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 September 30, 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	**77-0469558**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
224 Airport Parkway, San Jose, California	**95110**
(Address of Principal Executive Offices)	(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 61,303,366 shares of Common Stock outstanding on October 30, 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, and Rule 3b-6 promulgated thereunder and are intended to be protected by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. 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 statements reflect, and are based upon, facts and circumstances known to or expected by our executive leadership, and intentions and expectations of those individuals, as of the date of this Report.

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. Likewise, statements about or relating to our current plans and intentions are not promises that we will execute those plans, or that we will not deviate from them as a result of changes in conditions or otherwise. Risks and uncertainties that could cause our financial performance to differ materially from our goals, plans, expectations and projections, or that could cause us to deviate from our expected strategies, are identified in "*Part II, Item 1A—Risk Factors*" of this Report, and include but are not limited to the following:

- cybersecurity risks that may affect us directly or may impact us indirectly by virtue of their effects on our clients, markets or vendors, including our ability to identify and address cybersecurity 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, our clients, and our third-party vendors and service providers;

- 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 clients, and which may increase the volatility of financial markets;

- factors that affect our liquidity and our ability to meet client demands for withdrawals from deposit accounts and undrawn lines of credit, including our cash on hand and the availability of funds from our own lines of credit;

- market fluctuations that affect the costs we pay for sources of funding, including the interest we pay on deposits and on our borrowings;

- media items and consumer confidence as those factors affect our clients' 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;

- 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 portfolios and our factoring business;
- events and circumstances that affect our borrowers' and guarantors' 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 clients;
- 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 fluctuations in economic growth;
- 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 clients, 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;
- 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 clients, employees, businesses, liquidity, financial results and overall condition including severity and duration of the associated uncertainties in U.S. and global markets;
- 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;
- events that affect our ability to attract, recruit, and retain qualified officers and other personnel to implement our strategic plan, and that enable current and future personnel to protect and develop our relationships with clients, and to promote our business, results of operations and growth prospects;
- factors that affect the carrying value of the goodwill associated with our previous acquisitions;
- 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, particularly including but not limited to the effects of recent and ongoing developments in California labor and employment laws, regulations and court decisions;
- 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, including the particular risks of natural disasters (including earthquakes, fires, and flooding) and other events that disproportionately affect that region;
- 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 (UNAUDITED)

HERITAGE COMMERCE CORP
CONSOLIDATED BALANCE SHEETS
(Unaudited)

	September 30, 2024	December 31, 2023
	(Dollars in thousands)	
Assets		
Cash and due from banks	$ 49,722	$ 41,592
Other investments and interest-bearing deposits in other financial institutions	906,588	366,537
Total cash and cash equivalents	956,310	408,129
Securities available-for-sale, at fair value	237,612	442,636
Securities held-to-maturity, at amortized cost, net of allowance for credit losses of $12 (fair value of $531,533 and $564,127, respectively)	604,193	650,565
Loans held-for-sale - SBA, at lower of cost or fair value, including deferred costs	1,649	2,205
Loans, net of deferred fees	3,410,236	3,350,378
Allowance for credit losses on loans	(47,819)	(47,958)
Loans, net	3,362,417	3,302,420
Federal Home Loan Bank ("FHLB"), Federal Reserve Bank ("FRB") stock and other investments, at cost	32,553	32,540
Company-owned life insurance	80,682	79,489
Premises and equipment, net	10,398	9,857
Goodwill	167,631	167,631
Other intangible assets	6,966	8,627
Accrued interest receivable and other assets	91,185	89,996
Total assets	$ 5,551,596	$ 5,194,095
Liabilities and Shareholders' Equity		
Liabilities:		
Deposits:		
Demand, noninterest-bearing	$ 1,272,139	$ 1,292,486
Demand, interest-bearing	913,910	914,066
Savings and money market	1,309,676	1,087,518
Time deposits - under $250	39,060	38,055
Time deposits - $250 and over	196,945	192,228
Insured Cash Sweep ("ICS")/Certificates of Deposit Account Registry Service ("CDARS") - interest-bearing demand, money market and time deposits	997,803	854,105
Total deposits	4,729,533	4,378,458
Subordinated debt, net of issuance costs	39,615	39,502
Accrued interest payable and other liabilities	97,096	103,234
Total liabilities	4,866,244	4,521,194
Shareholders' equity:		
Preferred stock, no par value; 10,000,000 shares authorized; none issued and outstanding at September 30, 2024 and December 31, 2023	—	—
Common stock, no par value; 100,000,000 shares authorized; 61,297,344 and 61,146,835 shares issued and outstanding, respectively	509,134	506,539
Retained earnings	185,110	179,092
Accumulated other comprehensive loss	(8,892)	(12,730)
Total shareholders' equity	685,352	672,901
Total liabilities and shareholders' equity	$ 5,551,596	$ 5,194,095

See notes to consolidated financial statements (unaudited).

HERITAGE COMMERCE CORP
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2024	2023	2024	2023
	(Dollars in thousands, except per share amounts)			
Interest income:				
Loans, including fees	$ 45,781	$ 44,853	$ 135,851	$ 132,993
Securities, taxable	4,676	6,797	16,342	20,835
Securities, exempt from Federal tax	223	232	674	718
Other investments, interest-bearing deposits in other financial institutions and Federal funds sold	10,758	8,909	25,199	20,860
Total interest income	61,438	60,791	178,066	175,406
Interest expense:				
Deposits	20,985	14,880	56,989	31,504
Short-term borrowings	—	—	—	1,365
Subordinated debt	538	539	1,614	1,614
Total interest expense	21,523	15,419	58,603	34,483
Net interest income before provision for credit losses on loans	39,915	45,372	119,463	140,923
Provision for credit losses on loans	153	168	808	460
Net interest income after provision for credit losses on loans	39,762	45,204	118,655	140,463
Noninterest income:				
Service charges and fees on deposit accounts	908	859	2,676	3,503
Increase in cash surrender value of life insurance	530	517	1,569	1,512
Servicing income	108	62	288	297
Gain on sales of SBA loans	94	207	348	482
Termination fees	46	118	159	129
Gain on proceeds from company-owned life insurance	—	100	219	100
Other	554	353	1,304	1,033
Total noninterest income	2,240	2,216	6,563	7,056
Noninterest expense:				
Salaries and employee benefits	15,673	14,147	46,976	42,943
Occupancy and equipment	2,599	2,301	7,731	7,123
Professional fees	1,306	717	3,705	3,265
Other	7,977	8,006	24,867	22,232
Total noninterest expense	27,555	25,171	83,279	75,563
Income before income taxes	14,447	22,249	41,939	71,956
Income tax expense	3,940	6,454	12,032	20,841
Net income	$ 10,507	$ 15,795	$ 29,907	$ 51,115
Earnings per common share:				
Basic	$ 0.17	$ 0.26	$ 0.49	$ 0.84
Diluted	$ 0.17	$ 0.26	$ 0.49	$ 0.83

See notes to consolidated financial statements (unaudited).

HERITAGE COMMERCE CORP
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2024	2023	2024	2023
	(Dollars in thousands)			
Net income	$ 10,507	$ 15,795	$ 29,907	$ 51,115
Other comprehensive income (loss):				
Change in net unrealized holding gains (losses) on available-for-sale securities and I/O strips	4,024	(243)	5,549	(701)
Deferred income taxes	(1,167)	70	(1,609)	203
Change in unrealized gains (losses) on securities and I/O strips, net of deferred income taxes	2,857	(173)	3,940	(498)
Change in net pension and other benefit plan liability adjustment	(26)	(35)	(79)	(104)
Deferred income taxes	(8)	(3)	(23)	(11)
Change in pension and other benefit plan liability, net of deferred income taxes	(34)	(38)	(102)	(115)
Other comprehensive income (loss)	2,823	(211)	3,838	(613)
Total comprehensive income	$ 13,330	$ 15,584	$ 33,745	$ 50,502

See notes to consolidated financial statements (unaudited).

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

	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' 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, net of taxes	—	—	—	2,539	2,539
Net amortization of restricted stock awards	—	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
Net income	—	—	16,403	—	16,403
Other comprehensive loss, net of taxes	—	—	—	(2,941)	(2,941)
Issuance (forfeitures) of restricted stock awards, net	65,446	—	—	—	—
Net amortization of restricted stock awards	—	376	—	—	376
Cash dividend declared $0.13 per share	—	—	(7,940)	—	(7,940)
Restricted stock units ("RSUs") and performance-based restricted stock units ("PRSUs") expense, net of taxes	—	96	—	—	96
Stock option expense, net of forfeitures and taxes	—	154	—	—	154
Stock options exercised	77,102	314	—	—	314
Balance June 30, 2023	61,091,155	505,075	165,853	(17,258)	653,670
Net income	—	—	15,795	—	15,795
Other comprehensive loss, net of taxes	—	—	—	(211)	(211)
Issuance (forfeitures) of restricted stock awards, net	8,000	—	—	—	—
Amortization of restricted stock awards, net of forfeitures and taxes	—	321	—	—	321
Cash dividend declared $0.13 per share	—	—	(7,941)	—	(7,941)
RSUs and PRSUs expense, net of taxes	—	148	—	—	148
Stock option expense, net of forfeitures and taxes	—	148	—	—	148
Stock options exercised	—	—	—	—	—
Balance September 30, 2023	61,099,155	$ 505,692	$ 173,707	$ (17,469)	$ 661,930
Balance, January 1, 2024	61,146,835	$ 506,539	$ 179,092	$ (12,730)	$ 672,901
Net income	—	—	10,166	—	10,166
Other comprehensive income, net of taxes	—	—	—	142	142
Issuance of restricted stock awards, net of forfeitures	33,908	—	—	—	—
Net amortization of restricted stock awards	—	311	—	—	311
Cash dividend declared $0.13 per share	—	—	(7,952)	—	(7,952)
RSUs and 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
Net income	—	—	9,234	—	9,234
Other comprehensive income, net of taxes	—	—	—	873	873
Issuance (forfeitures) of restricted stock awards, net	(8,000)	—	—	—	—
Net amortization of restricted stock awards	—	165	—	—	165
Cash dividend declared $0.13 per share	—	—	(7,969)	—	(7,969)
RSUs and PRSUs expense, net of taxes	—	413	—	—	413
RSUs vested	35,837	—	—	—	—
Stock option expense, net of forfeitures and taxes	—	129	—	—	129
Stock options exercised	10,632	58	—	—	58
Balance June 30, 2024	61,292,094	508,343	182,571	(11,715)	679,199
Net income	—	—	10,507	—	10,507
Other comprehensive income, net of taxes	—	—	—	2,823	2,823
Amortization of restricted stock awards, net of forfeitures and taxes	—	239	—	—	239
Cash dividend declared $0.13 per share	—	—	(7,968)	—	(7,968)
RSUs and PRSUs expense, net of taxes	—	396	—	—	396
Stock option expense, net of forfeitures and taxes	—	121	—	—	121
Stock options exercised	5,250	35	—	—	35
Balance September 30, 2024	61,297,344	$ 509,134	$ 185,110	$ (8,892)	$ 685,352

See notes to consolidated financial statements (unaudited).

HERITAGE COMMERCE CORP
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30, 2024	Nine Months Ended September 30, 2023
	(Dollars in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 29,907	$ 51,115
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of premiums and accretion of discounts on securities, net	(2,139)	(3,746)
Gain on sale of SBA loans	(348)	(482)
Proceeds from sale of SBA loans originated for sale	4,563	8,035
SBA loans originated for sale	(3,659)	(5,938)
Provision for credit losses on loans	808	460
Increase in cash surrender value of life insurance	(1,569)	(1,512)
Depreciation and amortization	977	828
Amortization of other intangible assets	1,661	1,804
Stock option expense, net	395	449
RSUs and PRSUs expense	1,007	244
Amortization of restricted stock awards, net	715	1,079
Amortization of subordinated debt issuance costs	113	113
Gain on proceeds from company-owned life insurance	(219)	(100)
Effect of changes in:		
Accrued interest receivable and other assets	202	(4,400)
Accrued interest payable and other liabilities	(9,262)	29,642
Net cash provided by operating activities	23,152	77,591
CASH FLOWS FROM INVESTING ACTIVITIES:		
Maturities/paydowns/calls of securities available-for-sale	213,508	36,283
Maturities/paydowns/calls of securities held-to-maturity	45,598	49,500
Net change in loans	(60,805)	12,819
Changes in FHLB stock and other investments	(13)	(13)
Proceeds from redemption of company-owned life insurance	595	950
Purchase of premises and equipment	(1,518)	(1,234)
Net cash provided by investing activities	197,365	98,305
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net change in deposits	351,075	185,853
Exercise of stock options	478	997
Payment of cash dividends	(23,889)	(23,797)
Net cash provided by financing activities	327,664	163,053
Net increase in cash and cash equivalents	548,181	338,949
Cash and cash equivalents, beginning of period	408,129	306,603
Cash and cash equivalents, end of period	$ 956,310	$ 645,552
Supplemental disclosures of cash flow information:		
Interest paid	$ 56,140	$ 29,887
Income taxes paid, net	$ 12,342	$ 79
Supplemental schedule of non-cash activity:		
Recording of right of use assets in exchange for lease obligations	$ 3,045	$ 541

See notes to consolidated financial statements (unaudited).

HERITAGE COMMERCE CORP
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
September 30, 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 (“2023 Form 10-K”).

HBC is a commercial bank serving clients 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 client 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 and nine months ended September 30, 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.

Issued But Not Yet Effective Accounting Standards

In October 2023, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2023-06 - Disclosure Improvements - Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative. ASU 2023-06 amends the disclosure or presentation requirements related to various subtopics in the FASB Accounting Standards Codification. ASU 2023-06 was issued in response to the SEC's August 2018 final rule that updated and simplified disclosure requirements. In the final rule, the SEC identified 27 disclosure requirements that were incremental to those in the ASC and referred them to the FASB for potential incorporation into US GAAP. To avoid duplication, the SEC intended to eliminate those disclosure requirements from existing SEC regulations if the FASB incorporated them into the relevant ASC subtopics. The disclosure requirements are currently included in either SEC Regulation S-X or SEC Regulation S-K. ASU 2023-06 adds 14 of the 27 identified disclosure or presentation requirements to the ASC.

For entities like HCC that are subject to the SEC's existing disclosure requirements, the effective date for each amendment will be the date on which the SEC's removal of that related disclosure from Regulation S-X or Regulation S-K becomes effective, with early adoption prohibited. The amendments are to be applied prospectively and, if by June 30, 2027 the SEC has not removed the applicable requirement from Regulation S-X or S-K, the pending content of the related amendment will be removed from the ASC and will not become effective for any entity. Management intends to adopt the provisions of ASU 2023-06 on their respective effective dates. The adoption of the provisions of ASU 2023-06 is not expected to have a material impact on HCC's consolidated financial statements.

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. The Company will update the related disclosures upon adoption.

In December 2023, 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) Shareholders’ Equity and Earnings Per Share

Share Repurchase Program – On July 25, 2024, the Company announced that its Board of Directors adopted a share repurchase program (the “Repurchase Program”) under which the Company is authorized to repurchase up to $15,000,000 of the Company’s shares of its issued and outstanding common stock. Unless otherwise suspended or terminated, the Repurchase Program expires on July 31, 2025. The Company did not repurchase any of its common stock during the third quarter of 2024.

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 1,440,168, and 1,841,601 weighted average stock options outstanding for the three months and nine months ended September 30, 2024, respectively, considered to be antidilutive and excluded from the computation of diluted earnings per share. There were 1,905,852 and 1,763,377 weighted average stock options outstanding for the three months and nine months ended September 30, 2023, respectively, considered to be antidilutive and excluded from the computation of diluted earnings per share. There were 1,467 and 493 weighted average RSUs outstanding for the three months and nine months ended September 30, 2024, respectively, 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 September 30, 2023, and 66,458 weighted average RSUs outstanding for the nine months ended September 30, 2023, respectively, 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 September 30,		**Nine Months Ended September 30,**	
	2024	**2023**	**2024**	**2023**
	(Dollars in thousands, except per share amounts)			
Net income	$ 10,507	$ 15,795	$ 29,907	$ 51,115
Weighted average common shares outstanding for basic earnings per common share	61,295,877	61,093,289	61,254,138	61,012,315
Dilutive potential common shares	250,280	342,951	243,789	272,275
Shares used in computing diluted earnings per common share	61,546,157	61,436,240	$ 61,497,927	$ 61,284,590
Basic earnings per share	$ 0.17	$ 0.26	$ 0.49	$ 0.84
Diluted earnings per share	$ 0.17	$ 0.26	$ 0.49	$ 0.83

3) Accumulated Other Comprehensive Income (Loss) (“AOCI”)

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

	Three Months Ended September 30, 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 July 1, 2024, net of taxes	$ (5,946)	$ (5,769)	$ (11,715)
Other comprehensive income (loss) before reclassification, net of taxes	2,857	(16)	2,841
Amounts reclassified from other comprehensive income (loss), net of taxes	—	(18)	(18)
Net current period other comprehensive income (loss), net of taxes	2,857	(34)	2,823
Ending balance September 30, 2024, net of taxes	$ (3,089)	$ (5,803)	$ (8,892)
Beginning balance July 1, 2023, net of taxes	$ (11,719)	$ (5,539)	$ (17,258)
Other comprehensive income (loss) before reclassification, net of taxes	(173)	(13)	(186)
Amounts reclassified from other comprehensive income (loss), net of taxes	—	(25)	(25)
Net current period other comprehensive income (loss), net of taxes	(173)	(38)	(211)
Ending balance September 30, 2023, net of taxes	$ (11,892)	$ (5,577)	$ (17,469)

(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.

	Nine Months Ended September 30, 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	3,940	(47)	3,893
Amounts reclassified from other comprehensive income (loss), net of taxes	—	(55)	(55)
Net current period other comprehensive income (loss), net of taxes	3,940	(102)	3,838
Ending balance September 30, 2024, net of taxes	$ (3,089)	$ (5,803)	$ (8,892)
Beginning balance January 1, 2023, net of taxes	$ (11,394)	$ (5,462)	$ (16,856)
Other comprehensive income (loss) before reclassification, net of taxes	(498)	(41)	(539)
Amounts reclassified from other comprehensive income (loss), net of taxes	—	(74)	(74)
Net current period other comprehensive income (loss), net of taxes	(498)	(115)	(613)
Ending balance September 30, 2023, net of taxes	$ (11,892)	$ (5,577)	$ (17,469)

(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 September 30, 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	$ 48	
Prior service cost and actuarial losses (3)	(26)	(13)	
	26	35	Other noninterest expense
	(8)	(10)	Income tax benefit
Total reclassification from AOCI for the period	$ 18	$ 25	Net of tax

(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.

Details About AOCI Components	Amounts Reclassified from AOCI Nine Months Ended September 30, 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]	$ 157	$ 143	
Prior service cost and actuarial losses [3]	(78)	(39)	
	79	104	Other noninterest expense
	(24)	(30)	Income tax benefit
Total reclassification from AOCI for the period	$ 55	$ 74	Net of tax

(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 at the dates indicated:

September 30, 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	$ 185,602	$ —	$ (1,440)	$ —	$ 184,162
Agency mortgage-backed securities	56,373	—	(2,923)	—	53,450
Total	$ 241,975	$ —	$ (4,363)	$ —	$ 237,612

September 30, 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	$ 573,621	$ 381	$ (72,377)	$ 501,625	$ —
Municipals - exempt from Federal tax	30,584	3	(679)	29,908	(12)
Total	$ 604,205	$ 384	$ (73,056)	$ 531,533	$ (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 at the dates indicated:

	Less Than 12 Months		12 Months or More		Total	
September 30, 2024	**Fair Value**	**Unrealized (Losses)**	**Fair Value**	**Unrealized (Losses)**	**Fair Value**	**Unrealized (Losses)**
			(Dollars in thousands)			
Securities available-for-sale:						
U.S. Treasury	$ —	$ —	$ 184,162	$ (1,440)	$ 184,162	$ (1,440)
Agency mortgage-backed securities	—	—	53,450	(2,923)	53,450	(2,923)
Total	$ —	$ —	$ 237,612	$ (4,363)	$ 237,612	$ (4,363)
Securities held-to-maturity:						
Agency mortgage-backed securities	$ —	$ —	$ 490,099	$ (72,377)	$ 490,099	$ (72,377)
Municipals — exempt from Federal tax	4,288	(40)	20,521	(639)	24,809	(679)
Total	$ 4,288	$ (40)	$ 510,620	$ (73,016)	$ 514,908	$ (73,056)

	Less Than 12 Months		12 Months or More		Total	
December 31, 2023	**Fair Value**	**Unrealized (Losses)**	**Fair Value**	**Unrealized (Losses)**	**Fair Value**	**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.

At the dates and during the periods covered by these financial statements, 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 September 30, 2024, the Company held 396 securities (130 available-for-sale and 266 held-to-maturity), of which 375 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 September 30, 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	Estimated Fair Value
	(Dollars in thousands)	
Due three months or less	$ 8,981	$ 8,972
Due after three months through one year	176,621	175,190
Agency mortgage-backed securities	56,373	53,450
Total	$ 241,975	$ 237,612

	Held-to-maturity	
	Amortized Cost (1)	Estimated Fair Value
	(Dollars in thousands)	
Due after three months through one year	$ 1,805	$ 1,799
Due after one through five years	7,395	7,307
Due after five through ten years	21,384	20,802
Agency mortgage-backed securities	573,621	501,625
Total	$ 604,205	$ 531,533

(1) Gross of the allowance for credit losses of ($12,000) at September 30, 2024.

Securities with amortized cost of $ 777,327,000 and $1,041,608,000 as of September 30, 2024 and December 31, 2023, respectively, were pledged to secure the Bank's lines of credit and for other purposes as required or permitted by law or contract. The decrease in pledged securities at September 30, 2024 was due to securities maturities.

The allowance for credit losses on the Company's held-to-maturity debt securities is presented as a reduction to the amortized cost basis of held-to-maturity securities on the Company's Consolidated Balance Sheet. The table below presents a roll-forward by major security type for the nine months ended September 30, 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 September 30, 2024	$ 12

The bond ratings for the Company's municipal investment securities at September 30, 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. Descriptions of the Company's loan portfolio segments are included in Note 1 "*Summary of Significant Accounting Policies*" of the 2023 Form 10-K.

Loan Distribution

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

	September 30, 2024	December 31, 2023
	(Dollars in thousands)	
Loans held-for-investment:		
Commercial	$ 481,266	$ 463,778
Real estate:		
CRE - owner occupied	602,062	583,253
CRE - non-owner occupied	1,310,578	1,256,590
Land and construction	125,761	140,513
Home equity	124,090	119,125
Multifamily	273,103	269,734
Residential mortgages	479,524	496,961
Consumer and other	14,179	20,919
Loans	3,410,563	3,350,873
Deferred loan fees, net	(327)	(495)
Loans, net of deferred fees	3,410,236	3,350,378
Allowance for credit losses on loans	(47,819)	(47,958)
Loans, net	$ 3,362,417	$ 3,302,420

The allowance for credit losses is an estimate of the expected credit losses on financial assets measured at amortized cost, which is measured using relevant information about past events, including historical credit loss experience on financial assets with similar risk characteristics, current conditions, and reasonable and supportable forecasts that affect the collectability of the remaining cash flows over the contractual term of the financial assets.

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

	Three Months Ended September 30, 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	$ 5,010	$ 5,344	$ 26,847	$ 1,523	$ 814	$ 4,269	$ 3,960	$ 187	$ 47,954
Charge-offs	(174)	—	—	—	—	—	—	(300)	(474)
Recoveries	154	14	—	—	18	—	—	—	186
Net (charge-offs) recoveries	(20)	14	—	—	18	—	—	(300)	(288)
Provision for (recapture of) credit losses on loans	(273)	62	603	(195)	(72)	86	(291)	233	153
End of period balance	$ 4,717	$ 5,420	$ 27,450	$ 1,328	$ 760	$ 4,355	$ 3,669	$ 120	$ 47,819

	Three Months Ended September 30, 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	$ 6,550	$ 5,463	$ 23,523	$ 2,870	$ 730	$ 4,383	$ 4,129	$ 155	$ 47,803
Charge-offs	(447)	—	—	—	—	—	—	—	(447)
Recoveries	59	2	—	—	117	—	—	—	178
Net (charge-offs) recoveries	(388)	2	—	—	117	—	—	—	(269)
Provision for (recapture of) credit losses on loans	(557)	(120)	1,396	(126)	(140)	331	(635)	19	168
End of period balance	$ 5,605	$ 5,345	$ 24,919	$ 2,744	$ 707	$ 4,714	$ 3,494	$ 174	$ 47,702

	Nine Months Ended September 30, 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	(1,042)	—	—	—	—	—	—	(300)	(1,342)
Recoveries	300	24	—	—	71	—	—	—	395
Net (charge-offs) recoveries	(742)	24	—	—	71	—	—	(300)	(947)
Provision for (recapture of) credit losses on loans	(394)	275	2,127	(1,024)	45	(698)	244	233	808
End of period balance	$ 4,717	$ 5,420	$ 27,450	$ 1,328	$ 760	$ 4,355	$ 3,669	$ 120	$ 47,819

	Nine Months Ended September 30, 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	(605)	—	—	—	(246)	—	—	—	(851)
Recoveries	247	10	—	—	324	—	—	—	581
Net (charge-offs) recoveries	(358)	10	—	—	78	—	—	—	(270)
Provision for (recapture of) credit losses on loans	(654)	(416)	2,784	(197)	(37)	1,348	(2,413)	45	460
End of period balance	$ 5,605	$ 5,345	$ 24,919	$ 2,744	$ 707	$ 4,714	$ 3,494	$ 174	$ 47,702

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

	September 30, 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	$ 620	$ 132	$ 460	$ 1,212
Real estate:				
CRE - Owner Occupied	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—
Land and construction	5,862	—	—	5,862
Home equity	84	—	—	84
Total	$ 6,566	$ 132	$ 460	$ 7,158

	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 at the dates indicated:

	September 30, 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	$ 4,390	$ 1,755	$ 1,082	$ 7,227	$ 474,039	$ 481,266
Real estate:						
CRE - Owner Occupied	—	—	—	—	602,062	602,062
CRE - Non-Owner Occupied	4,513	—	—	4,513	1,306,065	1,310,578
Land and construction	—	—	5,862	5,862	119,899	125,761
Home equity	659	—	—	659	123,431	124,090
Multifamily	—	—	—	—	273,103	273,103
Residential mortgages	—	—	—	—	479,524	479,524
Consumer and other	—	—	—	—	14,179	14,179
Total	$ 9,562	$ 1,755	$ 6,944	$ 18,261	$ 3,392,302	$ 3,410,563

	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 at the dates indicated:

	September 30, 2024	December 31, 2023
	(Dollars in thousands)	
Past due nonaccrual loans	$ 6,484	$ 6,100
Current nonaccrual loans	214	718
Total nonaccrual loans	$ 6,698	$ 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

Credit quality indicators, specifically the Company's internal risk rating systems, reflect how the Company monitors credit losses and represents factors used by the Company when measuring the allowance for credit losses. Descriptions of the Company’s credit quality indicators by financial asset are included in Note 4 “*Loans and Allowance for Credit Losses on Loans*” of the 2023 Form 10-K.

The following tables show the Company’s loan portfolio by credit quality indicator and year of origination at September 30, 2024 and December 31, 2023. The loan categories are based on the loan segmentation in the Company's

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current expected credit loss ("CECL") reserve methodology for the calculation of the allowance for credit losses on loans based on loan purpose and type.

	Term Loans Amortized Cost Basis by Originated Period as of September 30, 2024						Revolving Loans Amortized	
	2024	2023	2022	2021	2020	Prior Periods	Cost Basis	Total
				(Dollars in thousands)				
Commercial:								
Pass	$ 89,567	$ 27,960	$ 18,909	$ 17,627	$ 11,351	$ 30,452	$ 275,491	$ 471,357
Special Mention	3,029	—	358	131	—	185	200	3,903
Substandard	—	147	592	—	—	4,415	100	5,254
Substandard-Nonaccrual	—	—	—	223	—	529	—	752
Total	92,596	28,107	19,859	17,981	11,351	35,581	275,791	481,266
CRE - Owner Occupied:								
Pass	42,069	31,845	83,140	102,419	66,720	253,342	9,407	588,942
Special Mention	—	—	—	8,282	447	1,217	—	9,946
Substandard	—	—	—	—	3,174	—	—	3,174
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	42,069	31,845	83,140	110,701	70,341	254,559	9,407	602,062
CRE - Non-Owner Occupied:								
Pass	97,037	223,427	232,175	255,074	27,272	446,572	3,833	1,285,390
Special Mention	—	—	4,841	2,201	—	1,279	—	8,321
Substandard	—	—	—	4,514	—	11,753	600	16,867
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	97,037	223,427	237,016	261,789	27,272	459,604	4,433	1,310,578
Land and construction:								
Pass	26,745	43,646	30,987	15,984	214	—	—	117,576
Special Mention	—	—	—	—	—	2,323	—	2,323
Substandard	—	—	—	—	—	—	—	—
Substandard-Nonaccrual	—	—	—	3,815	966	1,081	—	5,862
Total	26,745	43,646	30,987	19,799	1,180	3,404	—	125,761
Home equity:								
Pass	—	—	—	—	—	2,098	119,357	121,455
Special Mention	—	—	—	—	—	—	2,110	2,110
Substandard	—	—	—	—	—	—	441	441
Substandard-Nonaccrual	—	—	—	—	—	84	—	84
Total	—	—	—	—	—	2,182	121,908	124,090
Multifamily:								
Pass	13,397	46,528	39,833	54,067	5,286	113,429	563	273,103
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	13,397	46,528	39,833	54,067	5,286	113,429	563	273,103
Residential mortgage:								
Pass	3,937	1,665	184,031	255,131	1,014	33,570	—	479,348
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	176	—	176
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	3,937	1,665	184,031	255,131	1,014	33,746	—	479,524
Consumer and other:								
Pass	175	674	1,339	48	—	1,998	9,871	14,105
Special Mention	—	—	—	—	—	74	—	74
Substandard	—	—	—	—	—	—	—	—
Substandard-Nonaccrual	—	—	—	—	—	—	—	—
Total	175	674	1,339	48	—	2,072	9,871	14,179
Total loans	$ 275,956	$ 375,892	$ 596,205	$ 719,516	$ 116,444	$ 904,577	$ 421,973	$ 3,410,563
Risk Grades:								
Pass	$ 272,927	$ 375,745	$ 590,414	$ 700,350	$ 111,857	$ 881,461	$ 418,522	$ 3,351,276
Special Mention	3,029	—	5,199	10,614	447	5,078	2,310	26,677
Substandard	—	147	592	4,514	3,174	16,344	1,141	25,912
Substandard-Nonaccrual	—	—	—	4,038	966	1,694	—	6,698
Grand Total	$ 275,956	$ 375,892	$ 596,205	$ 719,516	$ 116,444	$ 904,577	$ 421,973	$ 3,410,563

	Term Loans Amortized Cost Basis by Originated Period as of December 31, 2023						Revolving Loans Amortized Cost Basis	Total
	2023	2022	2021	2020	2019	Prior Periods		
	(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 September 30, 2024							
	2024	2023	2022	2021	2020	Prior Periods	Revolving Loans	Total
	(Dollars in thousands)							
Commercial	$ —	$ —	$ —	$ —	$ —	$ 25	$ 149	$ 174
Real estate:								
CRE - Owner Occupied	—	—	—	—	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—	—	—	—	—
Land and construction	—	—	—	—	—	—	—	—
Home equity	—	—	—	—	—	—	—	—
Multifamily	—	—	—	—	—	—	—	—
Residential mortgages	—	—	—	—	—	—	—	—
Consumer and other	—	—	—	—	—	—	300	300
Total	$ —	$ —	$ —	$ —	$ —	$ 25	$ 449	$ 474

	Gross Charge-offs by Originated Period for the Three Months Ended September 30, 2023							
	2023	2022	2021	2020	2019	Prior Periods	Revolving Loans	Total
	(Dollars in thousands)							
Commercial	$ 1	$ 45	$ —	$ —	$ 229	$ 172	$ —	$ 447
Real estate:								
CRE - Owner Occupied	—	—	—	—	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—	—	—	—	—
Land and construction	—	—	—	—	—	—	—	—
Home equity	—	—	—	—	—	—	—	—
Multifamily	—	—	—	—	—	—	—	—
Residential mortgages	—	—	—	—	—	—	—	—
Consumer and other	—	—	—	—	—	—	—	—
Total	$ 1	$ 45	$ —	$ —	$ 229	$ 172	$ —	$ 447

	Gross Charge-offs by Originated Period for the Nine Months Ended September 30, 2024							
	2024	2023	2022	2021	2020	Prior Periods	Revolving Loans	Total
	(Dollars in thousands)							
Commercial	$ —	$ 416	$ —	$ —	$ —	$ 477	$ 149	$ 1,042
Real estate:								
CRE - Owner Occupied	—	—	—	—	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—	—	—	—	—
Land and construction	—	—	—	—	—	—	—	—
Home equity	—	—	—	—	—	—	—	—
Multifamily	—	—	—	—	—	—	—	—
Residential mortgages	—	—	—	—	—	—	—	—
Consumer and other	—	—	—	—	—	—	300	300
Total	$ —	$ 416	$ —	$ —	$ —	$ 477	$ 449	$ 1,342

	Gross Charge-offs by Originated Period for the Nine Months Ended September 30, 2023							
	2023	2022	2021	2020	2019	Prior Periods	Revolving Loans	Total
	(Dollars in thousands)							
Commercial	$ 1	$ 49	$ —	$ —	$ 278	$ 277	$ —	$ 605
Real estate:								
CRE - Owner Occupied	—	—	—	—	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—	—	—	—	—
Land and construction	—	—	—	—	—	—	—	—
Home equity	—	—	—	—	—	—	246	246
Multifamily	—	—	—	—	—	—	—	—
Residential mortgages	—	—	—	—	—	—	—	—
Consumer and other	—	—	—	—	—	—	—	—
Total	$ 1	$ 49	$ —	$ —	$ 278	$ 277	$ 246	$ 851

The amortized cost basis of collateral-dependent loans at September 30, 2024 and December 31, 2023 was $132,000 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 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 method 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.

During the three months ended September 30, 2024, there were no loan modifications to borrowers experiencing financial difficulty. During the three months ended September 30, 2023, there were commercial loan modifications with a payment delay totaling $25,000, representing 0.01% of the total class of financing receivables. During the nine months ended September 30, 2024, there were commercial loan modifications with a term extension totaling $15,000, representing 0.00% of the total class of financing receivables, and included a weighted average term extension of 12 months. During the nine months ended September 30, 2023, there were commercial loan modifications with a payment delay totaling $79,000, a combination term extension and interest rate reduction totaling $ 2,000, representing 0.02% of the total class of financing receivables, and included principal forgiveness totaling $3,000, a weighted average interest rate reduction of 0.25%, and a weighted average term extension of 14 months.

The Company has not committed to lend any additional amounts to these borrowers. There were no payment defaults for loans modified for the three and nine months ended September 30, 2024 and September 30, 2023.

6) Goodwill and Other Intangible Assets

Goodwill

At September 30, 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, the Bank's factoring subsidiary, $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.

On a quarterly basis, management assesses whether it is necessary to perform a quantitative impairment test of goodwill. Management concluded that there were no triggering events and circumstances that would indicate that the fair value of the reporting unit is less that its carrying amount as of September 30, 2024. In addition, the Company hires a third party vendor to test goodwill for impairment annually as of November 30, or on an interim basis if an event triggering impairment assessment may have occurred. Potential impairment indicators considered include the condition of the economy and banking industry; government intervention and regulatory updates; the impact of recent events to financial performance and cost factors of the reporting units; performance of the Company's stock and other relevant events. 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 carrying 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:

	September 30, 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:

	September 30, 2024		
	Gross Carrying Amount	Accumulated Amortization	Total
	(Dollars in thousands)		
Core deposit intangibles	$ 25,023	(18,164)	$ 6,859
Customer relationship and brokered relationship intangibles	1,900	(1,883)	17
Below market leases	110	(20)	90
Total	$ 27,033	$ (20,067)	$ 6,966

	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 September 30, 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	$ 505	$ 17	$ 4	$ 526
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
	$ 6,859	$ 17	$ 90	$ 6,966

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 September 30, 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 $ 26,390,000 and $29,765,000, at September 30, 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 September 30, 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:

	September 30, 2024	December 31, 2023
	(Dollars in thousands)	
Low income housing investments	$ 2,349	$ 2,794
Future commitments	$ 491	$ 494

The Company expects $11,000 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 September 30, 2024 and 2023, respectively, and low income housing investment expense of $148,000 and $186,000, respectively. For tax purposes, the Company had low income housing tax credit of $ 422,000 and $540,000 for the nine months ended September 30, 2024 and 2023, respectively, and low income housing investment expense of $445,000 and $557,000, 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. While the Plan remains active for those participants, the Company has not approved any new participation in the Plan since 2011. 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 September 30,		Nine Months Ended September 30,	
	2024	2023	2024	2023
	(Dollars in thousands)			
Components of net periodic benefit cost:				
Service cost	$ 52	$ 48	$ 154	$ 144
Interest cost	318	324	954	972
Amortization of net actuarial loss	26	13	78	39
Net periodic benefit cost	$ 396	$ 385	$ 1,186	$ 1,155
Amount recognized in other comprehensive income (loss)	$ 18	$ 9	$ 54	$ 27

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:

	September 30, 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	259	365
Actuarial loss	—	(474)
Projected benefit obligation at end of period	$ 7,210	$ 6,951

	September 30, 2024	December 31, 2023
	(Dollars in thousands)	
Net actuarial loss	$ (2,332)	$ (2,108)
Prior transition obligation	(633)	(701)
Accumulated other comprehensive income (loss)	$ (2,965)	$ (2,809)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2024	2023	2024	2023
	(Dollars in thousands)			
Amortization of prior transition obligation and actuarial losses	$ (53)	$ (48)	$ (157)	$ (143)
Interest cost	87	92	259	274
Net periodic benefit cost	$ 34	$ 44	$ 102	$ 131
Amount recognized in other comprehensive income (loss)	$ (53)	$ (48)	$ (157)	$ (143)

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 September 30, 2024				
Available-for-sale securities:				
U.S. Treasury	$ 184,162	$ 184,162	$ —	$ —
Agency mortgage-backed securities	53,450	—	53,450	—
I/O strip receivables	95	—	95	—
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 September 30, 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 September 30, 2024 and December 31, 2023, there were no foreclosed assets on the balance sheet.

The carrying amounts and estimated fair values of the Company's financial instruments at September 30, 2024 are as follows:

		Estimated Fair Value			
	Carrying Amounts	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	$ 956,310	$ 956,310	$ —	$ —	$ 956,310
Securities available-for-sale	237,612	184,162	53,450	—	237,612
Securities held-to-maturity	604,193	—	531,533	—	531,533
Loans (including loans held-for-sale)	3,411,885 (1)	—	1,649	3,246,881	3,248,530
FHLB stock, FRB stock, and other investments	32,553	—	—	—	N/A
Accrued interest receivable	15,220	604	3,020	11,596	15,220
I/O strips receivables	95	—	95	—	95
Liabilities:					
Time deposits	$ 523,396	$ —	$ 525,656	$ —	$ 525,656
Other deposits	4,206,137	—	4,206,137	—	4,206,137
Subordinated debt	39,615	—	33,215	—	33,215
Accrued interest payable	7,037	—	7,037	—	7,037

(1) Before allowance for credit losses on loans of $ 47,819,000.

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

		Estimated Fair Value			
	Carrying Amounts	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. Each RSU granted to non-executive employees generally vests ratably over three years. For the nine months ended September 30, 2024, the Company granted 273,841 RSUs. 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 941,181 shares available for the issuance of equity awards under the 2023 Plan as of September 30, 2024.

The executive officers that participate in the Company's Long Term Incentive Equity Program receive 50% of their award value in RSUs and 50% of their award value in PRSUs contingent on 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 nine months ended September 30, 2024, the Company granted 149,923 shares of PRSUs.

Restricted stock is subject to time vesting. Restricted stock granted to the Board of Directors generally vests in one year. For the nine months ended September 30, 2024, the Company granted 57,213 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	(88,764)	$ 5.39		
Forfeited or expired	(222,399)	$ 10.58		
Outstanding at September 30, 2024	2,326,193	$ 10.58	5.07	$ 1,867,043
Vested or expected to vest	2,186,621		5.07	$ 1,755,020
Exercisable at September 30, 2024	1,898,485		4.39	$ 1,328,659

The table below provides information related to stock option activity under the Equity Plans for the periods indicated:

	Nine Months Ended September 30,	
	2024	2023
Intrinsic value of options exercised	$ 321,882	$ 620,013
Cash received from option exercise	$ 478,358	$ 996,453
Tax (expense) benefit realized from option exercises	$ (17,785)	$ (5,902)
Weighted average fair value of options granted	N/A	$ 1.32

As of September 30, 2024, there was $ 724,000 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 1.94 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
Vested	(123,260)	$ 9.12
Forfeited or expired	(31,215)	$ 11.43
Nonvested shares at September 30, 2024	88,061	$ 9.45

As of September 30, 2024, there was $ 482,000 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 0.73 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	273,841	$ 8.47
Vested	(35,837)	$ 7.46
Forfeited or expired	(40,589)	$ 7.84
Nonvested shares at September 30, 2024	316,777	$ 8.26

As of September 30, 2024, there were $ 2,136,000 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 2.32 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	(39,862)	$ 7.75
Nonvested shares at September 30, 2024	229,419	$ 8.06

As of September 30, 2024, there were $ 1,307,000 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 2.20 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 at the dates indicated:

	September 30, 2024			
	Collateral Value	Total Available	Outstanding	Remaining Available
	(Dollars in thousands)			
FHLB collateralized borrowing capacity	$ 1,204,712	$ 765,134	$ —	$ 765,134
FRB discount window collateralized line of credit	1,755,474	1,397,326	—	1,397,326
Federal funds purchase arrangements	N/A	90,000	—	90,000
Holding company line of credit	N/A	25,000	—	25,000
	$ 2,960,186	$ 2,277,460	$ —	$ 2,277,460

	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 September 30, 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 $385,000, totaled $39,615,000 at September 30, 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 September 30, 2024. There are no conditions or events since September 30, 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 September 30, 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 at the dates indicated:

	Actual		Required For Capital Adequacy Purposes Under Basel III	
	Amount	**Ratio**	**Amount**	**Ratio (1)**
	(Dollars in thousands)			
As of September 30, 2024				
Total Capital (to risk-weighted assets)	$ 605,396	15.6 %	$ 406,919	10.5 %
Tier 1 Capital (to risk-weighted assets)	$ 520,133	13.4 %	$ 329,411	8.5 %
Common Equity Tier 1 Capital (to risk-weighted assets)	$ 520,133	13.4 %	$ 271,279	7.0 %
Tier 1 Capital (to average assets)	$ 520,133	10.0 %	$ 207,279	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.

The Subordinated Debt, net of unamortized issuance costs, totaled $ 39,615,000 at September 30, 2024, and qualifies as Tier 2 capital for the Company under the guidelines established by the Federal Reserve Board.

HBC's actual capital amounts and ratios are presented in the following table, together with capital adequacy requirements, under the Basel III regulatory requirements at the dates 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 September 30, 2024						
Total Capital (to risk-weighted assets)	$ 585,034	15.1 %	$ 387,242	10.0 %	$ 406,604	10.5 %
Tier 1 Capital (to risk-weighted assets)	$ 539,386	13.9 %	$ 309,793	8.0 %	$ 329,156	8.5 %
Common Equity Tier 1 Capital (to risk-weighted assets)	$ 539,386	13.9 %	$ 251,707	6.5 %	$ 271,069	7.0 %
Tier 1 Capital (to average assets)	$ 539,386	10.4 %	$ 258,949	5.0 %	$ 207,159	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.

Under the 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 September 30, 2024, HBC would not be required to obtain regulatory approval, and the amount available for cash dividends is $71,477,000. HBC distributed to HCC dividends of $ 8,000,000 during the first, second, and third quarters of 2024 for a total of $24,000,000.

13) Commitments and Loss Contingencies

Loss Contingencies

Within the ordinary course of our business, we are from time to time subject to private lawsuits, government audits and examinations, administrative proceedings and other claims. Under certain circumstances, we also may be subjected to increased risk associated with the acts or omissions of our clients (such as clients who, unbeknownst to the Bank or the Company, may engage in or become 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 ultimately determined to be liable.

At September 30, 2024, the Company was the subject of three pending legal proceedings (excluding pending and potential litigation arising in the ordinary course of business) each of which was an employment-related action asserted between November 2020 and October 2021. Two of 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 third such claim is an individual claim alleging race and gender discrimination, wage violations, and a variety of other claims. The claimants in all three actions allege various instances of disability, race and gender discrimination, wage-and-hour violations, retaliation, and related claims. Two of these cases remain pending in Alameda County Superior Court following a series of motions and interlocutory appeals, and are currently set for trial late in the summer of 2025. The third claim was substantially resolved through mediation in October 2024, after the period covered by the accompanying financial statements, for an amount that is immaterial to the Company's financial condition and results of operations. The Company contends that the claims are without merit and intends 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 always 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, once made, may prove inaccurate.

At this time, we believe that the amount of reasonably possible losses resulting from final disposition of pending or threatened 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, and that, associated with the defense of such claims, we may incur elevated levels of attorney fees and other litigation costs. Likewise, factors that affect the insurance coverage for these matters may affect our estimates of the relevant contingent liabilities, and we generally adjust our estimates based on known factors that affect that coverage as those factors come to light. 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 clients 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 $1,117,775,000 at September 30, 2024, and $ 1,149,056,000 at December 31, 2023. Unused commitments represented 33% and 34% of outstanding gross loans at September 30, 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 at the dates indicated:

	September 30, 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	$ 122,471	$ 972,291	$ 1,094,762	$ 96,166	$ 1,041,608	$ 1,137,774
Standby letters of credit	6,178	16,835	23,013	4,283	6,999	11,282
	$ 128,649	$ 989,126	$ 1,117,775	$ 100,449	$ 1,048,607	$ 1,149,056

For the nine months ended September 30, 2024, there was a decrease of ($ 111,000) 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 nine months of 2024 was driven by a decline in the loss factor due to an improved forecast 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 $656,000 at September 30, 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 clients fees that are not specifically related to the client 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 client 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 client behavior. An example would be where we do not charge a monthly service fee, or do not charge for certain transactions, for clients 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 clients' 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 ASU 2020-05 Revenue from Contracts with Customers (Topic 606), for the periods indicated:

	Three Months Ended September 30,	
	2024	2023
	(Dollars in thousands)	
Noninterest Income In-scope of Topic 606:		
Service charges and fees on deposit accounts	$ 908	$ 859
Total noninterest income in-scope of Topic 606	908	859
Noninterest Income Out-of-scope of Topic 606	1,332	1,357
Total noninterest income	$ 2,240	$ 2,216

	Nine Months Ended September 30,	
	2024	2023
	(Dollars in thousands)	
Noninterest Income In-scope of Topic 606:		
Service charges and fees on deposit accounts	$ 2,676	$ 3,503
Total noninterest income in-scope of Topic 606	2,676	3,503
Noninterest Income Out-of-scope of Topic 606	3,887	3,553
Total noninterest income	$ 6,563	$ 7,056

15) Noninterest Expense

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2024	2023	2024	2023
	(Dollars in thousands)			
Salaries and employee benefits	$ 15,673	$ 14,147	$ 46,976	$ 42,943
Occupancy and equipment	2,599	2,301	7,731	7,123
Insurance expense	1,715	1,595	4,988	4,627
Professional fees	1,306	717	3,705	3,265
Client services	809	682	2,497	1,633
Data processing	800	906	2,635	2,593
Software subscriptions	743	682	2,034	1,903
Other	3,910	4,141	12,713	11,476
Total noninterest expense	$ 27,555	$ 25,171	$ 83,279	$ 75,563

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 September 30, 2024, operating lease ROU assets, included in other assets, and lease liabilities, included in other liabilities, totaled $31,912,000.

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2024	2023	2024	2023
	(Dollars in thousands)			
Operating Lease Cost (Cost resulting from lease payments)	$ 1,727	$ 1,677	$ 5,125	$ 5,087
Operating Lease - Operating Cash Flows (Fixed Payments)	$ 1,764	$ 1,678	$ 5,165	$ 5,026
Operating Lease - ROU assets	$ 31,912	$ 31,979	$ 31,912	$ 31,979
Operating Lease - Liabilities	$ 31,912	$ 31,979	$ 31,912	$ 31,979
Weighted Average Lease Term - Operating Leases	5.32 years	6.10 years	5.32 years	6.10 years
Weighted Average Discount Rate - Operating Leases	5.56%	4.86%	5.56%	4.86%

The following maturity analysis shows the undiscounted cash flows due on the Company’s operating lease liabilities as of September 30, 2024:

	(Dollars in thousands)
2024 remaining	$ 1,778
2025	7,145
2026	6,603
2027	6,380
2028	5,779
Thereafter	9,457
Total undiscounted cash flows	37,142
Discount on cash flows	(5,230)
Total lease liability	$ 31,912

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 September 30, 2024		
	Banking (1)	**Factoring**	**Consolidated**
	(Dollars in thousands)		
Interest income	$ 59,294	$ 2,144	$ 61,438
Intersegment interest allocations	470	(470)	—
Total interest expense	21,523	—	21,523
Net interest income	38,241	1,674	39,915
Provision for (recapture of) credit losses on loans	186	(33)	153
Net interest income after provision	38,055	1,707	39,762
Noninterest income	1,982	258	2,240
Noninterest expense	25,808	1,747	27,555
Intersegment expense allocations	121	(121)	—
Income before income taxes	14,350	97	14,447
Income tax expense	3,911	29	3,940
Net income	$ 10,439	$ 68	$ 10,507
Total assets	$ 5,466,494	$ 85,102	$ 5,551,596
Loans, net of deferred fees	$ 3,353,037	$ 57,199	$ 3,410,236
Goodwill	$ 154,587	$ 13,044	$ 167,631

	Three Months Ended September 30, 2023		
	Banking (1)	**Factoring**	**Consolidated**
	(Dollars in thousands)		
Interest income	$ 58,016	$ 2,775	$ 60,791
Intersegment interest allocations	397	(397)	—
Total interest expense	15,419	—	15,419
Net interest income	42,994	2,378	45,372
Provision for (recapture of) credit losses on loans	254	(86)	168
Net interest income after provision	42,740	2,464	45,204
Noninterest income	2,044	172	2,216
Noninterest expense	23,588	1,583	25,171
Intersegment expense allocations	109	(109)	—
Income before income taxes	21,305	944	22,249
Income tax expense	6,175	279	6,454
Net income	$ 15,130	$ 665	$ 15,795
Total assets	$ 5,314,922	$ 88,385	$ 5,403,307
Loans, net of deferred fees	$ 3,233,379	$ 52,082	$ 3,285,461
Goodwill	$ 154,587	$ 13,044	$ 167,631

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

	Nine Months Ended September 30, 2024		
	Banking (1)	Factoring	Consolidated
	(Dollars in thousands)		
Interest income	$ 170,170	$ 7,896	$ 178,066
Intersegment interest allocations	1,346	(1,346)	—
Total interest expense	58,603	—	58,603
Net interest income	112,913	6,550	119,463
Provision for credit losses on loans	556	252	808
Net interest income after provision	112,357	6,298	118,655
Noninterest income	6,030	533	6,563
Noninterest expense	78,438	4,841	83,279
Intersegment expense allocations	381	(381)	—
Income before income taxes	40,330	1,609	41,939
Income tax expense	11,556	476	12,032
Net income	$ 28,774	$ 1,133	$ 29,907
Total assets	$ 5,466,494	$ 85,102	$ 5,551,596
Loans, net of deferred fees	$ 3,353,037	$ 57,199	$ 3,410,236
Goodwill	$ 154,587	$ 13,044	$ 167,631

	Nine Months Ended September 30, 2023		
	Banking (1)	Factoring	Consolidated
	(Dollars in thousands)		
Interest income	$ 164,783	$ 10,623	$ 175,406
Intersegment interest allocations	1,626	(1,626)	—
Total interest expense	34,483	—	34,483
Net interest income	131,926	8,997	140,923
Provision (recapture) for credit losses on loans	807	(347)	460
Net interest income after provision	131,119	9,344	140,463
Noninterest income	6,743	313	7,056
Noninterest expense	70,645	4,918	75,563
Intersegment expense allocations	435	(435)	—
Income before income taxes	67,652	4,304	71,956
Income tax expense	19,572	1,269	20,841
Net income	$ 48,080	$ 3,035	$ 51,115
Total assets	$ 5,314,922	$ 88,385	$ 5,403,307
Loans, net of deferred fees	$ 3,233,379	$ 52,082	$ 3,285,461
Goodwill	$ 154,587	$ 13,044	$ 167,631

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

18) Subsequent Events

On October 24, 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 November 21, 2024, to shareholders of record at the close of the business day on November 7, 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 ("2023 Form 10-K") 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

The Company conducts a general commercial banking business through the Bank. Our primary 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. Our 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 Bank's clients are primarily closely held businesses and professionals. We also have limited operations in other regions primarily by virtue of Bay View Funding, the Bank's factoring subsidiary, which provides factoring and other alternative corporate financing services.

Performance Overview

For the three months ended September 30, 2024, net income was $10.5 million, or $0.17 per average diluted common share, compared to $15.8 million, or $0.26 per average diluted common share, for the three months ended September 30, 2023. The Company's annualized return on average assets was 0.78% and annualized return on average equity was 6.14% for the three months ended September 30, 2024, compared to 1.16% and 9.54%, respectively, for the three months ended September 30, 2023. The Company's annualized return on average tangible assets was 0.81% and annualized return on average tangible common equity was 8.27% for the three months ended September 30, 2024, compared to 1.20% and 13.06%, respectively, for the three months ended September 30, 2023. The annualized return on average tangible assets and annualized return on average tangible common equity are non-GAAP financial measures.

For the nine months ended September 30, 2024, net income was $29.9 million, or $0.49 per average diluted common share, compared to $51.1 million, or $0.83 per average diluted common share, for the nine months ended September 30, 2023. The Company's annualized return on average assets was 0.76% and annualized return on average equity was 5.91% for the nine months ended September 30, 2024, compared to 1.29% and 10.54%, respectively, for the nine months ended September 30, 2023. The Company's annualized return on average tangible assets was 0.79% and annualized return on average tangible common equity was 7.98% for the nine months ended September 30, 2024, compared to 1.33% and 14.52%, respectively, for the nine months ended September 30, 2023. The annualized return on average tangible assets and annualized return on average tangible common equity are non-GAAP financial measures.

Third Quarter 2024 Highlights

Results of Operations:

- Net interest income decreased (12%) to $39.9 million for the third quarter of 2024, compared to $45.4 million for the third quarter of 2023. The non-GAAP fully tax equivalent ("FTE") net interest margin contracted 40 basis points to 3.17% for the third quarter of 2024, from 3.57% for the third quarter of 2023, primarily due to higher rates paid on client deposits, a decrease in the average balance of noninterest-bearing demand deposits, and a decrease in average interest earning assets, partially offset by a higher average yield on core loans and a higher average balance of loans.

- For the first nine months of 2024, net interest income decreased (15%) to $119.5 million, compared to $140.9 million for the first nine months of 2023. The non-GAAP FTE net interest margin contracted 54 basis points to 3.26% for the first nine months of 2024, from 3.80% for the first nine months of 2023, primarily due to higher rates paid on client deposits, a decrease in the average balance of noninterest-bearing demand deposits, and a decrease in average interest earning assets, partially offset by an increase in the yield on core loans and overnight funds and a higher average balance of loans.

- The average yield on the total loan portfolio decreased to 5.42% for the third quarter of 2024, compared to 5.46% for the third quarter of 2023.

- The average yield on the total loan portfolio decreased to 5.45% for the first nine months of 2024, compared to 5.46% for the first nine months of 2023, primarily due to a lower average balance of Bay View Funding factored receivables, a decrease in the accretion of loan purchase discount into interest income from acquired loans, and lower prepayment fees, mostly offset by increases in the prime rate for the first nine months of 2024.

- In aggregate, the unamortized net purchase discount on total loans acquired was $2.5 million at September 30, 2024.

- The average cost of total deposits increased to 1.84% for the third quarter of 2024, compared to 1.29% for the third quarter of 2023.

- The average cost of total deposits increased to 1.72% for the first nine months of 2024, compared to 0.94% for the first nine months of 2023.

- During the third quarter of 2024, we recorded a provision for credit losses on loans of $153,000, compared to a provision for credit losses on loans of $168,000 for the third quarter of 2023. There was a provision for credit losses on loans of $808,000 for the nine months ended September 30, 2024, compared to a provision for credit losses on loans of $460,000 for the nine months ended September 30, 2023.

- Total noninterest income was relatively flat at $2.2 million for both the third quarter of 2024 and the third quarter of 2023.

- Total noninterest income decreased (7%) to $6.6 million for the first nine months of 2024, compared to $7.1 million for the first nine months of 2023, primarily due to lower service charges and fees on deposit accounts, partially offset by a higher gain on proceeds from company-owned life insurance for the first nine months of 2024.

- Total noninterest expense for the third quarter of 2024 increased to $27.6 million, compared to $25.2 million for the third quarter of 2023, primarily due to higher salaries and employee benefits, rent expense included in occupancy and equipment, and professional fees.

- Total noninterest expense for the first nine months of 2024 increased to $83.3 million, compared to $75.6 million for the first nine months of 2023, primarily due to higher salaries and employee benefits, rent expense, and information technology related expenses, marketing related expenses, regulatory assessments, and ICS/CDARS fee expense included in other noninterest expense.

- The efficiency ratio as 65.37% for the third quarter of 2024, compared to 52.89% for the third quarter of 2023. The efficiency ratio increased to 66.08% for the nine months ended September 30, 2024, compared to 51.06% for the nine months ended September 30, 2023. The increase in the efficiency ratio for the third quarter of 2024 and nine months ended September 30, 2024, compared to the respective periods in 2023, was due to both higher noninterest expense and lower net revenue. The efficiency ratio is a non-GAAP financial measure.

- Income tax expense was $3.9 million for the third quarter of 2024, compared to $6.5 million for the third quarter of 2023. Income tax expense for the nine months ended September 30, 2024 was $12.0 million, compared to $20.8 million for the nine months ended September 30, 2023.

Financial Condition and Liquidity Position:

- Our liquidity, including cash on hand, undrawn lines of credit, and other sources of liquidity, totaled $3.2 billion, or 66% of the Company's total deposits and approximately 147% of the Bank's estimated uninsured deposits, at September 30, 2024. The Bank's uninsured deposits were approximately $2.2 billion, or 47% of the Company's total deposits, at September 30, 2024. The following table shows our liquidity, available lines of credit and the amounts outstanding at September 30, 2024:

	Total Available	Outstanding	Remaining Available
	(Dollars in thousands)		
Excess funds at the Federal Reserve Bank ("FRB")	$ 903,900	$ —	$ 903,900
FRB discount window collateralized line of credit	1,397,326	—	1,397,326
Federal Home Loan Bank ("FHLB") collateralized borrowing capacity	765,134	—	765,134
Unpledged investment securities (at fair value)	66,158	—	66,158
Federal funds purchase arrangements	90,000	—	90,000
Holding company line of credit	25,000	—	25,000
Total	$ 3,247,518	$ —	$ 3,247,518

- Cash, interest-bearing deposits in other financial institutions and securities available-for-sale, at fair value, increased 8% to $1.2 billion at September 30, 2024, from $1.1 billion at September 30, 2023, and increased 40% from $850.8 million at December 31, 2023.

- Securities held-to-maturity, at amortized cost, totaled $604.2 million at September 30, 2024, compared to $664.7 million at September 30, 2023, and $650.6 million, at December 31, 2023.

- The pre-tax unrealized loss on the securities available-for-sale portfolio was ($4.4) million, or ($3.2) million net of taxes, which equaled less than 1% of total shareholders' equity at September 30, 2024. The pre-tax unrealized loss on the securities held-to-maturity portfolio was ($72.7) million at September 30, 2024, or ($51.2) million net of taxes, which equaled 7.5% of total shareholders' equity at September 30, 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 1.32 years, the weighted average life of the securities held-to-maturity portfolio was 5.94 years, and the average life of the total investment securities portfolio was 4.62 years at September 30, 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 (Par Value)	Agency Mortgage-backed and Municipal Securities	Total
	(Dollars in thousands)		
Fourth quarter of 2024	9,000	26,727	$ 35,727
First quarter of 2025	35,000	21,336	56,336
Second quarter of 2025	118,000	20,700	138,700
Third quarter of 2025	25,500	21,585	47,085
Fourth quarter of 2025	—	19,486	19,486
First quarter of 2026	—	19,001	19,001
Second quarter of 2026	—	18,349	18,349
Third quarter of 2026	—	18,645	18,645
Total	$ 187,500	$ 165,829	$ 353,329

- Loans, excluding loans held-for-sale, increased $124.8 million, or 4%, to $3.4 billion at September 30, 2024, compared to $3.3 billion at September 30, 2023, and increased $59.9 million or 2% from December 31, 2023. Loans, excluding residential mortgages, increased $148.3 million, or 5%, to $2.9 billion at September 30, 2024, compared to $2.8 billion at September 30, 2023, and increased $77.3 million, or 3%, from December 31, 2023.

- Loan growth continued at an orderly organic rate as the Bank continues to serve our clients in the community.

- There were 10 borrowers included in nonperforming assets (“NPAs”) totaling $7.2 million, or 0.13% of total assets, at September 30, 2024, compared to 11 borrowers totaling $5.5 million, or 0.10% of total assets, at September 30, 2023, and 12 borrowers totaling $7.7 million, or 0.15% of total assets at December 31, 2023.

- Classified assets totaled $32.6 million, or 0.59% of total assets, at September 30, 2024, compared to $31.1 million, or 0.57% of total assets, at September 30, 2023, and $31.8 million, or 0.61% of total assets, at December 31, 2023.

- Net charge-offs totaled $288,000 for the third quarter of 2024, compared to $269,000 for the third 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 September 30, 2024 was $47.8 million, or 1.40% of total loans, representing 668% of total nonperforming loans. The ACLL at September 30, 2023 was $47.7 million, or 1.45% of total loans, representing 870% 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 increased $154.1 million, or 3%, to $4.7 billion at September 30, 2024, compared to $4.6 billion at September 30, 2023. Total deposits increased $351.1 million, or 8%, from $4.4 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 $997.8 million at September 30, 2024, compared to $921.2 million at September 30, 2023, and $854.1 million at December 31, 2023.

- Noninterest-bearing demand deposits increased $28.6 million, or 2%, to $1.27 billion at September 30, 2024 from $ 1.24 billion at September 30, 2023, and decreased ($20.3) million, or (2%), 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 4.26% at September 30, 2024, compared to 5.39% at September 30, 2023, and 4.46% at December 31, 2023.

- The loan to deposit ratio was 72.11% at September 30, 2024, compared to 71.81% at September 30, 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 September 30, 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	10.0 %	10.4 %	5.0 %	4.0 %
Tangible common equity / tangible assets (2)	9.5 %	9.9 %	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 clients.

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 September 30, 2024			Three Months Ended September 30, 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]	$ 3,361,140	$ 45,781	5.42 %	$ 3,257,480	$ 44,853	5.46 %
Securities — taxable	838,375	4,676	2.22 %	1,114,782	6,797	2.42 %
Securities — exempt from Federal tax [3]	31,311	282	3.58 %	32,947	293	3.53 %
Other investments, interest-bearing deposits in other financial institutions and Federal funds sold	781,039	10,758	5.48 %	646,501	8,909	5.47 %
Total interest earning assets	5,011,865	61,497	4.88 %	5,051,710	60,852	4.78 %
Cash and due from banks	33,425			35,911		
Premises and equipment, net	10,471			9,374		
Goodwill and other intangible assets	174,953			177,238		
Other assets	121,353			125,697		
Total assets	$ 5,352,067			$ 5,399,930		
Liabilities and shareholders' equity:						
Deposits:						
Demand, noninterest-bearing	$ 1,172,304			$ 1,302,606		
Demand, interest-bearing	907,346	1,714	0.75 %	1,017,686	1,730	0.67 %
Savings and money market	1,188,057	9,128	3.06 %	1,087,336	5,514	2.01 %
Time deposits — under $100	11,133	47	1.68 %	11,966	30	0.99 %
Time deposits — $100 and over	229,565	2,349	4.07 %	272,362	2,489	3.63 %
ICS/CDARS — interest-bearing demand, money market and time deposits	1,017,541	7,747	3.03 %	881,665	5,117	2.30 %
Total interest-bearing deposits	3,353,642	20,985	2.49 %	3,271,015	14,880	1.80 %
Total deposits	4,525,946	20,985	1.84 %	4,573,621	14,880	1.29 %
Short-term borrowings	32	—	0.00 %	31	—	0.00 %
Subordinated debt, net of issuance costs	39,590	538	5.41 %	39,439	539	5.42 %
Total interest-bearing liabilities	3,393,264	21,523	2.52 %	3,310,485	15,419	1.85 %
Total interest-bearing liabilities and demand, noninterest-bearing / cost of funds	4,565,568	21,523	1.88 %	4,613,091	15,419	1.33 %
Other liabilities	106,095			129,866		
Total liabilities	4,671,663			4,742,957		
Shareholders' equity	680,404			656,973		
Total liabilities and shareholders' equity	$ 5,352,067			$ 5,399,930		
Net interest income / margin		39,974	3.17 %		45,433	3.57 %
Less tax equivalent adjustment		(59)			(61)	
Net interest income		$ 39,915	3.17 %		$ 45,372	3.56 %

(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 $184,000 for the third quarter of 2024, compared to $201,000 for the third quarter of 2023. Prepayment fees totaled $4,000 for the third quarter of 2024, compared to $182,000 for the third quarter of 2023.
(3) Reflects the non-GAAP FTE adjustment for Federal tax-exempt income based on a 21% tax rate.

	Nine Months Ended September 30, 2024			Nine Months Ended September 30, 2023		
	Average Balance	Interest Income / Expense	Average Yield / Rate	Average Balance	Interest Income / Expense	Average Yield / Rate
Assets:						
Loans, gross [1][2]	$ 3,330,442	$ 135,851	5.45 %	$ 3,255,375	$ 132,993	5.46 %
Securities — taxable	940,755	16,342	2.32 %	1,140,890	20,835	2.44 %
Securities — exempt from Federal tax [3]	31,683	853	3.60 %	34,332	908	3.54 %
Other investments, interest-bearing deposits in other financial institutions and Federal funds sold	606,360	25,199	5.55 %	535,016	20,860	5.21 %
Total interest earning assets [3]	4,909,240	178,245	4.85 %	4,965,613	175,596	4.73 %
Cash and due from banks	33,353			36,205		
Premises and equipment, net	10,235			9,278		
Goodwill and other intangible assets	175,495			177,837		
Other assets	120,015			127,514		
Total assets	$ 5,248,338			$ 5,316,447		
Liabilities and shareholders' equity:						
Deposits:						
Demand, noninterest-bearing	$ 1,158,891			$ 1,444,744		
Demand, interest-bearing	919,786	4,987	0.72 %	1,117,140	4,994	0.60 %
Savings and money market	1,120,324	23,644	2.82 %	1,159,894	13,641	1.57 %
Time deposits — under $100	11,020	135	1.64 %	11,951	60	0.67 %
Time deposits — $100 and over	226,353	6,658	3.93 %	212,736	4,744	2.98 %
ICS/CDARS — interest-bearing demand, money market and time deposits	990,868	21,565	2.91 %	525,318	8,065	2.05 %
Total interest-bearing deposits	3,268,351	56,989	2.33 %	3,027,039	31,504	1.39 %
Total deposits	4,427,242	56,989	1.72 %	4,471,783	31,504	0.94 %
Short-term borrowings	22	—	0.00 %	36,283	1,365	5.03 %
Subordinated debt, net of issuance costs	39,553	1,614	5.45 %	39,401	1,614	5.48 %
Total interest-bearing liabilities	3,307,926	58,603	2.37 %	3,102,723	34,483	1.49 %
Total interest-bearing liabilities and demand, noninterest-bearing / cost of funds	4,466,817	58,603	1.75 %	4,547,467	34,483	1.01 %
Other liabilities	105,570			120,639		
Total liabilities	4,572,387			4,668,106		
Shareholders' equity	675,951			648,341		
Total liabilities and shareholders' equity	5,248,338			$ 5,316,447		
Net interest income [3] / margin		119,642	3.26 %		141,113	3.80 %
Less tax equivalent adjustment [3]		(179)			(190)	
Net interest income		$ 119,463	3.25 %		$ 140,923	3.79 %

(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 $461,000 for the first nine months of 2024, compared to $595,000 for the first nine months of 2023. Prepayment fees totaled $82,000 for the first nine months of 2024, compared to $393,000 for the first nine months of 2023.
(3) Reflects the non-GAAP FTE 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 September 30, 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	$ 1,401	$ (473)	$ 928
Securities — taxable	(1,545)	(576)	(2,121)
Securities — exempt from Federal tax [(1)]	(14)	3	(11)
Other investments, interest-bearing deposits in other financial institutions and Federal funds sold	1,853	(4)	1,849
Total interest income on interest-earning assets	1,695	(1,050)	645
Expense from the interest-bearing liabilities:			
Demand, interest-bearing	(205)	189	(16)
Savings and money market	764	2,850	3,614
Time deposits — under $100	(4)	21	17
Time deposits — $100 and over	(437)	297	(140)
CDARS — interest-bearing demand, money market and time deposits	1,032	1,598	2,630
Short-term borrowings	—	—	—
Subordinated debt, net of issuance costs	2	(3)	(1)
Total interest expense on interest-bearing liabilities	1,152	4,952	6,104
Net interest income	$ 543	$ (6,002)	(5,459)
Less tax equivalent adjustment			2
Net interest income			$ (5,457)

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

	Nine Months Ended September 30, 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	$ 3,030	$ (172)	$ 2,858
Securities — taxable	(3,473)	(1,020)	(4,493)
Securities — exempt from Federal tax (1)	(72)	17	(55)
Other investments, interest-bearing deposits in other financial institutions and Federal funds sold	2,970	1,369	4,339
Total interest income on interest-earning assets	2,455	194	2,649
Expense from the interest-bearing liabilities:			
Demand, interest-bearing	(1,035)	1,028	(7)
Savings and money market	(843)	10,846	10,003
Time deposits — under $100	(12)	87	75
Time deposits — $100 and over	399	1,515	1,914
CDARS — interest-bearing demand, money market and time deposits	10,121	3,379	13,500
Short-term borrowings	—	(1,365)	(1,365)
Subordinated debt, net of issuance costs	6	(6)	—
Total interest expense on interest-bearing liabilities	8,636	15,484	24,120
Net interest income	$ (6,181)	$ (15,290)	(21,471)
Less tax equivalent adjustment			11
Net interest income			$ (21,460)

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

Net interest income decreased (12%) to $39.9 million for the third quarter of 2024, compared to $45.4 million for the third quarter of 2023. The non-GAAP FTE net interest margin contracted 40 basis points to 3.17% for the third quarter of 2024, from 3.57% for the third quarter of 2023, primarily due to higher rates paid on client deposits, a decrease in the average balance of noninterest-bearing demand deposits, and a decrease in average interest earning assets, partially offset by a higher average yield on core loans and a higher average balance of loans.

For the first nine months of 2024, net interest income decreased (15%) to $119.5 million, compared to $140.9 million for the first nine months of 2023. The non-GAAP FTE net interest margin contracted 54 basis points to 3.26% for the first nine months of 2024, from 3.80% for the first nine months of 2023, primarily due to higher rates paid on client deposits, a decrease in the average balance of noninterest-bearing demand deposits, and a decrease in average interest earning assets, partially offset by an increase in the yield on core loans and overnight funds and a higher average balance of loans.

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

	Three Months Ended September 30, 2024			Three Months Ended September 30, 2023		
	Average Balance	Interest Income	Average Yield	Average Balance	Interest Income	Average Yield
	(Dollars in thousands)					
Loans, core bank	$ 2,867,076	$ 39,621	5.50 %	$ 2,743,993	$ 37,764	5.46 %
Prepayment fees	—	4	0.00 %	—	182	0.03 %
Bay View Funding factored receivables (1)	55,391	2,144	15.40 %	51,664	2,775	21.31 %
Purchased residential mortgages	441,294	3,779	3.41 %	465,471	3,811	3.25 %
Loan fair value mark / accretion	(2,621)	233	0.03 %	(3,648)	321	0.05 %
Total loans (includes loans held-for-sale)	$ 3,361,140	$ 45,781	5.42 %	$ 3,257,480	$ 44,853	5.46 %

(1) Interest income for the third quarter and first nine months of 2024 was reduced by an immaterial out-of-period adjustment of ($804,000).

The average yield on the total loan portfolio decreased to 5.42% for the third quarter of 2024, compared to 5.46% for the third quarter of 2023.

	Nine Months Ended September 30, 2024			Nine Months Ended September 30, 2023		
	Average Balance	Interest Income	Average Yield	Average Balance	Interest Income	Average Yield
	(Dollars in thousands)					
Loans, core bank	$ 2,831,035	$ 115,838	5.47 %	$ 2,716,345	$ 109,354	5.38 %
Prepayment fees	—	82	0.00 %	—	393	0.02 %
Bay View Funding factored receivables (1)	54,563	7,896	19.33 %	65,938	10,623	21.54 %
Purchased residential mortgages	447,709	11,306	3.37 %	477,068	11,497	3.22 %
Loan fair value mark / accretion	(2,865)	729	0.03 %	(3,976)	1,126	0.06 %
Total loans (includes loans held-for-sale)	$ 3,330,442	$ 135,851	5.45 %	$ 3,255,375	$ 132,993	5.46 %

(1) Interest income for the third quarter and first nine months of 2024 was reduced by an immaterial out-of-period adjustment of ($804,000).

The average yield on the total loan portfolio decreased to 5.45% for the first nine months of 2024, compared to 5.46% for the first nine months of 2023, primarily due to a lower average balance of Bay View Funding factored receivables, a decrease in the accretion of loan purchase discount into interest income from acquired loans, and lower prepayment fees, mostly offset by increases in the prime rate for the first nine months of 2024.

In aggregate, the remaining net purchase discount on total loans acquired was $2.5 million at September 30, 2024.

The average cost of total deposits increased to 1.84% for the third quarter of 2024, compared to 1.29% for the third quarter of 2023. The average cost of funds increased to 1.88% for the third quarter of 2024, compared to 1.33% for the third quarter of 2023. The average cost of total deposits increased to 1.72% for the first nine months of 2024, compared to 0.94% for the first nine months of 2023. The average cost of funds increased to 1.75% for the first nine months of 2024, compared to 1.01% for the first nine months of 2023.

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

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 $153,000 for the third quarter of 2024, compared to a provision for credit losses on loans of $168,000 for the third quarter of 2023. There was a provision for credit losses on loans of $808,000 for the nine months ended September 30, 2024, compared to a provision for credit losses on loans of $460,000 for the nine months ended September 30, 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 September 30,		Increase (decrease) 2024 versus 2023	
	2024	2023	Amount	Percent
	(Dollars in thousands)			
Service charges and fees on deposit accounts	$ 908	$ 859	$ 49	6 %
Increase in cash surrender value of life insurance	530	517	13	3 %
Servicing income	108	62	46	74 %
Gain on sales of SBA loans	94	207	(113)	(55)%
Termination fees	46	118	(72)	(61)%
Gain on proceeds from company-owned life insurance	—	100	(100)	(100)%
Other	554	353	201	57 %
Total	$ 2,240	$ 2,216	$ 24	1 %

	Nine Months Ended September 30,		Increase (decrease) 2024 versus 2023	
	2024	2023	Amount	Percent
	(Dollars in thousands)			
Service charges and fees on deposit accounts	$ 2,676	$ 3,503	$ (827)	(24)%
Increase in cash surrender value of life insurance	1,569	1,512	57	4 %
Servicing income	288	297	(9)	(3)%
Gain on sales of SBA loans	348	482	(134)	(28)%
Termination fees	159	129	30	23 %
Gain on proceeds from company-owned life insurance	219	100	119	119 %
Other	1,304	1,033	271	26 %
Total	$ 6,563	$ 7,056	$ (493)	(7)%

Total noninterest income was relatively flat at $2.2 million for both the third quarter of 2024 and the third quarter of 2023. For the nine months ended September 30, 2024, total noninterest income decreased (7%) to $6.6 million, compared to $7.1 million for the nine months ended September 30, 2023, primarily due to lower service charges and fees on deposit accounts, partially offset by a higher gain on proceeds from company-owned life insurance for the first nine months 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 third quarter of 2024, SBA loan sales resulted in a $94,000 gain, compared to a $207,000 gain on sales of SBA loans for the third quarter of 2023. For the nine months ended September 30, 2024, SBA loan sales resulted in a $348,000 gain, compared to a $482,000 gain for the nine months ended September 30, 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 September 30,		Increase (Decrease) 2024 versus 2023	
	2024	2023	Amount	Percent
	(Dollars in thousands)			
Salaries and employee benefits	$ 15,673	$ 14,147	$ 1,526	11 %
Occupancy and equipment	2,599	2,301	298	13 %
Insurance expense	1,715	1,595	120	8 %
Professional fees	1,306	717	589	82 %
Client services	809	682	127	19 %
Data processing	800	906	(106)	(12)%
Software subscriptions	743	682	61	9 %
Other	3,910	4,141	(231)	(6)%
Total noninterest expense	$ 27,555	$ 25,171	$ 2,384	9 %

	Nine Months Ended September 30,		Increase (Decrease) 2024 versus 2023	
	2024	2023	Amount	Percent
	(Dollars in thousands)			
Salaries and employee benefits	$ 46,976	$ 42,943	$ 4,033	9 %
Occupancy and equipment	7,731	7,123	608	9 %
Insurance expense	4,988	4,627	361	8 %
Professional fees	3,705	3,265	440	13 %
Client services	2,497	1,633	864	53 %
Data processing	2,635	2,593	42	2 %
Software subscriptions	2,034	1,903	131	7 %
Other	12,713	11,476	1,237	11 %
Total noninterest expense	$ 83,279	$ 75,563	$ 7,716	10 %

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

	Three Months Ended September 30,			
	2024	Percent of Total	2023	Percent of Total
	(Dollars in thousands)			
Salaries and employee benefits	$ 15,673	57 %	$ 14,147	56 %
Occupancy and equipment	2,599	9 %	2,301	9 %
Insurance expense	1,715	6 %	1,595	6 %
Professional fees	1,306	5 %	717	3 %
Client services	809	3 %	682	3 %
Data processing	800	3 %	906	4 %
Software subscriptions	743	3 %	682	3 %
Other	3,910	14 %	4,141	16 %
Total noninterest expense	$ 27,555	100 %	$ 25,171	100 %

	Nine Months Ended September 30,			
	2024	Percent of Total	2023	Percent of Total
	(Dollars in thousands)			
Salaries and employee benefits	$ 46,976	56 %	$ 42,943	57 %
Occupancy and equipment	7,731	9 %	7,123	9 %
Insurance expense	4,988	6 %	4,627	6 %
Professional fees	3,705	5 %	3,265	4 %
Client services	2,497	3 %	1,633	2 %
Data processing	2,635	3 %	2,593	4 %
Software subscriptions	2,034	3 %	1,903	3 %
Other	12,713	15 %	11,476	15 %
Total noninterest expense	$ 83,279	100 %	$ 75,563	100 %

Total noninterest expense for the third quarter of 2024 increased to $27.6 million, compared to $25.2 million for the third quarter of 2023, primarily due to higher salaries and employee benefits, rent expense included in occupancy and equipment, and professional fees. Total noninterest expense for the nine months ended September 30, 2024 increased to $83.3 million, compared to $75.6 million for the nine months ended September 30, 2023, primarily due to higher salaries and employee benefits, rent expense, and information technology related expenses, marketing related expenses, homeowner association vendor payments, regulatory assessments, and ICS/CDARS fee expense included in other noninterest expense.

Full time equivalent employees were 353 at September 30, 2024, compared to 348 at September 30, 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:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2024	2023	2024	2023
Effective income tax rate	27.3 %	29.0 %	28.7 %	29.0 %

The Company's Federal and state income tax expense for the third quarter of 2024 was $3.9 million, compared to $6.5 million for the third quarter of 2023. The Company's Federal and state income tax expense for the first nine months of 2024 was $12.0 million, compared to $20.8 million for the first nine months 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.

FINANCIAL CONDITION

At September 30, 2024, total assets increased 3% to $5.6 billion, compared to $5.4 billion at September 30, 2023, and increased 7% from $5.2 billion at December 31, 2023, primarily related to growth in client deposits.

Securities available-for-sale, at fair value, were $237.6 million at September 30, 2024, a decrease of (48%) from $457.2 million at September 30, 2023, and decreased (46%) from $442.6 million at December 31, 2023. Securities held-to-maturity, at amortized cost, were $604.2 million at September 30, 2024, a decrease of (9%) from $664.7 million at September 30, 2023, and a decrease of (7%) from $650.6 million at December 31, 2023.

Loans, excluding loans held-for-sale, increased $124.8 million, or 4%, to $3.4 billion at September 30, 2024, compared to $3.3 billion at September 30, 2023, and increased $59.9 million, or 2%, from December 31, 2023. Loans, excluding residential mortgages, increased $148.3 million, or 5%, to $2.9 billion at September 30, 2024, compared to $2.8 billion at September 30, 2023, and increased $77.3 million, or 3%, from December 31, 2023.

Total deposits increased $154.1 million, or 3%, to $4.7 billion at September 30, 2024, compared to $4.6 billion at September 30, 2023, and increased $351.1 million, or 8%, from $4.4 billion at December 31, 2023.

Securities Portfolio

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

	September 30,		December 31,
	2024	2023	2023
	(Dollars in thousands)		
Securities available-for-sale (at fair value):			
U.S. Treasury	$ 184,162	$ 396,996	$ 382,369
Agency mortgage-backed securities	53,450	60,198	60,267
Total	$ 237,612	$ 457,194	$ 442,636
Securities held-to-maturity (at amortized cost):			
Agency mortgage-backed securities	$ 573,621	$ 632,241	$ 618,374
Municipals — exempt from Federal tax (1)	30,584	32,453	32,203
Total (1)	$ 604,205	$ 664,694	$ 650,577

(1) Gross of the allowance for credit losses of ($12,000) at September 30, 2024 and December 31, 2023, and ($13,000) at September 30, 2023.

The reduction in the securities available-for-sale portfolio was due to maturities and not due to any securities sold since December 31, 2023.

The following table summarizes the weighted average life and weighted average yields of securities at September 30, 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	$ 184,162	2.95 %	$ —	— %	$ —	— %	$ —	— %	$ 184,162	2.95 %
Agency mortgage-backed securities	108	2.77 %	43,880	2.51 %	9,462	2.64 %	—	— %	53,450	2.53 %
Total	$ 184,270	2.95 %	$ 43,880	2.51 %	$ 9,462	2.64 %	$ —	— %	$ 237,612	2.85 %
Securities held-to-maturity (at amortized cost):										
Agency mortgage-backed securities	$ 2,107	1.37 %	$ 97,986	1.97 %	$ 390,636	1.83 %	$ 82,892	2.64 %	$ 573,621	1.97 %
Municipals — exempt from Federal tax (1) (2)	6,216	4.12 %	6,050	3.26 %	18,318	3.52 %	—	— %	30,584	3.59 %
Total (2)	$ 8,323	3.42 %	$ 104,036	2.05 %	$ 408,954	1.90 %	$ 82,892	2.64 %	$ 604,205	2.05 %

(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 September 30, 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 clients; (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 at the dates indicated:

	September 30, 2024	September 30, 2023	December 31, 2023
	(Dollars in thousands)		
Securities available-for-sale pre-tax unrealized (loss):			
U.S. Treasury	$ (1,440)	$ (9,606)	$ (5,621)
Agency mortgage-backed securities	(2,923)	(7,185)	(4,313)
Total	$ (4,363)	$ (16,791)	$ (9,934)
Securities held-to-maturity pre-tax unrecognized (loss):			
Agency mortgage-backed securities	$ (71,996)	$ (119,932)	$ (85,729)
Municipals — exempt from Federal tax	(676)	(2,753)	(721)
Total	$ (72,672)	$ (122,685)	$ (86,450)
Allowance for credit losses on municipal securities	$ (12)	$ (13)	$ (12)

The net pre-tax unrealized loss on the securities available-for-sale was ($4.4) million, or ($3.2) million net of taxes, which equaled less than 1% of total shareholders' equity at September 30, 2024. The pre-tax unrecognized loss on securities held-to-maturity was ($72.7) million, or ($51.2) million net of taxes, which equaled 7.5% of total shareholders' equity at September 30, 2024. The unrealized and unrecognized losses in both the available-for-sale and held-to-maturity portfolios were due to higher interest rates at September 30, 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 61% of total assets at both September 30, 2024 and September 30, 2023, and 65% at December 31, 2023. The loan to deposit ratio was 72.11% at September 30, 2024, compared to 71.81% at September 30, 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:

	September 30, 2024		September 30, 2023		December 31, 2023	
	Balance	% to Total	Balance	% to Total	Balance	% to Total
	(Dollars in thousands)					
Commercial	$ 481,266	14 %	$ 430,664	13 %	$ 463,778	14 %
Real estate:						
CRE - owner occupied	602,062	18 %	589,751	18 %	583,253	17 %
CRE - non-owner occupied	1,310,578	38 %	1,208,324	37 %	1,256,590	37 %
Land and construction	125,761	4 %	158,138	5 %	140,513	4 %
Home equity	124,090	4 %	124,477	4 %	119,125	4 %
Multifamily	273,103	8 %	253,129	7 %	269,734	8 %
Residential mortgages	479,524	14 %	503,006	15 %	496,961	15 %
Consumer and other	14,179	< 1 %	18,526	1 %	20,919	1 %
Total Loans	3,410,563	100 %	3,286,015	100 %	3,350,873	100 %
Deferred loan fees, net	(327)	—	(554)	—	(495)	—
Loans, net of deferred fees	3,410,236	100 %	3,285,461	100 %	3,350,378	100 %
Allowance for credit losses on loans	(47,819)		(47,702)		(47,958)	
Loans, net	$ 3,362,417		$ 3,237,759		$ 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 both September 30, 2024 and September 30, 2023, compared to 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 nine months ended September 30, 2024 and 2023, loans were sold resulting in a gain on sales of SBA loans of $348,000 and $482,000, 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 nine months of 2024, compared to 39 days for the first nine 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:

	September 30, 2024	September 30, 2023
	(Dollars in thousands)	
Total factored receivables at period-end	$ 57,199	$ 52,082
Average factored receivables:		
For the three months ended	$ 55,391	$ 51,664
For the nine months ended	54,563	65,938
Total full time equivalent employees at period-end	30	28

The commercial loan portfolio increased $50.6 million, or 12%, to $481.3 million at September 30, 2024, from $430.7 million at September 30, 2023, and increased $17.5 million, or 4%, from $463.8 million at December 31, 2023. Commercial and industrial line usage was 31% at September 30, 2024, compared to 27% at September 30, 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 increased $12.3 million, or 2%, to $602.1 million at September 30, 2024, from $589.8 million at September 30, 2023, and increased $18.8 million, or 3%, from $583.3 million at December 31, 2023. CRE non-owner occupied loans increased $102.3 million, or 8%, to $1.3 billion at September 30, 2024, compared to $1.2 billion at September 30, 2023, and increased $54.0 million, or 4%, from $1.3 billion at December 31, 2023. At September 30, 2024, 31% of the CRE loan portfolio secured by owner-occupied real estate, compared to 33% at September 30, 2023, and 32% at December 31, 2023.

During the third quarter of 2024, there were 41 new owner occupied and non-owner occupied CRE loans originated totaling $67 million with a weighted average loan-to-value ("LTV") of 49%; the weighted average debt-service coverage ratio ("DSCR") for the non-owner occupied portfolio was 1.92 times. The average loan size for all CRE loans at September 30, 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 $419 million, including 32 loans totaling approximately $73 million, in San Jose, 19 loans totaling approximately $26 million in San Francisco, and eight loans totaling approximately $16 million, in Oakland, at September 30, 2024. Non-owner occupied CRE with office exposure totaled $329 million at September 30, 2024.

At September 30, 2024, the weighted average LTV and DSCR for the entire non-owner occupied office portfolio were 41.8% and 1.82 times, respectively.

Total medical/dental office exposure in the non-owner occupied CRE portfolio consisted of 15 loans totaling $12 million, with a weighted average LTV and DSCR ratio of 37.4% and 2.41 times, respectively, at September 30, 2024.

The following table presents the weighted average LTV and DSCR by collateral type for CRE loans at September 30, 2024:

	CRE - Non-owner Occupied			CRE - Owner Occupied		Total CRE	
Collateral Type	**Outstanding**	**LTV**	**DSCR**	**Outstanding**	**LTV**	**Outstanding**	**LTV**
Industrial	26 %	38.0 %	1.89	16 %	46.3 %	23 %	39.6 %
Retail	19 %	39.1 %	2.46	34 %	43.7 %	23 %	40.9 %
Mixed-Use, Special Purpose and Other	18 %	41.6 %	1.91	34 %	40.7 %	22 %	41.2 %
Office	20 %	41.8 %	1.82	16 %	44.3 %	19 %	42.5 %
Multifamily	17 %	42.6 %	1.95	0 %	0.0 %	13 %	42.6 %
Hotel/Motel	< 1 %	16.4 %	1.32	0 %	0.0 %	< 1 %	16.4 %
Total	100 %	40.3 %	1.99	100 %	43.2 %	100 %	41.1 %

The following table presents the weighted average LTV and DSCR by county for CRE loans at September 30, 2024:

	CRE - Non-owner Occupied			CRE - Owner Occupied		Total CRE	
County	**Outstanding**	**LTV**	**DSCR**	**Outstanding**	**LTV**	**Outstanding**	**LTV**
Alameda	25 %	44.3 %	1.93	18 %	45.6 %	23 %	44.6 %
Contra Costa	7 %	41.8 %	1.79	8 %	47.8 %	7 %	43.5 %
Marin	7 %	46.3 %	2.02	1 %	52.4 %	5 %	46.8 %
Monterey	2 %	43.8 %	1.85	2 %	41.1 %	2 %	43.0 %
Napa	< 1 %	30.0 %	1.73	1 %	52.0 %	1 %	36.3 %
Out of Area	8 %	42.3 %	2.06	9 %	49.0 %	9 %	44.3 %
San Benito	1 %	35.1 %	2.00	3 %	39.7 %	2 %	37.5 %
San Francisco	9 %	37.5 %	1.48	4 %	39.8 %	8 %	37.8 %
San Mateo	11 %	37.5 %	2.20	15 %	40.0 %	12 %	38.3 %
Santa Clara	24 %	37.4 %	2.25	34 %	41.1 %	26 %	38.8 %
Santa Cruz	2 %	33.1 %	1.74	1 %	49.2 %	2 %	36.2 %
Solano	1 %	32.1 %	1.95	2 %	37.8 %	1 %	33.8 %
Sonoma	3 %	39.7 %	2.22	2 %	43.1 %	2 %	40.5 %
Total	100 %	40.3 %	1.99	100 %	43.2 %	100 %	41.1 %

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 ($32.3) million, or (20%), to $125.8 million at September 30, 2024, compared to $158.1 million at September 30, 2023, and decreased ($14.7) million, or (10%), from $140.5 million at December 31, 2023.

The Company makes home equity lines of credit available to its existing clients. Home equity lines of credit are underwritten initially with a maximum 75% loan to value ratio. Home equity lines of credit remained relatively flat $124.1 million at September 30, 2024, compared to $124.5 million at September 30, 2023, and increased $5.0 million, or 4%, from $119.1 million at December 31, 2023.

Multifamily loans increased $20.0 million, or 8%, to $273.1 million at September 30, 2024, compared to $253.1 million at September 30, 2023, and increased $3.4 million, or 1%, 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 ($23.5) million, or (5%), to $479.5 million at September 30, 2024, compared to $503.0 million at September 30, 2023, and decreased ($17.5) million, or (4%) 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 ($4.3) million, or (23%), to $14.2 million at September 30, 2024, compared to $18.5 million at September 30, 2023, and decreased ($6.7) million, or (32%) 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 $112.9 million and $188.1 million at September 30, 2024, respectively.

Loan Maturities

The following table presents the maturity distribution of the Company's loans (excluding loans held-for-sale) as of September 30, 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 September 30, 2024, approximately 25% 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	$ 291,053	$ 147,487	$ 42,726	$ 481,266
Real estate:				
CRE - owner occupied	30,284	195,681	376,097	602,062
CRE - non-owner occupied	35,700	474,559	800,319	1,310,578
Land and construction	116,882	8,752	127	125,761
Home equity	5,562	26,179	92,349	124,090
Multifamily	20,108	124,758	128,237	273,103
Residential mortgages	6,040	15,404	458,080	479,524
Consumer and other	11,701	2,311	167	14,179
Loans	$ 517,330	$ 995,131	$ 1,898,102	$ 3,410,563
Loans with variable interest rates	$ 375,424	227,201	247,622	$ 850,247
Loans with fixed interest rates	141,906	767,930	1,650,480	2,560,316
Loans	$ 517,330	$ 995,131	$ 1,898,102	$ 3,410,563

Loan Servicing

As of September 30, 2024 and 2023, SBA loans that the Company serviced for others totaled $48.9 million and $60.1 million, respectively. Activity for loan servicing rights was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2024	2023	2024	2023
	(Dollars in thousands)			
Beginning of period balance	$ 363	$ 506	$ 415	$ 549
Additions	20	63	81	126
Amortization	(24)	(95)	(137)	(201)
End of period balance	$ 359	$ 474	$ 359	$ 474

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 September 30, 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 September 30,		Nine Months Ended September 30,	
	2024	2023	2024	2023
	(Dollars in thousands)			
Beginning of period balance	$ 101	$ 139	$ 117	$ 152
Unrealized holding loss	(6)	(14)	(22)	(27)
End of period balance	$ 95	$ 125	$ 95	$ 125

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 clients' 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 clients 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:

	September 30, 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	$ 4,390	$ 1,755	$ 1,082	$ 7,227	$ 474,039	$ 481,266
Real estate:						
CRE - Owner Occupied	—	—	—	—	602,062	602,062
CRE - Non-Owner Occupied	4,513	—	—	4,513	1,306,065	1,310,578
Land and construction	—	—	5,862	5,862	119,899	125,761
Home equity	659	—	—	659	123,431	124,090
Multifamily	—	—	—	—	273,103	273,103
Residential mortgages	—	—	—	—	479,524	479,524
Consumer and other	—	—	—	—	14,179	14,179
Total	$ 9,562	$ 1,755	$ 6,944	$ 18,261	$ 3,392,302	$ 3,410,563

	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 at the dates indicated:

	September 30, 2024	December 31, 2023
	(Dollars in thousands)	
Past due nonaccrual loans	$ 6,484	$ 6,100
Current nonaccrual loans	214	718
Total nonaccrual loans	$ 6,698	$ 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. 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 September 30, 2024, September 30, 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 September 30, 2024, September 30, 2023, or December 31, 2023.

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

	September 30, 2024	September 30, 2023	December 31, 2023
	(Dollars in thousands)		
Nonaccrual loans — held-for-investment	$ 6,698	$ 3,518	$ 6,818
Loans 90 days past due and still accruing	460	1,966	889
Total nonperforming loans	7,158	5,484	7,707
Foreclosed assets	—	—	—
Total nonperforming assets	$ 7,158	$ 5,484	$ 7,707
Nonperforming assets as a percentage of loans plus foreclosed assets	0.21 %	0.17 %	0.23 %
Nonperforming assets as a percentage of total assets	0.13 %	0.10 %	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 dates indicated:

	September 30, 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	$ 620	$ 132	$ 460	$ 1,212
Real estate:				
CRE - Owner Occupied	—	—	—	—
CRE - Non-Owner Occupied	—	—	—	—
Land and construction	5,862	—	—	5,862
Home equity	84	—	—	84
Total	$ 6,566	$ 132	$ 460	$ 7,158

	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 $132,000 and $290,000 at September 30, 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 $32.6 million, or 0.59% of total assets, at September 30, 2024, compared to $31.1 million, or 0.57% of total assets, at September 30, 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 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. Descriptions of the Company's loan portfolio segments are included in Note 1 "*Summary of Significant Accounting Policies*" of the 2023 Form 10-K.

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.

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 September 30, 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	$ 5,010	$ 5,344	$ 26,847	$ 1,523	$ 814	$ 4,269	$ 3,960	$ 187	$ 47,954
Charge-offs	(174)	—	—	—	—	—	—	(300)	(474)
Recoveries	154	14	—	—	18	—	—	—	186
Net (charge-offs) recoveries	(20)	14	—	—	18	—	—	(300)	(288)
Provision for (recapture of) credit losses on loans	(273)	62	603	(195)	(72)	86	(291)	233	153
End of period balance	$ 4,717	$ 5,420	$ 27,450	$ 1,328	$ 760	$ 4,355	$ 3,669	$ 120	$ 47,819
Percent of ACLL to Total ACLL at end of period	10%	11%	57%	3%	2%	9%	8%	< 1%	100%

	Three Months Ended September 30, 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	$ 6,550	$ 5,463	$ 23,523	$ 2,870	$ 730	$ 4,383	$ 4,129	$ 155	$ 47,803
Charge-offs	(447)	—	—	—	—	—	—	—	(447)
Recoveries	59	2	—	—	117	—	—	—	178
Net (charge-offs) recoveries	(388)	2	—	—	117	—	—	—	(269)
Provision for (recapture of) credit losses on loans	(557)	(120)	1,396	(126)	(140)	331	(635)	19	168
End of period balance	$ 5,605	$ 5,345	$ 24,919	$ 2,744	$ 707	$ 4,714	$ 3,494	$ 174	$ 47,702
Percent of ACLL to Total ACLL at end of period	12%	11%	52%	6%	2%	10%	7%	< 1%	100%

	Nine Months Ended September 30, 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	(1,042)	—	—	—	0	—	—	(300)	(1,342)
Recoveries	300	24	—	—	71	—	—	—	395
Net (charge-offs) recoveries	(742)	24	—	—	71	—	—	(300)	(947)
Provision for (recapture of) credit losses on loans	(394)	275	2,127	(1,024)	45	(698)	244	233	808
End of period balance	$ 4,717	$ 5,420	$ 27,450	$ 1,328	$ 760	$ 4,355	$ 3,669	$ 120	$ 47,819
Percent of ACLL to Total ACLL at end of period	10%	11%	57%	3%	2%	9%	8%	< 1%	100%

	Nine Months Ended September 30, 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	(605)	—	—	—	(246)	—	—	—	(851)
Recoveries	247	10	—	—	324	—	—	—	581
Net (charge-offs) recoveries	(358)	10	—	—	78	—	—	—	(270)
Provision for (recapture of) credit losses on loans	(654)	(416)	2,784	(197)	(37)	1,348	(2,413)	45	460
End of period balance	$ 5,605	$ 5,345	$ 24,919	$ 2,744	$ 707	$ 4,714	$ 3,494	$ 174	$ 47,702
Percent of ACLL to Total ACLL at end of period	12%	11%	52%	6%	2%	10%	7%	< 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.

	September 30,				December 31, 2023	
	2024		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	$ 4,717	14 %	$ 5,605	13 %	$ 5,853	14 %
Real estate:						
CRE - owner occupied	5,420	18 %	5,345	18 %	5,121	17 %
CRE - non-owner occupied	27,450	38 %	24,919	37 %	25,323	37 %
Land and construction	1,328	4 %	2,744	5 %	2,352	4 %
Home equity	760	4 %	707	4 %	644	4 %
Multifamily	4,355	8 %	4,714	7 %	5,053	8 %
Residential mortgages	3,669	14 %	3,494	15 %	3,425	15 %
Consumer and other	120	< 1 %	174	1 %	187	1 %
Total	$ 47,819	100 %	$ 47,702	100 %	$ 47,958	100 %

The ACLL totaled $47.8 million, or 1.40% of total loans at September 30, 2024, compared to $47.7 million, or 1.45% of total loans at September 30, 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 ($139,000) for the nine months ended September 30, 2024, compared to December 31, 2023, was primarily attributed to an increase of $11,000 in the reserve for pooled loans, and a decrease of ($150,000) in specific reserves for individually evaluated loans.

The ACLL was 668.05% of nonperforming loans at September 30, 2024, compared to 869.84% of nonperforming loans at September 30, 2023, and 622.27% of nonperforming loans at December 31, 2023. The Company had net charge-offs of $288,000, or 0.03% of average loans, for the third quarter of 2024, compared to net charge-offs of $269,000 or 0.03% of average loans, for the third 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, second, and third quarters 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
Portfolio changes during the second quarter of 2024	616
Qualitative and quantitative changes during the second quarter of 2024 including changes in economic forecasts	(550)
ACLL at June 30, 2024	47,954
Portfolio changes during the third quarter of 2024	599
Qualitative and quantitative changes during the third quarter of 2024 including changes in economic forecasts	(734)
ACLL at September 30, 2024	$ 47,819

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 $31.9 million on its consolidated statement of financial condition at September 30, 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 clients with balances of that magnitude are typically more rate-sensitive than clients with smaller balances.

The following table summarizes the distribution of deposits and the percentage of distribution in each category of deposits at the dates indicated:

	September 30, 2024		September 30, 2023		December 31, 2023	
	Balance	% to Total	Balance	% to Total	Balance	% to Total
	(Dollars in thousands)					
Demand, noninterest-bearing	$ 1,272,139	27 %	$ 1,243,501	27 %	$ 1,292,486	30 %
Demand, interest-bearing	913,910	19 %	1,004,185	22 %	914,066	21 %
Savings and money market	1,309,676	28 %	1,110,640	24 %	1,087,518	25 %
Time deposits — under $250	39,060	1 %	43,906	1 %	38,055	1 %
Time deposits — $250 and over	196,945	4 %	252,001	6 %	192,228	4 %
ICS/CDARS — interest-bearing demand, money market and time deposits	997,803	21 %	921,224	20 %	854,105	19 %
Total deposits	$ 4,729,533	100 %	$ 4,575,457	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 September 30, 2024, September 30, 2023, and December 31, 2023.

Total deposits increased $154.1 million, or 3%, to $4.7 billion at September 30, 2024 from $4.6 billion at September 30, 2023. Total deposits increased $351.1 million, or 8%, from $4.4 billion at December 31, 2023. Migration of client deposits resulted in an increase in ICS/CDARS deposits to $997.8 million at September 30, 2024, compared to $921.2 million at September 30, 2023, and $854.1 million at December 31, 2023. Noninterest-bearing demand deposits increased $28.6 million, or 2%, to $1.27 billion at September 30, 2024, compared to $1.24 billion at September 30, 2023, and decreased ($20.3) million, or (2%), from $1.29 billion at December 31, 2023.

The Company had 25,373 deposits accounts at September 30, 2024, with an average balance of $ 186,000, compared to 24,769 deposit accounts at September 30, 2023, with an average balance of $185,000. At December 31, 2023, the Company 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 $2.2 billion, representing 47% of total deposits, with an average account size of $394,000 at September 30, 2024. At September 30, 2023, deposits from the Bank's top 100 client relationships, representing 22% of the total number of accounts, totaled $2.2 billion, representing 48% of total deposits, with an average account size of $408,000. At December 31, 2023, deposits from the Bank's top 100 client relationships, representing 22% of the total number of accounts, totaled $2.0 billion, representing 45% of total deposits, with an average account size of $368,000.

The Bank's uninsured deposits were approximately $2.2 billion, or 47% of the Company's total deposits, at September 30, 2024, compared to $2.1 billion, or 46% of the Company's total deposits, at September 30, 2023, and $2.0 billion, or 46% of the Company's total deposits at December 31, 2023.

At September 30, 2024, the $997.8 million ICS/CDARS deposits comprised $417.1 million of interest-bearing demand deposits, $293.3 million of money market accounts and $287.4 million of time deposits. At September 30, 2023, the $921.2 million ICS/CDARS deposits comprised $452.4 million of interest-bearing demand deposits, $305.8 million of money market accounts and $163.0 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 September 30, 2024:

	Balance	% of Total
	(Dollars in thousands)	
Three months or less	$ 58,050	40 %
Over three months through six months	39,330	27 %
Over six months through twelve months	22,541	16 %
Over twelve months	25,023	17 %
Total	$ 144,944	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 September 30,		Nine Months Ended September 30,	
	2024	2023	2024	2023
Return on average assets	0.78 %	1.16 %	0.76 %	1.29 %
Return on average tangible assets [1]	0.81 %	1.20 %	0.79 %	1.33 %
Return on average equity	6.14 %	9.54 %	5.91 %	10.54 %
Return on average tangible common equity [1]	8.27 %	13.06 %	7.98 %	14.52 %
Average equity to average assets ratio	12.71 %	12.17 %	12.88 %	12.20 %

(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 72.11% at September 30, 2024, compared to 71.81% at September 30, 2023, and 76.52% at December 31, 2023.

The Company's total liquidity and borrowing capacity was $3.2 billion, all of which remained available at September 30, 2024. The available liquidity and borrowing capacity was 69% of the Company's total deposits and approximately 147% of the Bank's estimated uninsured deposits at September 30, 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 at the dates indicated:

	September 30, 2024			
	Collateral Value	Total Available	Outstanding	Remaining Available
	(Dollars in thousands)			
FHLB collateralized borrowing capacity	$ 1,204,712	$ 765,134	$ —	$ 765,134
FRB discount window collateralized line of credit	1,755,474	1,397,326	—	1,397,326
Federal funds purchase arrangements	N/A	90,000	—	90,000
Holding company line of credit	N/A	25,000	—	25,000
	$ 2,960,186	$ 2,277,460	$ —	$ 2,277,460

	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 September 30, 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 July 25, 2024, the Company announced that its Board of Directors adopted a share repurchase program (the "Repurchase Program") under which the Company is authorized to repurchase up to $15.0 million of the Company's shares of its issued and outstanding common stock. Unless otherwise suspended or terminated, the Repurchase Program expires on July 31, 2025. The Company did not repurchase any of its common stock during the third quarter of 2024.

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 $385,000, totaled $39.6 million at September 30, 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 at the dates indicated:

	September 30, 2024	September 30, 2023	December 31, 2023
		(Dollars in thousands)	
Capital components:			
Common Equity Tier 1 capital	$ 520,133	$ 504,872	$ 511,799
Additional Tier 1 capital	—	—	—
Tier 1 Capital	520,133	504,872	511,799
Tier 2 Capital	85,263	82,302	82,572
Total Capital	$ 605,396	$ 587,174	$ 594,371
Risk-weighted assets	$ 3,875,418	$ 3,762,256	$ 3,838,667
Average assets for capital purposes	$ 5,181,966	$ 5,235,816	$ 5,100,600
Capital ratios:			
Total Capital	15.6 %	15.6 %	15.5 %
Tier 1 Capital	13.4 %	13.4 %	13.3 %
Common equity Tier 1 Capital	13.4 %	13.4 %	13.3 %
Tier 1 Leverage(1)	10.0 %	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 at the dates indicated:

	September 30, 2024	September 30, 2023	December 31, 2023
		(Dollars in thousands)	
Capital components:			
Common Equity Tier 1 capital	$ 539,386	$ 522,611	$ 529,836
Additional Tier 1 capital	—	—	—
Tier 1 Capital	539,386	522,611	529,836
Tier 2 Capital	45,648	42,839	43,071
Total Capital	$ 585,034	$ 565,450	$ 572,907
Risk-weighted assets	$ 3,872,418	$ 3,761,812	$ 3,835,419
Average assets for capital purposes	$ 5,178,977	$ 5,235,122	$ 5,097,382
Capital ratios:			
Total Capital	15.1 %	15.0 %	14.9 %
Tier 1 Capital	13.9 %	13.9 %	13.8 %
Common Equity Tier 1 Capital	13.9 %	13.9 %	13.8 %
Tier 1 Leverage(1)	10.4 %	10.0 %	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 September 30, 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 September 30, 2024, September 30, 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 September 30, 2024, that management believes have changed the categorization of the Company or HBC as well-capitalized.

At September 30, 2024, the Company had total shareholders’ equity of $685.3 million, compared to $661.9 million at September 30, 2023, and $672.9 million at December 31, 2023. At September 30, 2024, total shareholders’ equity included $509.1 million in common stock, $185.1 million in retained earnings, and ($8.9) million of accumulated other comprehensive income (loss). The book value per share was $11.18 at September 30, 2024, compared to $10.83 at September 30, 2023, and $11.00 at December 31, 2023. The tangible book value per share was $8.33 at September 30, 2024, compared to $7.94 at September 30, 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, at the dates indicated:

Accumulated Other Comprehensive Loss	September 30, 2024	September 30, 2023	December 31, 2023
	(Dollars in thousands)		
Unrealized loss on securities available-for-sale	$ (3,161)	$ (11,985)	$ (7,116)
Split dollar insurance contracts liability	(2,965)	(3,234)	(2,809)
Supplemental executive retirement plan liability	(2,838)	(2,343)	(2,892)
Unrealized gain on interest-only strip from SBA loans	72	93	87
Total accumulated other comprehensive loss	$ (8,892)	$ (17,469)	$ (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 client-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 (a non-GAAP financial measure) 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 September 30, 2024:

Change in Interest Rates (basis points)	Increase/(Decrease) in Estimated Net Interest Income[(1)] Amount	Percent
	(Dollars in thousands)	
+400	$ 24,681	13.6 %
+300	$ 18,438	10.2 %
+200	$ 12,241	6.8 %
+100	$ 6,082	3.4 %
0	—	—
−100	$ (8,242)	(4.5)%
−200	$ (18,720)	(10.3)%
−300	$ (31,428)	(17.3)%
−400	$ (47,015)	(25.9)%

Change in Interest Rates (basis points)	Increase/(Decrease) in Estimated Economic Value of Equity[(1)] Amount	Percent
	(Dollars in thousands)	
+400	$ 161,338	14.0 %
+300	$ 133,760	11.6 %
+200	$ 98,755	8.6 %
+100	$ 55,024	4.8 %
0	—	—
−100	$ (86,037)	(7.5)%
−200	$ (204,813)	(17.8)%
−300	$ (345,418)	(30.1)%
−400	$ (452,503)	(39.4)%

(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 affect 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 a 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:

	Three Months Ended September 30,	
	2024	2023
	(Dollars in thousands)	
Net interest income before provision for credit losses on loans (GAAP)	$ 39,915	$ 45,372
Tax-equivalent adjustment on securities - exempt from Federal tax	59	61
Net interest income, FTE (non-GAAP)	$ 39,974	$ 45,433
Average balance of total interest earning assets	$ 5,011,865	$ 5,051,710
Net interest margin (annualized net interest income divided by the average balance of total interest earnings assets) (GAAP)	3.17 %	3.56 %
Net interest margin, FTE (annualized net interest income, FTE, divided by the average balance of total interest earnings assets) (non-GAAP)	3.17 %	3.57 %

	Nine Months Ended September 30,	
	2024	2023
	(Dollars in thousands)	
Net interest income before provision for credit losses on loans (GAAP)	$ 119,463	$ 140,923
Tax-equivalent adjustment on securities - exempt from Federal tax	179	190
Net interest income, FTE (non-GAAP)	$ 119,642	$ 141,113
Average balance of total interest earning assets	$ 4,909,240	$ 4,965,613
Net interest margin (annualized net interest income divided by the average balance of total interest earnings assets) (GAAP)	3.25 %	3.79 %
Net interest margin, FTE (annualized net interest income, FTE, divided by the average balance of total interest earnings assets) (non-GAAP)	3.26 %	3.80 %

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:

	Three Months Ended September 30,	
	2024	2023
	(Dollars in thousands)	
Noninterest expense	$ 27,555	$ 25,171
Net interest income before provision for credit losses on loans	$ 39,915	$ 45,372
Noninterest income	2,240	2,216
Total revenue	$ 42,155	$ 47,588
Efficiency ratio (noninterest expense divided by total revenue) (non-GAAP)	65.37 %	52.89 %

	Nine Months Ended September 30,	
	2024	2023
	(Dollars in thousands)	
Noninterest expense	$ 83,279	$ 75,563
Net interest income before provision for credit losses on loans	$ 119,463	$ 140,923
Noninterest income	6,563	7,056
Total revenue	$ 126,026	$ 147,979
Efficiency ratio (noninterest expense divided by total revenue) (non-GAAP)	66.08 %	51.06 %

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:

	Three Months Ended September 30, 2024	Three Months Ended September 30, 2023
	(Dollars in thousands)	
Net income	$ 10,507	$ 15,795
Average tangible assets components:		
Average Assets (GAAP)	$ 5,352,067	$ 5,399,930
Less: Goodwill	(167,631)	(167,631)
Less: Other Intangible Assets	(7,322)	(9,607)
Total Average Tangible Assets (non-GAAP)	$ 5,177,114	$ 5,222,692
Annualized return on average tangible assets (non-GAAP)	0.81 %	1.20 %
Average tangible common equity components:		
Average Equity (GAAP)	$ 680,404	$ 656,973
Less: Goodwill	(167,631)	(167,631)
Less: Other Intangible Assets	(7,322)	(9,607)
Total Average Tangible Common Equity (non-GAAP)	$ 505,451	$ 479,735
Annualized return on average tangible common equity (non-GAAP)	8.27 %	13.06 %

	Nine Months Ended September 30, 2024	Nine Months Ended September 30, 2023
	(Dollars in thousands)	
Net income	$ 29,907	$ 51,115
Average tangible assets components:		
Average Assets (GAAP)	$ 5,248,338	$ 5,316,447
Less: Goodwill	(167,631)	(167,631)
Less: Other Intangible Assets	(7,864)	(10,206)
Total Average Tangible Assets (non-GAAP)	$ 5,072,843	$ 5,138,610
Annualized return on average tangible assets (non-GAAP)	0.79 %	1.33 %
Average tangible common equity components:		
Average Equity (GAAP)	$ 675,951	$ 648,341
Less: Goodwill	(167,631)	(167,631)
Less: Other Intangible Assets	(7,864)	(10,206)
Total Average Tangible Common Equity (non-GAAP)	$ 500,456	$ 470,504
Annualized return on average tangible common equity (non-GAAP)	7.98 %	14.52 %

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

	September 30, 2024	September 30, 2023	December 31, 2023
		(Dollars in thousands)	
Capital components:			
Total Equity (GAAP)	$ 685,352	$ 661,930	$ 672,901
Less: Preferred Stock	—	—	—
Total Common Equity	685,352	661,930	672,901
Less: Goodwill	(167,631)	(167,631)	(167,631)
Less: Other Intangible Assets	(6,966)	(9,229)	(8,627)
Total Tangible Common Equity (non-GAAP)	$ 510,755	$ 485,070	$ 496,643
Asset components:			
Total Assets (GAAP)	$ 5,551,596	$ 5,403,307	$ 5,194,095
Less: Goodwill	(167,631)	(167,631)	(167,631)
Less: Other Intangible Assets	(6,966)	(9,229)	(8,627)
Total Tangible Assets (non-GAAP)	$ 5,376,999	$ 5,226,447	$ 5,017,837
Tangible common equity / tangible assets (non-GAAP)	9.50 %	9.28 %	9.90 %

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

	September 30, 2024	September 30, 2023	December 31, 2023
		(Dollars in thousands)	
Capital components:			
Total Equity (GAAP)	$ 704,585	$ 679,644	$ 690,918
Less: Preferred Stock	—	—	—
Total Common Equity	704,585	679,644	690,918
Less: Goodwill	(167,631)	(167,631)	(167,631)
Less: Other Intangible Assets	(6,966)	(9,229)	(8,627)
Total Tangible Common Equity (non-GAAP)	$ 529,988	$ 502,784	$ 514,660
Asset components:			
Total Assets (GAAP)	$ 5,548,576	$ 5,402,838	$ 5,190,829
Less: Goodwill	(167,631)	(167,631)	(167,631)
Less: Other Intangible Assets	(6,966)	(9,229)	(8,627)
Total Tangible Assets (non-GAAP)	$ 5,373,979	$ 5,225,978	$ 5,014,571
Tangible common equity / tangible assets (non-GAAP)	9.86 %	9.62 %	10.26 %

The following table summarizes components of the tangible book value per share at the dates indicated:

	September 30, 2024	September 30, 2023	December 31, 2023
	(Dollars in thousands, except per share amounts)		
Capital components:			
Total Equity (GAAP)	$ 685,352	$ 661,930	$ 672,901
Less: Preferred Stock	—	—	—
Total Common Equity	685,352	661,930	672,901
Less: Goodwill	(167,631)	(167,631)	(167,631)
Less: Other Intangible Assets	(6,966)	(9,229)	(8,627)
Total Tangible Common Equity (non-GAAP)	$ 510,755	$ 485,070	$ 496,643
Common shares outstanding at period-end	61,297,344	61,099,155	61,146,835
Tangible book value per share (non-GAAP)	$ 8.33	$ 7.94	$ 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 September 30, 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 September 30, 2024, the period covered by this Report.

During the three and nine months ended September 30, 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. As of September 30, 2024, we were party to no litigation that we believe to be material to our business, financial condition, results of operations, or cash flows.

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.

General Risks Related to Our Business, Reputation and Operations

Interruptions, cyberattacks, fraudulent activity or other security breaches may 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 clients. We also rely heavily upon electronic infrastructure that we own or that we obtain via license or other contractual arrangements with third parties. This infrastructure is essential in the conduct of our business, including for allowing our clients to access and transfer funds, initiate and pay loans and leases, communicating with our client service teams, and a variety of other activities that form the foundation of modern financial services businesses. There have been a number of recent and well-publicized incidents involving various types of cybersecurity lapses, and many of these have had substantial impacts upon targeted businesses and on clients of even some of the world's most prominent cybersecurity firms. One of the most recent events resulted in a widespread failure of a large cybersecurity platform, some of the consequences of which are ongoing and may not be fully known or estimable. Similarly, extremely sophisticated criminal and nation-state organizations routinely target and exploit information technology networks, data systems, and other critical infrastructure. Some of the most common types of threats targeting financial institutions include:

- Ransomware Attacks. These threats ordinarily involve intrusions into networks or data storage systems by actors who render the platform inoperable or that obtain or obstruct access to sensitive data, whereupon the malefactor notifies the platform's owner and demands cash payment in exchange for a complex code that "unlocks" the malware. Another variant of this practice demands a ransom in exchange for a promise not to make sensitive data, such as client information, available to unauthorized sources.

- Cloud Services Attacks. Because financial institutions are highly reliant on data that is stored in "cloud" servers, and on services that use cloud-based software platforms, malefactors often seek to "hijack" these services, either by rendering them inaccessible or by misusing or damaging information or programs that depend on these systems.

- Artificial Intelligence-Based Attacks. As we experience an unprecedented growth in the development of artificial intelligence, various hostile actors and criminals are actively developing means by which this technology can be used to exploit computer networks. This technology can be used to manipulate a business' processes to produce erroneous or unreliable results, to perpetrate ransomware or cloud-based attacks, or to destroy or render unusable a company's systems or data.

- Phishing. A longstanding but still highly effective threat known as "phishing" involves tricking an unwitting employee, client or vendor into disclosing passwords, encryption keys, or other sensitive information that allows a threat actor to access networks or data systems, where the actor can engage in a ransomware attack, install a worm or virus, or engage in fraudulent activity.

We devote significant resources and management focus to ensure the integrity of our systems against cybercriminals and similar actors, as well as against threats from fires and 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. Likewise, we have made, and we continue to make, substantial investments in systems that are intended to protect against these vulnerabilities, including real-time threat detection and warning, security programs and protocols, backup and alternative-access systems, virus and malware protection programs, and a wide variety of other protective measures.

Notwithstanding these efforts, cybersecurity measures are, by their nature, largely reactive, and threats are constantly evolving. We expect that the development of AI-based technology will cause a rapid expansion in both the number and the sophistication of these threats. While we believe we maintain state-of-the-art defensive measures, we routinely experience attempts to exploit our networks and systems, and we must continue investing in increasingly sophisticated (and concomitantly expensive) technology to counteract these threats. Further, if our systems cannot timely detect and mitigate vulnerabilities, or cannot promptly respond to threats, we may experience damage to or interruptions in the availability of our computer networks, or we may experience a loss of data, unauthorized use or disclosure of client information, or a loss of client funds as a result of unauthorized access to client accounts.

Furthermore, enhancements and upgrades to our infrastructure or computer systems may be time-consuming, may entail significant costs, and may themselves create risks associated with implementing new systems and integrating them with existing ones. Due to the complexity and interconnectedness of our systems, the process of enhancing our infrastructure and operating systems, including their security measures and controls, also can create an inherent risk of system disruptions and security issues. Similarly, we may not be able to timely recover critical business processes or operations that have been disrupted, which may further increase any associated costs and consequences of such disruptions. Although we have enterprise incident response processes, business continuity plans and other safeguards in place to help provide operational resiliency, our business operations may be adversely affected by significant and widespread disruption to our physical infrastructure or computer systems that support our businesses and clients.

Additionally, as financial institutions and technology systems become more interconnected and more complex, any operational incident at a third party, such as a vendor or client, may increase our operational risks, including from information breaches or loss, breakdowns, disruptions or failures of their own systems or infrastructure, or any deficiencies in the performance of their responsibilities. These risks are increased to the extent we rely on a single-source vendor or provider.

We also must meet stringent and increasingly complex regulatory requirements regarding our use of third-party service providers, and any failure by our third-party service providers to meet their obligations to us or to comply with applicable laws, rules, regulations, or internal policies could result in the Company becoming subject to fines, penalties, or business restrictions, as well as to increased costs to remediate any actual or perceived deficiencies and potentially to legal and other costs associated with defending against such regulatory sanctions. Disruptions or failures in the physical infrastructure, controls or operating systems that support our businesses and clients, failures of the third parties on which we rely to adequately or appropriately provide their services or perform their responsibilities, or our failure to effectively manage or oversee our third-party relationships, could result in business disruptions, loss of revenue or clients, legal or regulatory proceedings, remediation and other costs, violations of applicable privacy and other laws, reputational damage, client harm, or other adverse consequences, any of which could materially adversely affect our results of operations or financial condition. Further, new and evolving SEC regulations, as well as federal and state banking and consumer privacy laws and regulations, could require us 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 or an adverse perception of our products and services.

The access by unauthorized persons to, or the improper disclosure by us or our third-party vendors of, confidential information regarding our clients 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 client relationship management, online banking, accounting or other systems. We cannot assure readers 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.

Accordingly, any failures or interruptions of our communications, information and technology systems could damage our reputation, result in a loss of client 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.

Our operations could be disrupted 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 that require us to 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 cyberattack or other security breach. We expect that our regulators would 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 client remediation, any of which could have a material adverse effect on our business, financial condition and results of 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, cybersecurity failures or disruptions, failure to deliver minimum standards of service or quality, compliance deficiencies, and questionable or fraudulent activities of our clients or third parties. Negative publicity regarding our business, employees, or clients, with or without merit, may result in the loss of clients, 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 client 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 generated significant market volatility among publicly traded bank holding companies. These market developments have negatively impacted client confidence in the safety and soundness in the financial services industry, which has persisted into 2024, and these perceptions may continue into the future. 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 client 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 and liquidity 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. 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.

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

We are vulnerable to reputational harm because we operate in an industry in which integrity and the confidence of our clients 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 clients and/or our business. The precautions we take to detect and prevent such misconduct may not always be effective and could result in regulatory sanctions and/or penalties, criminal or civil penalties and, serious harm to our reputation, financial condition, client relationships, employee relationships and ability to attract new clients. 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 clients 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 clients and counterparties, we may rely on information furnished to us by or on behalf of clients and counterparties, including financial statements and other financial information. Some of the information regarding clients 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 clients and the risk profiles of such clients some of these protocols are subsequently utilized by counterparties who may lend us capital to fund our operations. We may also rely on representations of clients and counterparties as to the accuracy and completeness of that information. In deciding whether to extend credit, we may rely upon our clients' representations that their financial statements conform to stated accounting principles and present fairly, in all material respects, the financial condition, results of operations and cash flows of the client. We also may rely on client representations and certifications, or other audit or accountants' reports, with respect to the business and financial condition of our clients. 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 clients, regulators, investors, and other stakeholders with respect to our environmental, social and governance practices may impose additional costs on us or may expose us to new or additional risks.

Companies are facing increasing scrutiny from clients, regulators, investors, and other stakeholders related to their environmental, social and governance ("ESG") practices and disclosure. Investor advocacy groups, investment funds and influential investors have recently been heavily 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 also 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 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 borrowers' repayment ability and collateral coverage as well as reduced demand for our products and services. 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 client 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, clients' 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 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 clients, 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 Bay View Funding, the Bank's factoring subsidiary, and our clients' 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 clients 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 client 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 client 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 client preferences, reductions in consumers' disposable income, regulatory actions that decrease client access to particular products, or the availability of competing products.

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 September 30, 2024, approximately $2.9 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 $602.1 million, or 18% 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 September 30, 2024, land and construction loans, (including land acquisition and development loans) totaled $125.8 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 September 30, 2024, commercial loans totaled $481.3 million or 14% of our loan portfolio (including SBA loans, asset-based lending, and factored receivables). 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. 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.

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 September 30, 2024, SBA loans totaled $29.9 million, which are included in the commercial loan portfolio. SBA loans held-for-sale totaled $1.6 million at September 30, 2024. In addition, the Company had $284,000 of SBA PPP loans at September 30, 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 clients 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 client 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 and nine months ended September 30, 2024 was $94,000 and $348,000, respectively. 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 $24.8 million of SBA loans for the nine months ended September 30, 2024. We sold $4.1 million of the guaranteed portion of our SBA loans for the nine months ended September 30, 2024. We generally retain the non-guaranteed portions of the SBA loans that we originate. Consequently, as of September 30, 2024, we held $31.4 million of SBA loans (including loans held-for-sale) on our balance sheet, $18.1 million of which consisted of the non-guaranteed portion of SBA loans, and $13.3 million of which consisted of the guaranteed portion of SBA loans. At September 30, 2024, $1.6 million, or 5.25%, 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 1.40%, at September 30, 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 $153,000 and $808,000 for the three months and nine months ended September 30, 2024, respectively. 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 September 30, 2024, our nonperforming loans (which consist of nonaccrual loans, loans past due 90 days or more and still accruing interest) totaled $7.2 million, or 0.21% of our loan portfolio, and our nonperforming assets (which include nonperforming loans plus other real estate owned) also totaled $7.2 million, or 0.13% 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 September 30, 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

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 September 30, 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.

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 client 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 clients 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.

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 clients 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, clients may withdraw their deposits or otherwise seek services from other banking institutions and prospective clients 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 clients 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.

Although the Federal Reserve System (commonly referred to as "the Fed") has recently made an incremental reduction in benchmark interest rates, the current interest rate environment remains significantly elevated from those of the recent past. These rates affect both our ability to reprice variable-rate loans and to originate new fixed-rate loans, and in times of significant uncertainty about interest rates, such as the present, customers and prospective investors often reduce their borrowing levels, which tends to have a deflating effect on our outstanding loan balances and thus on our interest income.

During the third quarter of 2024, the Federal Reserve Open Markets Committee cut benchmark interest rates for the first time since 2020. While we do not presently expect that the Fed will resume increases to benchmark interest rates, we are unable to predict changes in future interest rates. Further, the conditions that led the Fed to make these reductions remain uncertain and relatively volatile, and thus are highly unpredictable. This is particularly true of the risks of political instability associated with the 2024 presidential election and governmental and economic reactions to any such events. If rates resume increasing, or if they continue to remain at relatively elevated levels for prolonged periods, our borrowers may experience increasing difficulty in repaying their loans. Further, borrowers may defer additional borrowing decisions pending the resolution of both the political uncertainties and the potential for further market adjustments in response to those matters and to general economic conditions.

To the extent interest rates remain relatively elevated, 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. Concomitantly, even if interest rates stabilize or if reductions are less significant than customers expect, we may confront a loss of demand that adversely affects our interest earning assets. Either of 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.

Fluctuations in market interest rates may have a material effect on the value of the Company's securities portfolio.

As of September 30, 2024, the fair value of our securities portfolio was approximately $769.1 million, of which approximately $237.6 million were categorized as available for sale. Fixed-rate investment securities, such as bonds, treasuries and mortgage-backed securities, generally decline in value when interest rates rise above the rates applicable to such securities. Correspondingly, declining interest rates tend to increase the value of fixed-rate securities issued in times of relatively higher rates, but those declines also affect our net interest income because they force us to pay above-market rates on certificates of deposit and other longer-term obligations, and customers tend to exit those investments less frequently under those conditions because their earning capacity in other investments is relatively less attractive.

In response to inflationary pressures and other general economic conditions, the Federal Open Market Committee of the Board of Governors of the Fed rapidly and significantly increased interest rates between early 2022 and mid-2024, which resulted in declines in the carrying value of both our held-to-maturity and, particularly, our available-for-sale securities portfolios. Market interest rates have declined modestly in response to the Fed's recent interest rate reductions. However, the economy remains highly uncertain with respect to various factors, including inflation and employment statistics, and it is thus extremely difficult for management to predict when, to what degree, or in which direction the Fed may attempt to adjust rates further. Such 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. Correspondingly, additional rate reductions may affect our net interest income as we seek to price our deposit products in a way that remains competitive and attractive to customers, while also mitigating the risk that future declines may leave us with elevated borrowing costs.

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, or we may face periods of compressed net interest margins, either of 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 client 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 clients 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 clients about their deposits and may increase the costs of maintaining those deposits. Further, significant economic fluctuations, or clients' expectations about such events (whether or not those expectations materialize) may exacerbate depositors' sensitivity to the availability of cash to fund immediate withdrawals. If clients 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 client 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 fund share repurchases, 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 clients 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, as well as significant experience in our local markets, and their knowledge and relationships would be difficult to replace. Leadership changes will occur from time to time, and we cannot always anticipate or control the timing of these changes. Similarly, we cannot offer assurances that we would be able to recruit additional qualified personnel on a timely basis, either to fill vacancies created by departures or to grow our executive team to respond to and prepare for the expansion of our business. 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. Our ability to compete effectively for senior executives and other qualified leadership personnel may increase our compensation and administrative expenses 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 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 client 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 client relationships. Further, if there is a rebound of higher interest rates our deposit clients 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 clients 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 client 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 clients 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 clients and to reduce costs. Our future success depends, in part, upon our ability to address the needs of our clients by using technology to provide products and services that will satisfy client 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 clients. 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, punitive damages 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 clients, 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 clients 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 that 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 clients 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 clients' property and/or result in financial losses that could impair asset values and the creditworthiness of our clients. Such events could disrupt our operations or those of our clients, 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 clients.

The Company's business, as well as the operations and activities of our clients, could be negatively impacted by climate change, which 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 clients 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 Fed, 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 September 30, 2024, we had a net deferred tax asset of $26.4 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 Fed, 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 clients 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 Fed, 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 clients.

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 Fed 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 clients with nonaffiliated third parties; (ii) requires that we provide certain disclosures to clients about our information collection, sharing and security practices and afford clients 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 client 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 client 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 Fed. The Fed 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 Fed 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 September 30, 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 Fed. 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*	Employment Agreement by and among Heritage Bank of Commerce and Thomas A. Sa dated September 26, 2024 (incorporated by reference to Exhibit 10.01 to the Registrant's Current Report on Form 8-K filed on October 2, 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 September 30, 2024, formatted in Inline XBRL.

* Management contract or compensatory plan or arrangement.
**Furnished and not filed.

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: November 8, 2024	/s/ ROBERTSON CLAY JONES Robertson Clay Jones *Chief Executive Officer* (Duly Authorized Officer)
Date: November 8, 2024	/s/ LAWRENCE D. MCGOVERN Lawrence D. McGovern *Chief Financial Officer* (Principal 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 SEPTEMBER 30, 2024**

I, Robertson Clay Jones, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the Quarter Ended September 30, 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: November 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 SEPTEMBER 30, 2024

I, Lawrence D. McGovern, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the Quarter Ended September 30, 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: November 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 SEPTEMBER 30, 2024

In connection with the Quarterly Report of Heritage Commerce Corp (the “Company”) on Form 10-Q for the period ended September 30, 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: November 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 SEPTEMBER 30, 2024

In connection with the Quarterly Report of Heritage Commerce Corp (the “Company”) on Form 10-Q for the period ended September 30, 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: November 8, 2024

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