an insured deposit.

An investment in our common stock is not a bank deposit and, therefore, is not insured against loss by the FDIC, any other deposit insurance fund or by any other public or private entity. Investment in our common stock is inherently risky for the reasons described herein, and is subject to the same market forces that affect the price of common stock in any company. As a result, if you acquire our common stock, you could lose some or all of your investment.

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. 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.

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 under “*Cautionary Note Regarding Forward-Looking Statements*” and “*Part II, Item 1A—Risk Factors*” contained in this Report. These broad market fluctuations have adversely affected and may continue to adversely affect the market price of our common stock, some of which are out of our control. Among the factors that could affect our stock price are:

- changes in business and economic condition;
- actual or anticipated quarterly fluctuations in our operating results and financial condition;
- actual occurrence of one or more of the risk factors outlined above;
- recommendations by securities analysts or failure to meet, securities analysts' estimates of our financial and operating performance, or lack of research reports by industry analysts or ceasing of coverage;
- speculation in the press or investment community generally or relating to our reputation, our operations, 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 institutional investors;
- fluctuations in the stock price and operating results of our competitors;
- future sales of our equity, equity related or debt securities;
- proposed or adopted regulatory changes or developments;
- anticipated or pending investigations, proceedings, or litigation that involve or affect us;
- the level and extent to which we do or are allowed to pay dividends;
- trading activities in our common stock, including short selling;
- deletion from well-known index or indices;
- 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.

The trading volume in our common stock is less than that of other larger financial services companies.

Although our common stock is listed for trading on The Nasdaq Stock Market LLC ("Nasdaq"), its trading volume is less than that of other, larger financial services companies, and investors are not assured that a liquid market will exist at any given time for our common stock. A public trading market having the desired characteristics of depth, liquidity and orderliness depends on the presence in the marketplace at any given time of willing buyers and sellers of our common stock. This presence depends on the individual decisions of investors and general economic and market conditions over which we have no control. Given the lower trading volume of our common stock, significant sales of our common stock, or the expectation of these sales, could cause our stock price to fall.

Our dividend policy may change without notice, and our future ability to pay dividends is subject to restrictions.

Historically, our Board has declared quarterly dividends on our common stock. However, we have no obligation to continue doing so and may change our dividend policy at any time without notice to holders of our common stock. Holders of our common stock are only entitled to receive such cash dividends as our Board, in its discretion, may declare out of funds legally available for such payments. Furthermore, consistent with our strategic plans, growth initiatives, capital availability, projected liquidity needs, and other factors, we have made, and will continue to make, capital management decisions and policies that could adversely impact the amount of dividends paid to holders of our common stock.

HCC is a separate and distinct legal entity from HBC. We receive substantially all of our revenue from dividends paid to us by HBC, which we use as the principal source of funds to pay our expenses and to pay dividends to our shareholders, if any. Various federal and/or state laws and regulations limit the amount of dividends that HBC may pay us. The Basel III capital rules also provide for risk-based capital, leverage and liquidity standards, including capital conservation buffers, that result in restrictions on HBC and the Company's ability to make dividend payments, redemptions or other capital distributions. If the HBC does not receive regulatory approval or does not maintain a level of capital sufficient to permit it to make dividend payments to us while maintaining adequate capital levels, our ability to pay our expenses and our business, financial condition and results of operations could be materially adversely impacted.

As a bank holding company, we are subject to regulation by the Federal Reserve. The Federal Reserve has indicated that bank holding companies should carefully review their dividend policy in relation to the organization's overall asset quality, current and prospective earnings and level, composition and quality of capital. The guidance provides that we inform and consult with the Federal Reserve prior to declaring and paying a dividend that exceeds earnings for the period for which the dividend is being paid or that could result in an adverse change to our capital structure, including interest on our debt obligations. If required payments on our debt obligations are not made or are deferred, or dividends on any preferred stock we may issue are not paid, we will be prohibited from paying dividends on our common stock.

We have limited the circumstances in which our directors will be liable for monetary damages.

We have included in our articles of incorporation a provision to eliminate the liability of directors for monetary damages to the maximum extent permitted by California law. The effect of this provision will be to reduce the situations in which we or our shareholders will be able to seek monetary damages from our directors.

Our bylaws also have a provision providing for indemnification of our directors and executive officers and advancement of litigation expenses to the fullest extent permitted or required by California law, including circumstances in which indemnification is otherwise discretionary. Also, we have entered into agreements with our officers and directors in which we similarly agreed to provide indemnification that is otherwise discretionary. Such indemnification may be available for liabilities arising in connection with future offerings.

Future equity issuances could result in dilution, which could cause our common stock price to decline.

We are generally not restricted from issuing additional shares of our common stock, up to the 100 million shares of voting common stock and 10 million shares of preferred stock authorized in our articles of incorporation (subject to Nasdaq shareholder approval rules), which in each case could be increased by a vote of a majority of our shares. We may issue additional shares of our common stock in the future pursuant to current or future equity compensation plans, upon conversions of preferred stock or debt, upon exercise of warrants or in connection with future acquisitions or financings. If we choose to raise capital by selling shares of our common stock for any reason, the issuance would have a dilutive effect on the holders of our common stock and could have a material negative effect on the market price of our common stock.

We may issue shares of preferred stock in the future, which could make it difficult for another company to acquire us or could otherwise adversely affect holders of our common stock, which could depress the price of our common stock.

Although there are currently no shares of our preferred stock issued and outstanding, our articles of incorporation authorize us to issue up to 10 million shares of one or more series of preferred stock. The board also has the power, without shareholder approval (subject to Nasdaq shareholder approval rules), to set the terms of any series of preferred stock that may be issued, including voting rights, dividend rights, preferences over our common stock with respect to dividends or in the event of a dissolution, liquidation or winding up and other terms. In the event that we issue preferred stock in the future that has preference over our common stock with respect to payment of dividends or upon our liquidation, dissolution or winding up, or if we issue preferred stock with voting rights that dilute the voting power of our common stock, the rights of the holders of our common stock or the market price of our common stock could be adversely affected. In addition, the ability of our Board to issue shares of preferred stock without any action on the part of our shareholders may impede a takeover of us and prevent a transaction perceived to be favorable to our shareholders.

The holders of our debt obligations will have priority over our common stock with respect to payment in the event of liquidation, dissolution or winding up and with respect to the payment of interest and dividends.

The holders of our debt obligations will have priority over our common stock with respect to payment in the event of liquidation, dissolution or winding up and with respect to the payment of interest and dividends.

In any liquidation, dissolution or winding up of the Company, our common stock would rank below all claims of the holders of outstanding debt issued by the Company. As of March 31, 2024, we had $40.0 million principal amount of subordinated notes outstanding due May 15, 2032. In such event, holders of our common stock would not be entitled to receive any payment or other distribution of assets upon the liquidation, dissolution or winding up of the Company until after all of the Company’s obligations to the debt holders were satisfied and holders of the subordinated debt had received any payment or distribution due to them. In addition, we are required to pay interest on the subordinated notes and if we are in default in the payment of interest we would not be able to pay any dividends on our common stock.

Provisions in our charter documents and California law may have an anti-takeover effect, and there are substantial regulatory limitations on changes of control of bank holding companies.

Our articles of incorporation and bylaws contain a number of provisions relating to corporate governance and rights of shareholders that might discourage future takeover attempts. As a result, shareholders who might desire to participate in such transactions may not have an opportunity to do so. In addition, these provisions will also render the removal of our Board or management more difficult. Such provisions include a requirement that shareholder approval for any action proposed by the Company must be obtained at a shareholders meeting and may not be obtained by written consent. Our bylaws provide that shareholders seeking to make nominations of candidates for election as directors, or to bring other business before an annual meeting of the shareholders, must provide timely notice of their intent in writing and follow specific procedural steps in order for nominees or shareholder proposals to be brought before an annual meeting.

Provisions of our charter documents and the California General Corporation Law could make it more difficult for a third party to acquire us, even if doing so would be perceived to be beneficial by our shareholders. Furthermore, with certain limited exceptions, federal regulations prohibit a person or company or a group of persons deemed to be “acting in concert” from, directly or indirectly, acquiring more than 10% (5% if the acquirer is a bank holding company) of any class of our voting stock or obtaining the ability to control in any manner the election of a majority of our directors or otherwise direct the management or policies of our company without prior notice or application to and the approval of the Federal Reserve. Under the California Financial Code, no person may, directly or indirectly, acquire control of a California state bank or its holding company unless the DFPI has approved such acquisition of control. A person would be deemed to have acquired control of HBC if such person, directly or indirectly, has the power (i) to vote 25% or more of the voting power of HBC or (ii) to direct or cause the direction of the management and policies of HBC. For purposes of this law, a person who directly or indirectly owns or controls 10% or more of our outstanding common stock would be presumed to control HBC. Accordingly, prospective investors need to be aware of and comply with these requirements, if applicable, in connection with any purchase of shares of our common stock. Moreover, the combination of these provisions effectively inhibits certain mergers or other business combinations, which, in turn, could adversely affect the market price of our common stock.

ITEM 2—UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3—DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4—MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5—OTHER INFORMATION

None.

ITEM 6—EXHIBITS

Exhibit	Description
3.1	Heritage Commerce Corp Restated Articles of Incorporation, (incorporated by reference to Exhibit 3.1 to the Registrant’s Annual Report on Form 10-K filed on March 16, 2009).
3.2	Certificate of Amendment of Articles of Incorporation of Heritage Commerce Corp as filed with the California Secretary of State on June 1, 2010 (incorporated by reference to Exhibit 3.2 to the Registrant’s Registration Statement on Form S-1 filed July 23, 2010).
3.3	Certificate of Amendment of Articles of Incorporation of Heritage Commerce Corp as filed with the California Secretary of State on August 29, 2019 (incorporated by reference to Exhibit 3.3 to the Registrant’s Quarterly Report on Form 10-Q filed on November 7, 2019).
3.4	Heritage Commerce Corp Bylaws, as amended (incorporated by reference to Exhibit 3.1 to the Registrant’s Current Report on Form 8-K filed on June 28, 2013).
10.1*†	Amended and Restated Employment Agreement with Glen Shu, dated February 1, 2024 (incorporated by reference to Exhibit 10.8 to the Registrant’s Annual Report on Form 10-K filed on March 11, 2024).
10.2*†	Amended and Restated Employment Agreement with Susan Just, dated February 1, 2024 (incorporated by reference to Exhibit 10.10 to the Registrant’s Annual Report on Form 10-K filed on March 11, 2024).
10.3*†	Employment Agreement with Dustin Warford, dated February 1, 2024 (incorporated by reference to Exhibit 10.11 to the Registrant’s Annual Report on Form 10-K filed on March 11, 2024).
31.1	Certification of Registrant’s Chief Executive Officer Pursuant To Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Registrant’s Chief Financial Officer Pursuant To Section 302 of the Sarbanes-Oxley Act of 2002.
32.1**	Certification of Registrant’s Chief Executive Officer Pursuant To 18 U.S.C. Section 1350 .
32.2**	Certification of Registrant’s Chief Financial Officer Pursuant To 18 U.S.C. Section 1350 .
101.INS	Inline XBRL Instance Document Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.
101.SCH	Inline XBRL Taxonomy Extension Schema.
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase.
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase.
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase.
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase.
104.	The cover page from Heritage Commerce Corp's Quarterly Report on Form 10-Q for the quarter ended March 31, 2024, formatted in Inline XBRL.

* Management contract or compensatory plan or arrangement.
**Furnished and not filed.
† Certain identified information has been excluded from the exhibit pursuant to Regulation S-K Item 601(b)(10)(iv) because it is both (i) not material and (ii) is the type that the Company customarily treats as private or confidential.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Heritage Commerce Corp (Registrant)

Date: May 8, 2024	/s/ ROBERTSON CLAY JONES Robertson Clay Jones *Chief Executive Officer*
Date: May 8, 2024	/s/ LAWRENCE D. MCGOVERN Lawrence D. McGovern *Chief Financial Officer*

Exhibit 31.1

CERTIFICATION UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002
REGARDING THE QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED MARCH 31, 2024

I, Robertson Clay Jones, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2024 of Heritage Commerce Corp;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 8, 2024

/s/ ROBERTSON CLAY JONES
Robertson Clay Jones
Chief Executive Officer

Exhibit 31.2

CERTIFICATION UNDER SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002
REGARDING THE QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED MARCH 31, 2024

I, Lawrence D. McGovern, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2024 of Heritage Commerce Corp;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

   (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: May 8, 2024

/s/ LAWRENCE D. MCGOVERN
Lawrence D. McGovern
Chief Financial Officer

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002
REGARDING THE QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED MARCH 31, 2024

In connection with the Quarterly Report of Heritage Commerce Corp (the “Company”) on Form 10-Q for the period ended March 31, 2024 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Robertson Clay Jones, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 8, 2024

/s/ ROBERTSON CLAY JONES
Robertson Clay Jones
Chief Executive Officer

Exhibit 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002
REGARDING THE QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED MARCH 31, 2024

In connection with the Quarterly Report of Heritage Commerce Corp (the “Company”) on Form 10-Q for the period ended March 31, 2024 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Lawrence D. McGovern, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 8, 2024

/s/ LAWRENCE D. MCGOVERN
Lawrence D. McGovern
Chief Financial Officer