

SECURITIES AND EXCHANGE COMMISSION  
Washington D.C. 20549

FORM 10-Q

Quarterly Report  
Pursuant to Section 13 or 15(d) of  
the Securities Exchange Act of 1934

For the Quarterly Period Ended September 30, 2016

**FNB BANCORP**

(Exact name of registrant as specified in its charter)

California  
(State or other jurisdiction of incorporation)

000-49693  
(Commission File Number)

91-2115369  
(IRS Employer Identification No.)

975 El Camino Real, South San Francisco, California  
(Address of principal executive offices)

94080  
(Zip Code)

Registrant's telephone number, including area code: (650) 588-6800

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 and posted on its Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files).  Yes  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: Common Stock as of October 20, 2016: 4,616,901 shares.

**FNB BANCORP AND SUBSIDIARY  
QUARTERLY REPORT ON FORM 10-Q  
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PART I—FINANCIAL INFORMATION

Item 1. Financial Statements.

FNB BANCORP AND SUBSIDIARY  
CONSOLIDATED BALANCE SHEETS  
(UNAUDITED)

ASSETS

(Dollar amounts in thousands)	September 30, 2016	December 31, 2015
Cash and due from banks	\$ 17,342	\$ 12,314
Interest-bearing time deposits with financial institutions	204	205
Securities available-for-sale, at fair value	358,877	329,207
Other equity securities	7,206	6,748
Loans, net of allowance for loan losses of \$10,092 and \$9,970 on September 30, 2016 and December 31, 2015	741,407	722,747
Bank premises, equipment, and leasehold improvements, net	9,918	10,202
Bank owned life insurance	16,145	15,845
Accrued interest receivable	4,544	4,511
Other real estate owned, net	1,346	1,026
Goodwill	4,580	4,580
Prepaid expenses	670	997
Other assets	15,309	15,967
Total assets	<u>\$ 1,177,548</u>	<u>\$ 1,124,349</u>

LIABILITIES AND STOCKHOLDERS' EQUITY

<b>Deposits</b>		
Demand, noninterest bearing	\$ 285,767	\$ 263,822
Demand, interest bearing	110,147	102,304
Savings and money market	491,047	491,633
Time	116,496	125,430
Total deposits	<u>1,003,457</u>	<u>983,189</u>
Federal Home Loan Bank advances	37,000	17,000
Note payable	4,500	4,950
Accrued expenses and other liabilities	18,847	15,048
Total liabilities	<u>1,063,804</u>	<u>1,020,187</u>
<b>Stockholders' equity</b>		
Common stock, no par value, authorized 10,000,000 shares; issued and outstanding 4,616,076 shares at September 30, 2016 and 4,541,680 shares at December 31, 2015	76,065	74,805
Retained earnings	33,123	27,816
Accumulated other comprehensive income, net of tax	4,556	1,541
Total stockholders' equity	<u>113,744</u>	<u>104,162</u>
Total liabilities and stockholders' equity	<u>\$ 1,177,548</u>	<u>\$ 1,124,349</u>

See accompanying notes to consolidated financial statements.

**FNB BANCORP AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF EARNINGS**  
**(UNAUDITED)**

(Dollar amounts and average shares are in thousands, except earnings per share amounts)

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
<b>Interest income:</b>				
Interest and fees on loans	\$ 9,301	\$ 8,309	\$ 28,735	\$ 23,874
Interest on taxable securities	1,065	924	3,044	2,597
Interest on tax-exempt securities	750	651	2,187	1,754
Interest time deposits with other financial institutions	1	9	3	36
Total interest income	<u>11,117</u>	<u>9,893</u>	<u>33,969</u>	<u>28,261</u>
<b>Interest expense:</b>				
Interest on deposits	657	635	2,149	1,625
Interest on Federal Home Loan Bank advances	10	1	19	2
Interest on note payable	54	57	167	173
Total interest expense	<u>721</u>	<u>693</u>	<u>2,335</u>	<u>1,800</u>
Net interest income	10,396	9,200	31,634	26,461
Provision for loan losses	—	75	150	225
Net interest income after provision for loan losses	<u>10,396</u>	<u>9,125</u>	<u>31,484</u>	<u>26,236</u>
<b>Noninterest income:</b>				
Service charges	623	618	1,862	1,854
Net gain on sale of available-for-sale securities	140	29	381	250
Bank-owned life insurance earnings	95	90	300	261
Other income	249	287	763	1,002
Total noninterest income	<u>1,107</u>	<u>1,024</u>	<u>3,306</u>	<u>3,367</u>
<b>Noninterest expense:</b>				
Salaries and employee benefits	4,821	4,100	14,635	12,513
Occupancy expense	645	592	1,893	1,906
Equipment expense	445	718	1,317	1,533
Professional fees	298	334	979	1,075
FDIC assessment	150	150	450	450
Telephone, postage and supplies	300	237	901	782
Advertising	104	112	404	381
Data processing expense	147	659	479	940
Low income housing expense	71	70	213	212
Surety insurance	88	122	262	298
Directors expense	72	72	216	216
Other real estate owned expense (income), net	—	—	(10)	(6)
Other expense	372	313	1,210	911
Total noninterest expense	<u>7,513</u>	<u>7,479</u>	<u>22,949</u>	<u>21,211</u>
Earnings before provision for income taxes	3,990	2,670	11,841	8,392
Provision for income taxes	1,546	431	4,382	2,283
Net earnings	<u>2,444</u>	<u>2,239</u>	<u>7,459</u>	<u>6,109</u>
<b>Earnings per share data:</b>				
Basic	\$ 0.53	\$ 0.49	\$ 1.63	\$ 1.36
Diluted	\$ 0.52	\$ 0.48	\$ 1.59	\$ 1.32
<b>Weighted average shares outstanding:</b>				
Basic	4,612	4,524	4,582	4,508
Diluted	4,717	4,643	4,700	4,635

See accompanying notes to consolidated financial statements.

**FNB BANCORP AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS**  
**(UNAUDITED)**

(Dollar amounts in thousands)

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
Net earnings	\$ 2,444	\$ 2,239	\$ 7,459	\$ 6,109
Unrealized holding gain on available-for-sale securities, net of tax expense of \$399 and \$2,251 for three and nine months ended September 30, 2016, and net of tax expense of \$988 and \$953 for three and nine months ended September 30, 2015, respectively	574	1,422	3,240	1,372
Reclassification adjustment for gain on available-for-sale securities sold, net of tax benefit of \$57 and \$156 for three and nine months ended September 30, 2016, and \$12 and \$103 for three and nine months ended September 30, 2015, respectively	(83)	(17)	(225)	(147)
Other Comprehensive Earnings	491	1,405	3,015	1,225
Total comprehensive earnings	<u>\$ 2,935</u>	<u>\$ 3,644</u>	<u>\$ 10,474</u>	<u>\$ 7,334</u>

See accompanying notes to consolidated financial statements.

**FNB BANCORP AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**

(Dollar amounts in thousands)

	Nine months ended September 30	
	2016	2015
<b>Cash flow from operating activities:</b>		
Net earnings	\$ 7,459	\$ 6,109
<b>Adjustments to reconcile net earnings to net cash provided by operating activities:</b>		
Net gain on sale of securities available-for-sale	(381)	(250)
Depreciation, amortization and accretion	2,872	2,553
Stock-based compensation expense	227	183
Earnings on bank owned life insurance	(300)	(261)
Increase in net deferred loan fees	254	51
Provision for loan losses	150	225
Increase in accrued interest receivable	(33)	(288)
Decrease in prepaid expense	327	1,976
Decrease in other assets	658	2,888
Increase (decrease) in accrued expenses and other liabilities	967	(5,027)
Net cash provided by operating activities	<u>12,200</u>	<u>8,159</u>
<b>Cash flows from investing activities</b>		
Purchase of securities available-for-sale	(79,862)	(90,590)
Proceeds from matured/called/sold securities available-for-sale	53,606	40,514
Net (investment) in other equity securities	(458)	(300)
Acquisition, net of cash paid	—	(18,481)
Maturities of time deposits of other banks	1	9,374
Net investment in other real estate owned	(320)	(75)
Net increase in loans	(19,064)	(20,480)
Purchases of bank premises, equipment, leasehold improvements	(512)	(144)
Net cash used in investing activities	<u>(46,609)</u>	<u>(80,182)</u>

See accompanying notes to consolidated financial statements.

**FNB BANCORP AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**

(Dollar amounts in thousands)

	Nine months ended September 30	
	2016	2015
<b>Cash flows from financing activities</b>		
Net increase in demand and savings deposits	29,202	109,085
Net decrease in time deposits	(8,934)	(2,040)
Increase (decrease) in FHLB advances	20,000	(9,000)
Principal repayment on note payable	(450)	(450)
Dividends paid on common stock	(1,414)	(1,146)
Exercise of stock options	1,033	878
Net cash provided by financing activities	39,437	97,327
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	5,028	25,304
Cash and cash equivalents at beginning of period	12,314	14,978
Cash and cash equivalents at end of period	<u>\$ 17,342</u>	<u>\$ 40,282</u>
<b>Additional cash flow information:</b>		
Interest paid	\$ 2,284	\$ 1,745
Income taxes paid	\$ 4,215	\$ 1,938
Tax benefit on exercise of stock options	\$ —	\$ 154
<b>Non-cash investing and financing activities:</b>		
Accrued dividends	\$ 738	\$ 646
Change in unrealized gain in available for-sale securities, net of tax	\$ 3,015	\$ 1,224
<b>Acquisitions:</b>		
Fair value of assets acquired	\$ —	\$ 115,127
Fair value of liabilities assumed	\$ —	\$ 93,627

See accompanying notes to consolidated financial statements.

**FNB BANCORP AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**SEPTEMBER 30, 2016**

**(UNAUDITED)**

**NOTE A – BASIS OF PRESENTATION**

FNB Bancorp (the “Company”) is a bank holding company registered under the Bank Holding Company Act of 1956, as amended. The Company was incorporated under the laws of the State of California on February 28, 2001. The consolidated financial statements include the accounts of FNB Bancorp and its wholly-owned subsidiary, First National Bank of Northern California (the “Bank”). The Bank provides traditional banking services in San Francisco, San Mateo, and Santa Clara counties.

All intercompany transactions and balances have been eliminated in consolidation. The financial statements include all adjustments of a normal and recurring nature, which are, in the opinion of management, necessary for a fair presentation of the financial position and results of operations for the periods presented.

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and, therefore, do not include all information and footnotes normally included in annual financial statements prepared in conformity with accounting principles generally accepted in the United States of America. Accordingly, these consolidated financial statements should be read in conjunction with the consolidated audited financial statements and notes thereto for the year ended December 31, 2015. Results of operations for interim periods are not necessarily indicative of results for the full year. Certain prior year information has been reclassified to conform to current year presentation. The reclassifications had no impact on consolidated net earnings or stockholders’ equity.

**NOTE B – STOCK OPTION PLANS**

Stock option expense is recorded based on the fair value of option contracts issued. The fair value is determined using an option pricing model that considers the expected contract term, the risk free interest rate, the volatility of the Company’s stock price and the level of dividends the Company is expected to pay.

Measurement of the cost of the stock options granted is based on the grant-date fair value of each stock option using the Black-Scholes valuation model. The cost is then amortized over each option’s requisite service period. The expected term of options granted is derived from the period of time the options are expected to be outstanding. The risk free rate is based on the yield of an equivalent maturity U.S. Treasury note. Volatility is calculated using historical price changes on a monthly basis over the option’s expected life.

The amount of compensation expense for options recorded in the quarters ended September 30, 2016 and 2015 was \$70,000 and \$61,000 respectively. There was no income tax benefit for the quarter ended September 30, 2016, and 2015, respectively. The amount of compensation expense for options recorded in the nine months ended September 30, 2016 and September 30, 2015 was \$227,000 and \$183,000, respectively. There was an income tax benefit of \$0 and \$154,000 recorded for the nine months ended September 30, 2016 and 2015, respectively. There were no options granted for the first nine months ended September 30, 2016 and 2015 respectively.



The intrinsic value of options exercised during the nine months ended September 30, 2016 was \$1,151,000 and \$671,000, respectively. The intrinsic value for options exercised during the nine months ended September 30, 2015 was \$671,000. The intrinsic value for options exercisable at September 30, 2016 and 2015 was \$3,994,000 and \$3,042,000, respectively.

The amount of total unrecognized compensation expense related to non-vested options at September 30, 2016 was \$817,000, and the weighted average period over which it will be amortized is 3.4 years.

#### NOTE C – EARNINGS PER SHARE CALCULATION

Earnings per common share (EPS) are computed based on the weighted average number of common shares outstanding during the period. Basic EPS excludes dilution and is computed by dividing net earnings available to common stockholders (after deducting dividends and related accretion on preferred stock) by the weighted average of common shares outstanding. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. The number of potential common shares included in the quarterly diluted EPS is computed using the average market price during the three months included in the reporting period under the treasury stock method. The number of potential common shares included in year-to-date diluted EPS is a year-to-date weighted average of potential shares included in each quarterly diluted EPS computation. All common stock equivalents are anti-dilutive when a net loss occurs. A 5% stock dividend was declared and paid in the fourth quarter of 2015. Prior per share amounts have been adjusted to reflect the 5% stock dividend.

Earnings per share have been computed based on the following:

(Dollar amounts in thousands)

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
Net earnings	\$ 2,444	\$ 2,239	\$ 7,459	\$ 6,109
Average number of shares outstanding	4,612	4,524	4,582	4,508
Effect of dilutive options	105	119	118	127
Average number of shares outstanding used to calculate diluted earnings per share	4,717	4,643	4,700	4,635
Anti-dilutive options not included	68	103	70	104

**NOTE D – SECURITIES AVAILABLE FOR SALE**

The amortized cost and fair values of securities available-for-sale are as follows:

(Dollar amounts in thousands)

	<u>Amortized cost</u>	<u>Unrealized gains</u>	<u>Unrealized losses</u>	<u>Fair value</u>
<b>September 30, 2016</b>				
U.S. Treasury securities	\$ 975	\$ 28	\$ —	\$ 1,003
Obligations of U.S. government agencies	60,724	974	(1)	61,697
Mortgage-backed securities	98,933	2,219	(118)	101,034
Obligations of states and political subdivisions	154,304	4,344	(131)	158,517
Corporate debt	36,219	412	(5)	36,626
	<u>\$ 351,155</u>	<u>\$ 7,977</u>	<u>\$ (255)</u>	<u>\$ 358,877</u>
<b>December 31, 2015</b>				
U.S. Treasury securities	\$ 7,004	\$ 14	\$ (18)	\$ 7,000
Obligations of U.S. government agencies	84,842	168	(401)	84,609
Mortgage-backed securities	61,579	641	(557)	61,663
Obligations of states and political subdivisions	132,125	3,148	(83)	135,190
Corporate debt	41,045	50	(350)	40,745
	<u>\$ 326,595</u>	<u>\$ 4,021</u>	<u>\$ (1,409)</u>	<u>\$ 329,207</u>

An analysis of gross unrealized losses of the available-for-sale investment securities portfolio as of September 30, 2016 and December 31, 2015 follows:

(Dollar amounts in thousands)

	<u>Total Fair Value</u>	<u>Less than 12 Months Unrealized Losses</u>	<u>Total Fair Value</u>	<u>12 Months or Longer Unrealized Losses</u>	<u>Total Fair Value</u>	<u>Total Unrealized Losses</u>
<b>September 30, 2016</b>						
Obligations of U.S.						
Government agencies	\$ —	\$ —	\$ 1,008	\$ (1)	\$ 1,008	\$ (1)
Mortgage-backed securities	18,864	(114)	2,627	(4)	21,491	(118)
Obligations of states and political subdivisions	13,679	(126)	1,810	(5)	15,489	(131)
Corporate debt	2,015	(3)	1,000	(2)	3,015	(5)
Total	<u>\$ 34,558</u>	<u>\$ (243)</u>	<u>\$ 6,445</u>	<u>\$ (12)</u>	<u>\$ 41,003</u>	<u>\$ (255)</u>

	<b>Total Fair Value</b>	<b>12 Months Unrealized Losses</b>	<b>Total Fair Value</b>	<b>or Longer Unrealized Losses</b>	<b>Total Fair Value</b>	<b>Total Unrealized Losses</b>
December 31, 2015						
U. S. Treasury securities	\$ 5,042	\$ (18)	\$ —	\$ —	\$ 5,042	\$ (18)
Obligations of U.S.						
Government agencies	55,382	(338)	4,976	(62)	60,358	(401)
Mortgage-backed securities	19,458	(193)	16,714	(365)	36,172	(557)
Obligations of states and political subdivisions	14,988	(74)	1,856	(10)	16,844	(83)
Corporate debt	27,130	(300)	4,449	(50)	31,579	(350)
<b>Total</b>	<b>\$ 122,000</b>	<b>\$ (923)</b>	<b>\$ 27,995</b>	<b>\$ (487)</b>	<b>\$ 149,995</b>	<b>\$ (1,409)</b>

At September 30, 2016, there were 6 securities in an unrealized loss position for twelve consecutive months or more. At the same time, there were 33 securities in an unrealized loss position for less than twelve consecutive months. Management periodically evaluates each security in an unrealized loss position to determine if the impairment is temporary or other-than-temporary. Management reviews market rates, the entity's financial condition and any relevant news items or legal/tax/regulatory changes. The unrealized losses are due solely to interest rate changes and the Company does not intend to sell nor expects it will be required to sell investment securities identified with impairments prior to the earliest of forecasted recovery or the maturity of the underlying investment security. Management has determined that no investment security was other-than-temporarily impaired at September 30, 2016 and December 31, 2015.

The amortized cost and carrying value of available-for-sale debt securities as of September 30, 2016 by contractual maturity are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

September 30, 2016:

(Dollar amounts in thousands)

	<b>Amortized Cost</b>	<b>Fair Value</b>
Available-for-sale:		
Due in one year or less	\$ 12,725	\$ 12,755
Due after one through five years	146,953	150,017
Due after five years through ten years	138,771	142,744
Due after ten years	52,706	53,361
	<b>\$ 351,155</b>	<b>\$ 358,877</b>

For the nine months ended September 30, 2016, gross realized gains amounted to \$381,000 on securities sold or called for \$35,400,000. For the nine months ended September 30, 2015, gross realized gains amounted to \$250,000 on securities sold for \$11,463,000. For the nine months ended September 30, 2016 and September 30, 2015, respectively, there were no gross realized losses on securities sold. For the three months ended September 30, 2016, gross realized gains amounted to \$140,000 on securities sold for \$14,178,000. For the three months ended September 30, 2015, gross realized gains were \$29,000 on securities sold for \$3,187,000. For the three months ended September 30, 2016 and September 30, 2015, respectively, there were no gross realized losses on securities sold. At September 30, 2016, securities with an amortized cost of \$102,449,000 and fair value of \$104,857,000 were pledged as collateral for public deposits and for other purposes required by law.

#### NOTE E - LOANS

Loans are summarized as follows at September 30, 2016 and December 31, 2015:

(Dollar amounts in thousands)

September 30, 2016	FNB Bancorp Originated	PNCI	PCI	Total Balance September 30, 2016
Commercial real estate	\$ 331,392	\$ 72,339	\$ 1,233	\$ 404,964
Real estate construction	36,654	1,509	—	38,163
Real estate multi-family	74,712	9,232	—	83,944
Real estate 1 to 4 family	148,993	24,448	—	173,441
Commercial & industrial	42,839	8,031	—	50,870
Consumer	1,630	—	—	1,630
Gross loans	636,220	115,559	1,233	753,012
Net deferred loan fees	(1,513)	—	—	(1,513)
Allowance for loan losses	(10,092)	—	—	(10,092)
Net loans	\$ 624,615	\$ 115,559	\$ 1,233	\$ 741,407

(Dollar amounts in thousands)

December 31, 2015	FNB Bancorp Originated	PNCI	PCI	Total Balance December 31, 2015
Commercial real estate	\$ 314,141	\$ 84,548	\$ 1,304	\$ 399,993
Real estate construction	38,909	5,907	—	44,816
Real estate multi-family	47,607	15,990	—	63,597
Real estate 1 to 4 family	153,872	18,092	—	171,964
Commercial & industrial	39,894	12,139	—	52,033
Consumer	1,574	—	—	1,574
Gross loans	595,997	136,676	1,304	733,977
Net deferred loan fees	(1,260)	—	—	(1,260)
Allowance for loan losses	(9,970)	—	—	(9,970)
Net loans	\$ 584,767	\$ 136,676	\$ 1,304	\$ 722,747

Note: PNCI means Purchased, Not Credit Impaired. PCI means Purchased, Credit Impaired.

**Recorded Investment in Loans at September 30, 2016**

(Dollar amounts in thousands)

	<u>Commercial Real Estate</u>	<u>Real Estate Construction</u>	<u>Real Estate Multi family</u>	<u>Real Estate 1 to 4 family</u>	<u>Commercial &amp; industrial</u>	<u>Consumer</u>	<u>Total</u>
<b>Loans:</b>							
Ending balance	\$ 404,964	\$ 38,163	\$ 83,944	\$ 173,441	\$ 50,871	\$ 1,630	\$ 753,013
Ending balance: individually evaluated for impairment	\$ 10,214	\$ 2,072	\$ —	\$ 3,620	\$ 1,236	\$ —	\$ 17,142
Ending balance: collectively evaluated for impairment	\$ 394,750	\$ 36,091	\$ 83,944	\$ 169,821	\$ 49,635	\$ 1,630	\$ 735,871

**Recorded Investment in Loans at December 31, 2015**

(Dollar amounts in thousands)

	<u>Commercial Real Estate</u>	<u>Real Estate Construction</u>	<u>Real Estate Multi Family</u>	<u>Real Estate 1 to 4 Family</u>	<u>Commercial &amp; industrial</u>	<u>Consumer</u>	<u>Total</u>
<b>Loans:</b>							
Ending balance	\$ 399,993	\$ 44,816	\$ 63,597	\$ 171,964	\$ 52,033	\$ 1,574	\$ 733,977
Ending balance: individually evaluated for impairment	\$ 11,292	\$ 2,154	\$ —	\$ 4,218	\$ 1,782	\$ —	\$ 19,446
Ending balance: collectively evaluated for impairment	\$ 388,701	\$ 42,662	\$ 63,597	\$ 167,746	\$ 50,251	\$ 1,574	\$ 714,531

**Recorded Investment in Loans at September 30, 2015**

(Dollar amounts in thousands)

	<u>Commercial Real Estate</u>	<u>Real Estate Construction</u>	<u>Real Estate Multi family</u>	<u>Real Estate 1 to 4 family</u>	<u>Commercial &amp; industrial</u>	<u>Consumer</u>	<u>Total</u>
<b>Loans:</b>							
Ending balance	<u>\$ 394,090</u>	<u>\$ 35,868</u>	<u>\$ 63,928</u>	<u>\$ 172,280</u>	<u>\$ 39,843</u>	<u>\$ 1,497</u>	<u>\$ 707,506</u>
Ending balance: individually evaluated for impairment	<u>\$ 9,501</u>	<u>\$ 2,162</u>	<u>\$ —</u>	<u>\$ 4,857</u>	<u>\$ 1,813</u>	<u>\$ —</u>	<u>\$ 18,333</u>
Ending balance: collectively evaluated for impairment	<u>\$ 384,589</u>	<u>\$ 33,706</u>	<u>\$ 63,928</u>	<u>\$ 167,423</u>	<u>\$ 38,030</u>	<u>\$ 1,497</u>	<u>\$ 689,173</u>

**Impaired Loans**  
**As of and for the three months ended September 30, 2016**

(Dollar amounts in thousands)

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Income Recognized
<b>With no related allowance recorded</b>					
Commercial real estate	\$ 8,554	\$ 9,676	\$ —	\$ 8,449	\$ 95
Commercial real estate construction	2,072	2,259	—	2,090	—
Residential- 1 to 4 family	605	605	—	834	—
Commercial and industrial	116	116	—	316	6
Total	<u>11,347</u>	<u>12,656</u>	<u>—</u>	<u>11,689</u>	<u>101</u>
<b>With an allowance recorded</b>					
Commercial real estate	\$ 1,660	\$ 1,660	\$ 72	\$ 1,664	\$ 17
Residential- 1 to 4 family	3,015	2,618	453	3,019	13
Commercial and industrial	1,120	1,326	101	1,087	—
Total	<u>5,795</u>	<u>5,604</u>	<u>626</u>	<u>5,770</u>	<u>30</u>
<b>Total</b>					
Commercial real estate	\$ 10,214	\$ 11,336	\$ 72	\$ 10,113	\$ 112
Commercial real estate construction	2,072	2,259	—	2,090	—
Residential- 1 to 4 family	3,620	3,223	453	3,853	13
Commercial and industrial	1,236	1,442	101	1,403	6
Grand total	<u>\$ 17,142</u>	<u>\$ 18,260</u>	<u>\$ 626</u>	<u>\$ 17,459</u>	<u>\$ 131</u>

**Impaired Loans**

**As of and for the nine months ended September 30, 2016**

(Dollar amounts in thousands)

	<u>Recorded Investment</u>	<u>Unpaid Principal Balance</u>	<u>Related Allowance</u>	<u>Average Recorded Investment</u>	<u>Income Recognized</u>
<b>With no related allowance recorded</b>					
Commercial real estate	\$ 8,554	\$ 9,676	\$ —	\$ 8,637	\$ 520
Commercial real estate construction	2,072	2,259	—	2,118	104
Residential- 1 to 4 family	605	605	—	303	21
Commercial and industrial	116	116	—	320	20
Total	<u>11,347</u>	<u>12,656</u>	<u>—</u>	<u>11,378</u>	<u>665</u>
<b>With an allowance recorded</b>					
Commercial real estate	\$ 1,660	\$ 1,660	\$ 72	\$ 1,675	\$ 68
Residential- 1 to 4 family	3,015	2,618	453	3,032	80
Commercial and industrial	1,120	1,326	101	1,107	4
Total	<u>5,795</u>	<u>5,604</u>	<u>626</u>	<u>5,814</u>	<u>152</u>
<b>Total</b>					
Commercial real estate	\$ 10,214	\$ 11,336	\$ 72	\$ 10,312	\$ 588
Commercial real estate construction	2,072	2,259	—	2,118	104
Residential- 1 to 4 family	3,620	3,223	453	3,335	101
Commercial and industrial	1,236	1,442	101	1,427	24
Grand total	<u>\$ 17,142</u>	<u>\$ 18,260</u>	<u>\$ 626</u>	<u>\$ 17,192</u>	<u>\$ 817</u>



**Impaired Loans**

As of and for the year ended December 31, 2015

(Dollar amounts in thousands)

	<u>Recorded Investment</u>	<u>Unpaid Principal Balance</u>	<u>Related Allowance</u>	<u>Average Recorded Investment</u>	<u>Income Recognized</u>
<b>With no related allowance recorded</b>					
Commercial real estate	\$ 8,169	\$ 9,271	\$ —	\$ 8,379	\$ 282
Commercial real estate construction	2,154	2,337	—	2,264	130
Residential- 1 to 4 family	457	457	—	460	36
Commercial and industrial	524	524	—	731	27
Total	<u>11,304</u>	<u>12,589</u>	<u>—</u>	<u>11,834</u>	<u>475</u>
<b>With an allowance recorded</b>					
Commercial real estate	\$ 2,634	\$ 2,638	\$ 96	\$ 2,664	\$ 160
Residential- 1 to 4 family	3,761	3,782	479	3,786	149
Commercial and industrial	1,258	1,497	182	1,484	7
Total	<u>7,653</u>	<u>7,917</u>	<u>757</u>	<u>7,934</u>	<u>316</u>
<b>Total</b>					
Commercial real estate	\$ 10,803	\$ 11,909	\$ 96	\$ 11,043	\$ 442
Commercial real estate construction	2,154	2,337	—	2,264	130
Residential- 1 to 4 family	4,218	4,239	479	4,246	185
Commercial and industrial	1,782	2,021	182	2,215	34
Grand total	<u>\$ 18,957</u>	<u>\$ 20,506</u>	<u>\$ 757</u>	<u>\$ 19,768</u>	<u>\$ 791</u>

**Impaired Loans**  
**As of and for the three months ended September 30, 2015**

(Dollar amounts in thousands)

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Income Recognized
<b>With no related allowance recorded</b>					
Commercial real estate	\$ 4,392	\$ 5,271	\$ —	\$ 4,402	\$ 92
Commercial real estate construction	2,162	2,345	—	2,341	32
Residential- 1 to 4 family	1,475	1,476	—	1,479	18
Commercial and industrial	528	782	—	537	9
Total	<u>8,557</u>	<u>9,874</u>	<u>—</u>	<u>8,758</u>	<u>151</u>
<b>With an allowance recorded</b>					
Commercial real estate	\$ 5,109	\$ 5,113	\$ 126	\$ 5,121	\$ 66
Residential- 1 to 4 family	3,382	2,972	522	3,374	27
Commercial and industrial	1,285	1,539	224	1,339	—
Total	<u>9,776</u>	<u>9,624</u>	<u>872</u>	<u>9,834</u>	<u>93</u>
<b>Total</b>					
Commercial real estate	\$ 9,501	\$ 10,384	\$ 126	\$ 9,523	\$ 158
Commercial real estate construction	2,162	2,345	—	2,341	32
Residential- 1 to 4 family	4,857	4,448	522	4,853	45
Commercial and industrial	1,813	2,321	224	1,876	9
Grand total	<u>\$ 18,333</u>	<u>\$ 19,498</u>	<u>\$ 872</u>	<u>\$ 18,593</u>	<u>\$ 244</u>

**Impaired Loans**  
**As of and for the nine months ended September 30, 2015**

(Dollar amounts in thousands)

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Income Recognized
<b>With no related allowance recorded</b>					
Commercial real estate	\$ 4,392	\$ 5,271	\$ —	\$ 4,867	\$ 217
Commercial real estate construction	2,162	2,345	—	2,359	100
Residential - 1 to 4 family	1,475	1,476	—	1,482	49
Commercial and industrial	528	782	—	4,410	27
Total	<u>8,557</u>	<u>9,874</u>	<u>—</u>	<u>13,118</u>	<u>393</u>
<b>With an allowance recorded</b>					
Commercial real estate	\$ 5,109	\$ 5,113	\$ 126	\$ 5,162	\$ 196
Residential - 1 to 4 family	3,382	2,972	522	3,202	96
Commercial and industrial	1,285	1,539	224	1,489	5
Total	<u>9,776</u>	<u>9,624</u>	<u>872</u>	<u>9,853</u>	<u>297</u>
<b>Total</b>					
Commercial real estate	\$ 9,501	\$ 10,384	\$ 126	\$ 10,029	\$ 413
Commercial real estate construction	2,162	2,345	—	2,359	100
Residential - 1 to 4 family	4,857	4,448	522	4,684	145
Commercial and industrial	1,813	2,321	224	5,899	32
Grand total	<u>\$ 18,333</u>	<u>\$ 19,498</u>	<u>\$ 872</u>	<u>\$ 22,971</u>	<u>\$ 690</u>

Nonaccrual loans totaled \$6,903,000 and \$7,915,000 as of September 30, 2015 and December 31, 2015. The difference between impaired loans and nonaccrual loans represents loans that are restructured, are performing under modified loan agreements, and accruing interest.

(Dollar amounts in thousands)	Loans on Nonaccrual Status as of	
	September 30, 2016	December 31, 2015
Commercial real estate	\$ 5,707	\$ 6,021
Real estate 1 to 4 family	76	636
Commercial and industrial	1,120	1,258
Total	<u>\$ 6,903</u>	<u>\$ 7,915</u>

Interest income on impaired loans of \$817,000 and \$690,000 was recognized for cash payments received during the nine months ended September 30, 2016 and 2015 respectively. \$791,000 was recognized for cash payments received during the year ended December 31, 2015. Interest income recognized for cash payments received for the three months ended September 30, 2016 and 2015 was \$131,000 and \$244,000 respectively. The amount of interest on impaired loans not collected for the three and nine months ended September 30, 2016 was \$164,313 and \$439,579 respectively, and for the year ended December 31, 2015 was \$460,390. For the three and nine months ended September 30, 2015, the amount of interest on impaired loans not collected was \$86,430 and \$284,198, respectively. The cumulative amount of unpaid interest on impaired loans was \$3,844,000 for the nine months ended September 30, 2016, and \$3,405,000 for the year ended December 31, 2015.

### Troubled Debt Restructurings

(dollars in thousands)	Total troubled debt restructured loans outstanding at					
	September 30, 2016			December 31, 2015		
	Accrual status	Non- accrual status	Total modifications	Accrual status	Non- accrual status	Total modifications
Commercial real estate	\$ 4,625	\$ 1,233	\$ 5,858	\$ 4,775	\$ —	\$ 4,775
Real Estate construction	1,212	—	1,212	1,283	—	1,283
Real estate 1 to 4 family	3,543	—	3,543	3,583	2,060	5,643
Commercial & industrial	—	929	929	524	1,043	1,567
Total	<u>\$ 9,380</u>	<u>\$ 2,162</u>	<u>\$ 11,542</u>	<u>\$ 10,165</u>	<u>\$ 3,103</u>	<u>\$ 13,268</u>

### *Modification Categories*

The Company offers a variety of modifications to borrowers. The modification categories offered can generally be described in the following categories.

**Rate Modification** – A modification in which the interest rate is changed.

**Term modification** – A modification in which the maturity date, timing of payments, or frequency of payments is changed.

**Interest Only Modification** – A modification in which the loan is converted to interest only payments for a period of time.

**Payment Modification** – A modification in which the dollar amount of the payment is changed, other than an interest only modification described above.

There were no commitments for additional funding of troubled debt restructured loans as of September 30, 2016. There was one loan modified during the nine months ended September 30, 2015. There were no payment defaults during the three and nine month period ended September 30, 2016 or September 30, 2015 that were related to receivables modified as TDRs in the last twelve months.

The following table details modifications for the nine months ended September 30, 2015:

	<b>Modifications For the nine months ended September 30, 2015</b>		
	<u>Number of Contracts</u>	<u>Pre- Modification Outstanding Recorded Investment</u>	<u>Post- Modification Outstanding Recorded Investment</u>
(Dollar amounts in thousands)			
Real estate 1 to 4 family	1	\$ 474	\$ 474
Total	<u>1</u>	<u>\$ 474</u>	<u>\$ 474</u>

The restructuring total above was a modification of interest rate, and as a result, payment. There was no principal reduction granted.

**Allowance for Credit Losses**  
**For the Three Months Ended September 30, 2016**

(Dollar amounts in thousands)

	Commercial Real estate	Real Estate Construction	Real Estate Multi family	Real Estate 1 to 4 family	Commercial & industrial	Consumer	Total
<b>Allowance for credit losses</b>							
Beginning balance	\$ 6,206	\$ 404	\$ 335	\$ 2,261	\$ 799	\$ 33	\$ 10,038
Charge-offs	—	—	—	—	—	(8)	(8)
Recoveries	2	—	—	23	37	—	62
Provision	(63)	138	(3)	(77)	(47)	52	—
Ending balance	<u>\$ 6,145</u>	<u>\$ 542</u>	<u>\$ 332</u>	<u>\$ 2,207</u>	<u>\$ 789</u>	<u>\$ 77</u>	<u>\$ 10,092</u>
<b>Ending balance:</b>							
individually evaluated for impairment	<u>\$ 72</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 453</u>	<u>\$ 101</u>	<u>\$ —</u>	<u>\$ 626</u>
Ending balance:							
collectively evaluated for impairment	<u>\$ 6,073</u>	<u>\$ 542</u>	<u>\$ 332</u>	<u>\$ 1,754</u>	<u>\$ 688</u>	<u>\$ 77</u>	<u>\$ 9,466</u>

**Allowance for Credit Losses**  
**For the Nine Months Ended September 30, 2016**

(Dollar amounts in thousands)

	Commercial Real Estate	Real Estate Construction	Real Estate Multi Family	Real Estate 1 to 4 Family	Commercial & industrial	Consumer	Total
<b>Allowance for credit losses</b>							
Beginning balance	\$ 6,059	\$ 589	\$ 243	\$ 2,176	\$ 853	\$ 50	\$ 9,970
Charge-offs	—	—	—	(12)	(165)	(18)	(195)
Recoveries	6	—	—	42	119	—	167
Provision	80	(46)	89	1	(19)	45	150
Ending balance	<u>\$ 6,145</u>	<u>\$ 543</u>	<u>\$ 332</u>	<u>\$ 2,207</u>	<u>\$ 788</u>	<u>\$ 77</u>	<u>\$ 10,092</u>
<b>Ending balance:</b>							
individually evaluated for impairment	<u>\$ 72</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 453</u>	<u>\$ 101</u>	<u>\$ —</u>	<u>\$ 626</u>
Ending balance:							
collectively evaluated for impairment	<u>\$ 6,073</u>	<u>\$ 542</u>	<u>\$ 332</u>	<u>\$ 1,754</u>	<u>\$ 688</u>	<u>\$ 77</u>	<u>\$ 9,466</u>

**Allowance for Credit Losses**  
**As of and For the Year Ended December 31, 2015**

(Dollar amounts in thousands)

	Commercial Real estate	Real Estate Construction	Real Estate Multi family	Real Estate 1 to 4 family	Commercial & industrial	Consumer	Total
<b>Allowance for credit losses</b>							
Beginning balance	\$ 5,549	\$ 849	\$ 206	\$ 1,965	\$ 1,073	\$ 58	\$ 9,700
Charge-offs	—	—	—	(45)	—	(36)	(81)
Recoveries	576	—	—	15	60	5	656
Provision	(66)	(260)	37	241	(280)	23	(305)
Ending balance	<u>\$ 6,059</u>	<u>\$ 589</u>	<u>\$ 243</u>	<u>\$ 2,176</u>	<u>\$ 853</u>	<u>\$ 50</u>	<u>\$ 9,970</u>
<b>Ending balance:</b>							
individually evaluated for impairment	<u>\$ 96</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 479</u>	<u>\$ 182</u>	<u>\$ —</u>	<u>\$ 757</u>
Ending balance:							
collectively evaluated for impairment	<u>\$ 5,963</u>	<u>\$ 589</u>	<u>\$ 243</u>	<u>\$ 1,697</u>	<u>\$ 671</u>	<u>\$ 50</u>	<u>\$ 9,213</u>

**Allowance for Credit Losses**  
**For the Three Months Ended September 30, 2015**

(Dollar amounts in thousands)

	Commercial Real estate	Real Estate Construction	Real Estate Multi family	Real Estate 1 to 4 family	Commercial & industrial	Consumer	Total
<b>Allowance for credit losses</b>							
Beginning balance	\$ 6,027	\$ 697	\$ 198	\$ 2,014	\$ 848	\$ 52	\$ 9,836
Charge-offs	—	—	—	—	(23)	—	(23)
Recoveries	15	—	—	7	26	4	52
Provision	(67)	(49)	(10)	289	(73)	(15)	75
Ending balance	<u>\$ 5,975</u>	<u>\$ 648</u>	<u>\$ 188</u>	<u>\$ 2,310</u>	<u>\$ 778</u>	<u>\$ 41</u>	<u>\$ 9,940</u>
<b>Ending balance:</b>							
individually evaluated for impairment	<u>\$ 126</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 522</u>	<u>\$ 224</u>	<u>\$ —</u>	<u>\$ 872</u>
Ending balance:							
collectively evaluated for impairment	<u>\$ 5,849</u>	<u>\$ 648</u>	<u>\$ 188</u>	<u>\$ 1,788</u>	<u>\$ 554</u>	<u>\$ 41</u>	<u>\$ 9,068</u>

**Allowance for Credit Losses**  
**For the Nine Months Ended September 30, 2015**

(Dollar amounts in thousands)

	Commercial Real estate	Real Estate Construction	Real Estate Multi family	Real Estate 1 to 4 family	Commercial & industrial	Consumer	Total
<b>Allowance for credit losses</b>							
Beginning balance	\$ 5,549	\$ 849	\$ 206	\$ 1,965	\$ 1,073	\$ 58	\$ 9,700
Charge-offs	—	—	—	(45)	(23)	(11)	(79)
Recoveries	37	—	—	8	45	4	94
Provision	389	(201)	(18)	382	(317)	(10)	225
Ending balance	<u>\$ 5,975</u>	<u>\$ 648</u>	<u>\$ 188</u>	<u>\$ 2,310</u>	<u>\$ 778</u>	<u>\$ 41</u>	<u>\$ 9,940</u>
<b>Ending balance:</b>							
individually evaluated for impairment	<u>\$ 126</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 522</u>	<u>\$ 224</u>	<u>\$ —</u>	<u>\$ 872</u>
Ending balance:							
collectively evaluated for impairment	<u>\$ 5,849</u>	<u>\$ 648</u>	<u>\$ 188</u>	<u>\$ 1,788</u>	<u>\$ 554</u>	<u>\$ 41</u>	<u>\$ 9,068</u>



### Risk rating system

Loans to borrowers graded as pass or pooled loans represent loans to borrowers of acceptable or better credit quality. They demonstrate sound financial positions, repayment capacity and credit history. They have an identifiable and stable source of repayment.

Special mention loans have potential weaknesses that deserve management's attention. If left uncorrected these potential weaknesses may result in a deterioration of the repayment prospects for the asset or in the Bank's credit position at some future date. These assets are "not adversely classified" and do not expose the Bank to sufficient risk to warrant adverse classification.

Substandard loans are inadequately protected by current sound net worth, paying capacity of the borrower, or pledged collateral. Loans are normally classified as Substandard when there are unsatisfactory characteristics causing more than acceptable levels of risk. A substandard loan normally has one or more well-defined weaknesses that could jeopardize the repayment of the debt. These well-defined weaknesses may include a) cash flow deficiency, which may jeopardize future payments; b) sale of non-collateral assets has become primary source of repayment; c) the borrower is bankrupt; or d) for any other reason, future repayment is dependent on court action.

Doubtful loans represent credits with weakness inherent in the substandard classification and where collection or liquidation in full is highly questionable. To be classified doubtful, there must be specific pending factors which prevent the Loan Review Officer from determining the amount of loss contained in the credit. When the amount of loss can be reasonably estimated, that amount is classified as "loss" and the remainder is classified as Substandard.

### *Real Estate – Multi-Family*

Our multi-family commercial real estate loans are secured by multi-family properties located primarily in San Mateo and San Francisco Counties. These loans are made to investors where our primary source of repayment is from cash flows generated by the properties, through rent collections. The borrowers' promissory notes are secured with recorded liens on the underlying properties. The borrowers would normally also be required to personally guarantee repayment of the loans. The bank uses conservative underwriting standards in reviewing applications for credit. Generally, our borrowers have multiple sources of income, so if cash flow generated from the property declines, at least in the short term, the borrowers can normally cover these short term cash flow deficiencies from their available cash reserves. Risk of loss to the Bank is increased when there are cash flow decreases sufficiently large and for such a prolonged period of time that loan payments can no longer be made by the borrowers.

### *Commercial Real Estate Loans*

Other commercial real estate loans consist of loans secured by non-farm, non-residential properties, including, but not limited to industrial, hotel, assisted care, retail, office and mixed use buildings.

Our commercial real estate loans are made primarily to investors or small businesses where our primary source of repayment is from cash flows generated by the properties, either through rent collection or business profits. The borrower's promissory notes are secured with recorded liens on the underlying property. The borrowers would normally also be required to personally guarantee repayment of the loan. The Bank uses conservative underwriting standards in reviewing applications for credit. Generally, our borrowers have multiple sources of income, so if cash flow generated from the property declines, at least in the short term, the borrowers can normally cover these short term cash flow deficiencies from their available cash reserves. Risk of loss to the Bank is increased when there are cash flow decreases sufficiently large and for such a prolonged period of time that loan payments can no longer be made by the borrowers.

### *Real Estate Construction Loans*

Our real estate construction loans are generally made to borrowers who are rehabilitating a building, converting a building use from one type of use to another, or developing land and building residential or commercial structures for sale or lease. The borrower's promissory notes are secured with recorded liens on the underlying property. The borrowers would normally also be required to personally guarantee repayment of the loan. The Bank uses conservative underwriting standards in reviewing applications for credit. Generally, our borrowers have sufficient resources to make the required construction loan payments during the construction and absorption or lease-up period. After construction is complete, the loans are normally paid off from proceeds from the sale of the building or through a refinance to a commercial real estate loan. Risk of loss to the Bank is increased when there are material construction cost overruns, significant delays in the time to complete the project and/or there has been a material drop in the value of the projects in the marketplace since the inception of the loan.

### *Real Estate-1 to 4 family Loans*

Our residential real estate loans are generally made to borrowers who are buying or refinancing their primary personal residence or a rental property of 1-4 single family residential units. The Bank uses conservative underwriting standards in reviewing applications for credit. Risk of loss to the Bank is increased when borrowers lose their primary source of income and/or property values decline significantly.

### *Commercial and Industrial Loans*

Our commercial and industrial loans are generally made to small businesses to provide them with at least some of the working capital necessary to fund their daily business operations. These loans are generally either unsecured or secured by fixed assets, accounts receivable and/or inventory. The borrowers would normally also be required to personally guarantee repayment of the loan. The Bank uses conservative underwriting standards in reviewing applications for credit. Risk of loss to the Bank is increased when our small business customers experience a significant business downturn, incur significant financial losses, or file for relief from creditors through bankruptcy proceedings.

### *Consumer Loans*

Our consumer and installment loans generally consist of personal loans, credit card loans, automobile loans or other loans secured by personal property. The Bank uses conservative underwriting standards in reviewing applications for credit. Risk of loss to the Bank is increased if borrowers lose their primary source of income, or file for relief from creditors through bankruptcy proceedings.

**Age Analysis of Past Due Loans  
As of September 30, 2016**

(Dollar amounts in thousands)

	30-59 Days Past Due	60-89 Days Past Due	Over 90 Days	Total Past Due	Current	Total Loans
<b>Originated</b>						
Commercial real estate	\$ —	\$ —	\$ —	\$ —	\$ 331,392	\$ 331,392
Real estate construction	—	—	140	140	36,514	36,654
Real estate multi family	—	—	—	—	74,712	74,712
Real estate-1 to 4 family	—	—	76	76	148,917	148,993
Commercial and industrial	845	23	1,120	1,988	40,852	42,840
Consumer	—	—	—	—	1,630	1,630
Total	<u>\$ 845</u>	<u>\$ 23</u>	<u>\$ 1,336</u>	<u>\$ 2,204</u>	<u>\$ 634,017</u>	<u>\$ 636,221</u>
<b>Purchased</b>						
<i>Not credit impaired</i>						
Commercial real estate	\$ —	\$ —	\$ 550	\$ 550	\$ 71,789	\$ 72,339
Real estate construction	—	—	—	—	1,509	1,509
Real estate multi-family	—	—	—	—	9,232	9,232
Real estate-1 to 4 family	—	2,150	—	2,150	22,298	24,448
Commercial and industrial	—	—	—	—	8,031	8,031
Total	<u>\$ —</u>	<u>\$ 2,150</u>	<u>\$ 550</u>	<u>\$ 2,700</u>	<u>\$ 112,859</u>	<u>\$ 115,559</u>
<b>Purchased</b>						
<i>Credit impaired</i>						
Commercial real estate	\$ —	\$ —	\$ —	\$ —	\$ 1,233	\$ 1,233
Total	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 1,233</u>	<u>\$ 1,233</u>

At September 30, 2016, there were no loans 90 days or more past due where interest was still accruing.

The over 90 days column includes nonaccruals that were over 90 days, but does not include loans that are in nonaccrual status for reasons other than past due.

**Age Analysis of Past Due Loans  
As of December 31, 2015**

(Dollar amounts in thousands)

	30-59 Days Past Due	60-89 Days Past Due	Over 90 Days	Total Past Due	Current	Total Loans
<b>Originated</b>						
Commercial real estate	\$ 1,541	\$ —	\$ —	\$ 1,541	\$ 312,600	\$ 314,141
Real estate construction	706	725	—	1,431	37,478	38,909
Real estate multi family	—	—	—	—	47,607	47,607
Real estate 1 to 4 family	1,363	737	71	2,171	151,701	153,872
Commercial & industrial	—	—	1,258	1,258	38,636	39,894
Consumer	—	—	—	—	1,574	1,574
Total	<u>\$ 3,610</u>	<u>\$ 1,462</u>	<u>\$ 1,329</u>	<u>\$ 6,401</u>	<u>\$ 589,596</u>	<u>\$ 595,997</u>
<b>Purchased</b>						
<i>Not credit impaired</i>						
Commercial real estate	\$ —	\$ —	\$ 3,810	\$ 3,810	\$ 80,738	\$ 84,548
Real estate construction	—	—	—	—	5,907	5,907
Real estate multi-family	—	—	—	—	15,990	15,990
Real estate 1 to 4 family	175	—	—	175	17,917	18,092
Commercial & industrial	70	—	—	70	12,069	12,139
Total	<u>\$ 245</u>	<u>\$ —</u>	<u>\$ 3,810</u>	<u>\$ 4,055</u>	<u>\$ 132,621</u>	<u>\$ 136,676</u>
<b>Purchased</b>						
<i>Credit impaired</i>						
Commercial real estate	\$ —	\$ —	\$ —	\$ —	\$ 1,304	\$ 1,304
Total	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 1,304</u>	<u>\$ 1,304</u>

At December 31, 2015 there were no loans that were 90 days or more past due where interest was still accruing.

The over 90 days column includes nonaccrual loans that were over 90 days, but does not include loans that are in nonaccrual status for reasons other than past due.

**Credit Quality Indicators**  
**As of September 30, 2016**

(Dollar amounts in thousands)

<b>Originated</b>	Pass	Special mention	Sub- standard	Doubtful	Total loans
Commercial real estate	\$ 328,230	\$ —	\$ 3,162	\$ —	\$ 331,392
Real estate construction	35,654	—	1,000	—	36,654
Real estate multi-family	74,712	—	—	—	74,712
Real estate-1 to 4 family	148,917	—	76	—	148,993
Commercial and industrial	42,447	—	387	6	42,840
Consumer loans	1,630	—	—	—	1,630
<b>Total</b>	<b>\$ 631,590</b>	<b>\$ —</b>	<b>\$ 4,625</b>	<b>\$ 6</b>	<b>\$ 636,221</b>

<b>Purchased</b>					
<i>Not credit impaired</i>					
Commercial real estate	\$ 62,236	\$ 895	\$ 9,208	\$ —	\$ 72,339
Real estate construction	1,509	—	—	—	1,509
Real estate multi-family	9,232	—	—	—	9,232
Real estate-1 to 4 family	24,448	—	—	—	24,448
Commercial and industrial	7,939	—	92	—	8,031
<b>Total</b>	<b>\$ 105,364</b>	<b>\$ 895</b>	<b>\$ 9,300</b>	<b>\$ —</b>	<b>\$ 115,559</b>

<b>Purchased</b>					
<i>Credit impaired</i>					
Commercial real estate					\$ 1,233
<b>Total</b>					<b>\$ 1,233</b>

**Credit Quality Indicators**  
**As of December 31, 2015**

(Dollar amounts in thousands)

<b>Originated</b>	Pass	Special mention	Sub- standard	Doubtful	Total loans
Commercial real estate	\$ 308,164	\$ 1,857	\$ 4,120	\$ —	\$ 314,141
Real estate construction	37,850	—	1,059	—	38,909
Real estate multi-family	47,607	—	—	—	47,607
Real estate 1 to 4 family	153,285	—	587	—	153,872
Commercial & industrial	39,287	—	451	156	39,894
Consumer loans	1,574	—	—	—	1,574
<b>Totals</b>	<b>\$ 587,767</b>	<b>\$ 1,857</b>	<b>\$ 6,217</b>	<b>\$ 156</b>	<b>\$ 595,997</b>

**Purchased**

***Not credit impaired***

Commercial real estate	\$ 68,936	\$ 3,455	\$ 12,145	\$ 12	\$ 84,548
Real estate construction	5,907	—	—	—	5,907
Real estate multi-family	15,990	—	—	—	15,990
Real estate 1 to 4 family	18,092	—	—	—	18,092
Commercial & industrial	12,044	—	95	—	12,139
<b>Total</b>	<b>\$ 120,969</b>	<b>\$ 3,455</b>	<b>\$ 12,240</b>	<b>\$ 12</b>	<b>\$ 136,676</b>

**Purchased**

***Credit impaired***

Commercial real estate	\$ 1,304
<b>Total</b>	<b>\$ 1,304</b>

**NOTE F - BORROWINGS**

**Federal Home Loan Bank advances**

As of September 30, 2016 there were \$37,000,000 Federal Home Loan Bank Advances outstanding, consisting of \$8,000,000 on an overnight basis at 0.38%, \$7,000,000 at 0.40% due October 6, 2016, \$8,000,000 at 0.35% due October 24, 2016 \$6,000,000 at 0.26% due October 26, 2016 and \$8,000,000 at 0.35% due October 31, 2016.

**Corporate loan**

On March 27, 2014, FNB Bancorp received funding under a \$6,000,000 term loan credit facility. This loan carries a variable rate of interest that fluctuates on a monthly basis. The interest rate is based on the 3 month LIBOR rate plus 4%. Payments of \$50,000 in principal plus accrued interest are payable monthly. The first loan payment was due May 1, 2014. The maturity date on this credit facility is March 26, 2019. On the maturity date, all outstanding principal plus accrued interest shall become due and payable. FNB Bancorp has pledged its stock ownership in First National Bank of Northern California as collateral subject to the terms and conditions contained in the Loan Agreement and the Pledge and Security Agreement. FNB Bancorp retains the right to prepay this debt at any time upon not less than 7 days' prior written notice to Lender. The proceeds from this loan were contributed to the Bank as an additional capital contribution. This capital contribution qualified as Tier 1 capital for the Bank under regulatory capital guidelines.

## NOTE G – FAIR VALUE MEASUREMENT

The following tables present information about the Company’s assets and liabilities measured at fair value as of September 30, 2016 and December 31, 2015, and indicate the fair value techniques used by the Company to determine such fair value. In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company’s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability. Transfers between levels of the fair value hierarchy are recognized on the actual date of the event or circumstances that caused the transfer, which generally corresponds with the Company’s quarterly valuation process. During the first nine months of 2016 and 2015, there were no transfers between levels of fair value hierarchy.

The following table presents the recorded amounts of assets measured at fair value on a recurring basis:

(Dollar amounts in thousands)	Fair Value Measurements at December 31, 2015, Using			
	Fair Value 12/31/2015	Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Description				
U. S. Treasury securities	\$ 7,000	\$ 7,000	\$ —	\$ —
Obligations of U.S.				
Government agencies	84,609	—	84,609	—
Mortgage-backed securities	61,663	—	61,663	—
Obligations of states and political subdivisions	135,190	—	135,190	—
Corporate debt	40,745	—	40,745	—
Total assets measured at fair value	<u>\$ 329,207</u>	<u>\$ 7,000</u>	<u>\$ 322,207</u>	<u>\$ —</u>

The following tables present the recorded amounts of assets measured at fair value on a non-recurring ba

(Dollar amounts in thousands)	Fair Value Measurements at September 30, 2016, Using			
	Fair Value 9/30/2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Description				
Impaired loans:				
Commercial and industrial	\$ 984	\$ —	\$ —	\$ 984
Total impaired loans measured at fair value	\$ 984	\$ —	\$ —	\$ 984

(Dollar amounts in thousands)	Fair Value Measurements at December 31, 2015, Using			
	Fair Value 12/31/2015	Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Description				
Impaired loans:				
Commercial real estate loans	\$ 136	\$ —	\$ —	\$ 136
Residential-1 to 4 family loans	301	—	—	301
Commercial and industrial loans	1,065	—	—	1,065
Total impaired loans measured at fair value	\$ 1,502	\$ —	\$ —	\$ 1,502

The Bank does not record loans at fair value. However, from time to time, if a loan is considered impaired, a specific allocation within the allowance for loan losses may be required. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, liquidation value and cash flows. Those impaired loans not requiring an allowance represent loans for which the value of the expected repayments or collateral exceed the recorded investments in such loans. Impaired loans where an allowance is established based on the fair value of collateral or when the impaired loan has been written down to fair value require classification in the fair value hierarchy. If the fair value of the collateral is based on an observable market price or a current appraised value, the Bank records the impaired loans as nonrecurring Level 3. When an appraised value is not available, or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Bank also records the impaired loans as nonrecurring Level 3.



Other real estate owned is carried at the lower of historical cost or fair value less costs to sell. An appraisal (a Level 3 valuation) is obtained at the time the Bank acquires property through the foreclosure process. Any loan balance outstanding that exceeds the appraised value of the property is charged off against the allowance for loan loss at the time the property is acquired. Subsequent to acquisition, the Bank updates the property's appraised value on at least an annual basis. If the value of the property has declined during the year, a loss due to valuation impairment charge is recorded along with a corresponding reduction in the book carrying value of the property.

The Bank obtains third party appraisals on its impaired loans held-for-investment and foreclosed assets to determine fair value. When the appraisals are received, Management reviews the assumptions and methodology utilized in the appraisal, as well as the overall resulting value in conjunction with independent data sources such as recent market data and industry-wide statistics. We generally use a 6% discount for selling costs which is applied to all properties, regardless of size. Generally, the third party appraisals apply the "market approach," which is a valuation technique that uses prices and other relevant information generated by market transactions involving identical or comparable (that is, similar) assets, liabilities, or a group of assets and liabilities, such as a business. Adjustments are then made based on the type of property, age of appraisal, current status of property and other related factors to estimate the current value of collateral. The value of OREO is determined based on independent appraisals, similar to the process used for impaired loans, discussed above, and is generally classified as Level 3.

#### Fair Values of Financial Instruments.

The following methods and assumptions were used by the Company in estimating the fair value disclosures for financial instruments.

#### Cash and Cash Equivalents including Interest Bearing Time Deposits with Financial Institutions.

The carrying amounts reported in the balance sheet for cash and short-term instruments are a reasonable estimate of fair value, which will approximate their historical cost.

#### Securities Available-for-Sale.

Fair values for investment securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

#### Loans Receivable.

For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values and credit risk factors. For fixed rate loans, fair values are based on discounted cash flows, credit risk factors, and liquidity factors.

Other Equity Securities.

These are mostly Federal Reserve Bank stock and Federal Home Loan Bank stock, carried in Other Equity Securities. They are not traded, and not available for sale, and have no fair market value.

Deposit liabilities.

The fair values disclosed for demand deposits (e.g., interest and non-interest checking, savings, and money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amounts). The fair values for fixed-rate certificates of deposit are based on discounted cash flows.

Federal Home Loan Bank Advances.

The fair values of Federal Home Loan Bank Advances are based on discounted cash flows. The discount rate is equal to the market rate currently offered on similar products.

Note payable.

Fair value is equal to the current balance. They represent a corporate loan with a monthly variable rate, based on the 3-month LIBOR rate plus 4%.

Accrued Interest Receivable and Payable

The interest receivable and payable balances approximate their fair value due to the short-term nature of their settlement dates.

Undisbursed loan commitments, lines of credit, Mastercard line and standby letters of credit.

The fair value of these off-balance sheet items are based on discounted cash flows of expected fundings.

The Bank has excluded non-financial assets and non-financial liabilities defined by the Codification (ASC 820-10-15-A), such as Bank premises and equipment, deferred taxes and other liabilities. In addition, the Bank has not disclosed the fair value of financial instruments specifically excluded from disclosure requirements of the Financial Instruments Topic of the Codification (ASC 825-10-50-8), such as Bank-owned life insurance policies.

The following table provides summary information on the estimated fair value of financial instruments at September 30, 2016:

September 30, 2016 (Dollar amounts in thousands)	Carrying amount	Fair value	Fair value measurements		
			Level 1	Level 2	Level 3
<b>Financial assets:</b>					
Cash and cash equivalents	\$ 17,342	\$ 17,342	\$ 17,342	—	—
Interest-bearing time deposits with financial institutions	204	204	—	\$ 204	—
Securities available for sale	358,877	358,877	1,003	357,874	—
Loans	753,013	748,688	—	—	\$ 748,688
Other equity securities	7,206	7,206	—	—	7,206
Accrued interest receivable	4,544	4,544	4,544	—	—
<b>Financial liabilities:</b>					
Deposits	1,003,457	1,002,771	885,864	116,907	—
Federal Home Loan Bank advances	37,000	37,000	—	37,000	—
Note payable	4,500	4,500	—	4,500	—
Accrued interest payable	287	287	287	—	—
<b>Off-balance-sheet liabilities:</b>					
Undisbursed loan commitments, lines of credit, standby letters of credit and Mastercard lines of credit	—	1,702	—	—	1,702

The carrying amount of loans includes \$6,972,000 of nonaccrual loans (loans that are not accruing interest) as of September 30, 2016. The fair value of nonaccrual loans is based on the collateral values that secure the loans or the cash flows expected to be received.

The following table provides summary information on the estimated fair value of financial instruments at December 31, 2015:

December 31, 2015 (Dollar amounts in thousands)	Carrying amount	Fair value	Fair value measurements		
			Level 1	Level 2	Level 3
<b>Financial assets:</b>					
Cash and cash equivalents	\$ 12,314	\$ 12,314	\$ 12,314	—	—
Interest-bearing time deposits with financial institutions	205	205	—	\$ 205	—
Securities available for sale	329,207	329,207	7,000	322,207	—
Loans	733,977	725,196	—	—	\$ 725,196
Other equity securities	6,748	6,748	—	—	6,748
Accrued interest receivable	4,511	4,511	4,511	—	—
<b>Financial liabilities:</b>					
Deposits	983,199	983,771	857,759	125,430	—
Federal Home Loan Bank advances	17,000	17,000	—	17,000	—
Note payable	4,950	4,950	—	4,950	—
Accrued interest payable	236	236	236	—	—
<b>Off-balance-sheet liabilities:</b>					
Undisbursed loan commitments, lines of credit, standby letters of credit and Mastercard lines of credit	—	1,673	—	—	1,673

The carrying amount of loans includes \$7,915,000 of nonaccrual loans (loans that are not accruing interest) as of December 31, 2015. The fair value of nonaccrual loans is based on the collateral values that secure the loans or the cash flows expected to be received.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

### Forward-Looking Information and Uncertainties Regarding Future Financial Performance.

This report, including management's discussion below, concerning earnings and financial condition, contains "forward-looking statements". Forward-looking statements are estimates of or statements about expectations or beliefs regarding the Company's future financial performance or anticipated future financial condition that are based on current information and that are subject to a number of risks and uncertainties that could cause actual operating results in the future to differ significantly from those expected at the current time. Those risks and uncertainties include, although they are not limited to, the following:

**Increased Competition.** Increased competition from other banks and financial service businesses, mutual funds and securities brokerage and investment banking firms that offer competitive loan and investment products and competitive market pricing, which could require us to reduce interest rates and loan fees to attract new loans or to increase interest rates that we offer on time deposits, either or both of which could, in turn, reduce interest income and net interest margins. These factors could reduce our ability to attract new deposits and loans and leases.

**Liquidity Risk.** The stability of funding sources and continued availability of borrowings; our ability to raise capital or incur debt on reasonable terms.

Possible Adverse Changes in Economic Conditions. Adverse changes in national or local economic conditions over an extended period of time could (i) reduce loan demand which could, in turn, reduce interest income and net interest margins; (ii) adversely affect the financial capability of borrowers to meet their loan obligations, which, in turn, could result in increases in loan losses and require increases in provisions for possible loan losses, thereby adversely affecting operating results; and (iii) lead to reductions in real property values that, due to the Company's reliance on real property to secure many of its loans, could make it more difficult to prevent losses from being incurred on non-performing loans through the sale of such real properties.

Possible Adverse Changes in National Economic Conditions and Federal Reserve Board Monetary Policies. Changes in national economic policies and conditions, such as increases in inflation or declines in economic output often prompt changes in Federal Open Market Committee ("FOMC") monetary policies that could reduce interest income or increase the cost of funds to the Company, either of which could result in reduced earnings. In addition, deterioration in economic conditions that could result in increased loan and lease losses.

Changes in Regulatory Policies. Changes in federal and national bank regulatory policies, such as increases in capital requirements or in loan loss reserve or asset/liability ratio requirements, liquidity requirements, and the risks associated with concentration in real estate related loans could adversely affect earnings by reducing yields on earning assets or increasing operating costs.

Due to these and other possible uncertainties and risks, readers are cautioned not to place undue reliance on the forward-looking statements contained in this report, which speak only as of the date of this report, or to make predictions based solely on historical financial performance. The Company also disclaims any obligation to update forward-looking statements contained in this report.

#### Critical Accounting Policies And Estimates

Management's discussion and analysis of its financial condition and results of operations are based upon the Company's financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates, including those related to its loans and allowance for loan losses. The Company bases its estimates on current market conditions, historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. All adjustments that, in the opinion of management, are necessary for a fair presentation for the periods presented have been reflected as required by Regulation S-X, Rule 10-01. The Company believes the following critical accounting policy requires significant judgments and estimates used in the preparation of the consolidated financial statements.

#### Allowance for Loan Losses

The allowance for loan losses is periodically evaluated for adequacy by management.

Factors considered include the Company's loan loss experience, known and inherent risks in the portfolio, current economic conditions, known adverse situations that may affect the borrower's ability to repay, regulatory policies, and the estimated value of underlying collateral. The evaluation of the adequacy of the allowance is based on the above factors along with prevailing and anticipated economic conditions that may impact our borrowers' ability to repay their loans. Determination of the allowance is based upon objective and subjective judgments by management from the information currently available. Adverse changes in information could result in higher than expected charge-offs and loan loss provisions.

#### Goodwill

Goodwill arises when the Company's purchase price exceeds the fair value of the net assets of an acquired business. Goodwill represents the value attributable to intangible elements acquired. The value of goodwill is supported ultimately by profit from the acquired business. A decline in earnings could lead to impairment, which would be recorded as a write-down in the Company's consolidated statements of earnings. Events that may indicate goodwill impairment include significant or adverse changes in results of operations of the acquired business or asset, economic or political climate; an adverse action or assessment by a regulator; unanticipated competition; and a more-likely-than-not expectation that a reporting unit will be sold or disposed of at a loss.

#### Other Than Temporary Impairment

Other than temporary impairment ("OTTI") is triggered if the Company has the intent to sell a security, it is likely that it will be required to sell the security before recovery, or if the Company does not expect to recover the entire amortized cost basis of the security. If the Company intends to sell the security or it is likely it will be required to sell the security before recovering its cost basis, the entire impairment loss would be recognized in earnings as an OTTI. If the Company does not intend to sell the security and it is not likely that the Company will be required to sell the security but the Company does not expect to recover the entire amortized cost basis of the security, only the portion of the impairment loss representing credit losses would be recognized in earnings as an OTTI. The credit loss is measured as the difference between the amortized cost basis and the present value of the cash flows expected to be collected of a security. Projected cash flows are discounted by the original or current effective interest rate depending on the nature of the security being measured for potential OTTI. The remaining impairment loss related to all other factors, the difference between the present value of the cash flows expected to be collected and fair value, would be recognized as a charge to other comprehensive income ("OCI"). Impairment losses related to all other factors are to be presented as a separate category within OCI.

For investment securities held to maturity, this amount is accreted over the remaining life of the debt security prospectively based on the amount and timing of future estimated cash flows. The accretion of the OTTI amount recorded in OCI will increase the carrying value of the investment, and would not affect earnings. If there is an indication of additional credit losses the security is re-evaluated accordingly based on the procedures described above.

#### Provision for and Deferred Income Taxes

The Company is subject to income tax laws of the United States, its states, and the municipalities in which it operates. The Company considers its income tax provision methodology to be critical, as the determination of current and deferred taxes based on complex analyses of many factors including interpretation of federal and state laws, the difference between tax and financial reporting bases of assets and liabilities (temporary differences), estimates of amounts due or owed, the timing of reversals of temporary differences and current financial standards. Actual results could differ significantly from the estimates due to tax law interpretations used in determining the current and deferred income tax liabilities. Additionally, there can be no assurances that estimates and interpretations used in determining income tax liabilities may not be challenged by federal and state tax authorities.

## Recent Accounting Pronouncements

In September 2015, FASB issued ASU 2015-16, *Business Combinations (Topic 805) –Simplifying the Accounting for Measurement-Period Adjustments*. GAAP requires that during the amendment period, the acquirer retrospectively adjust the provisional amounts recognized at the acquisition date with a corresponding adjustment to goodwill. Those adjustments are required when new information is obtained about facts and circumstances that existed as of the acquisition date that, if known, would have affected the measurement of the amounts initially recognized or would have resulted in the recognition of additional assets or liabilities. To simplify the accounting for adjustments made to provisional amounts recognized in a business combination, the amendments in this Update eliminate the requirement to retrospectively account for those adjustments. These amendments in this Update are effective for fiscal years beginning after December 15, 2015. The adoption of this Update did not have a material impact on the Company's consolidated financial statements.

In January 2016 FASB issued ASU 2016-01, *Financial Instruments-overall (subtopic 825-10) Recognition and Measurement of Financial Assets and Financial Liabilities*. Before the global financial crisis that began in 2008, both the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) began a joint project to improve and to achieve convergence of their respective standards on the accounting for financial instruments. The global economic crisis further highlighted the need for improvement in the accounting models for financial instruments in today's complex economic environment. As a result, the main objective in developing this Update is enhancing the reporting model for financial instruments to provide users of financial statements with more decision-useful information. For public business entities, the amendments in this Update address certain aspects of recognition measurement. The amendments in this Update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The adoption of this Update is not expected to have a material impact on the Company's consolidated financial statements.

In February 2016 FASB issued ASU 2016-02, *Leases (Topic 842)*. The FASB is issuing this Update to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The core principle of Topic 842 is that a lessee should recognize the assets and liabilities that arise from leases. All leases create an asset and a liability for the lessee in accordance with FASB Concepts Statement No. 6, Elements of Financial Statements, and, therefore, recognition of those lease assets and lease liabilities represents an improvement over previous GAAP, which did not require lease assets and lease liabilities to be recognized for most leases. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is currently evaluating the impact of this ASU on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU 2016-08, *Revenue from Contracts with Customers (Topic 606); Principal versus agent considerations (reporting revenue gross versus net)*. The core principle of the guidance in Topic 606 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The amendments in this Update do not change the core principle of the guidance. The amendments clarify the implementation guidance on principal versus agent considerations. When another party is involved in providing goods or services to a customer, an entity is required to determine whether the nature of its promise to provide the specified good or service itself (that is, the entity is a principal) or to arrange for that good or service to be provided by the other party (that is, the entity is an agent). When (or as) an entity that is a principal satisfies a performance obligation, the entity recognizes revenue in the gross amount of consideration to which it expects to be entitled in exchange for the specified good or service transferred to the customer. When (or as) an entity that is an agent satisfies a performance obligation, the entity recognizes revenue in the amount of any fee or commission to which it expects to be entitled in exchange for arranging for the specified good or service to be provided by the other party. ASU 2016-08 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company is currently evaluating the impact of this ASU on the Company's consolidated financial statements.

In March 30, 2016 FASB issued ASU 2016-09, *Compensation-Stock Compensation (Topic 718); Improvements to employee share-based payment accounting*. The areas for simplification in this Update involve several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. Some of the specific changes associated with the Update include all excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) being recognized as income tax expense or benefit in the income statement. The tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur. An entity should also recognize excess tax benefits regardless of whether the benefit reduces taxes payable in the current period. An entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest (current GAAP) or account for forfeitures when they occur. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The adoption of this Update is not expected to have a material impact on the Company's consolidated financial statements.

In June, 2016, FASB issued ASU 2016-13, *Financial Instruments-Credit Losses (Topic 326; Measurement of Credit Losses)*. The amendments in this Update require a financial asset (or a group of financial assets) measured at amortized cost to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. The income statement reflects the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company is currently evaluating the impact of this ASU on the Company's consolidated financial statements.

In August, 2016, FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230; Classification of Certain Cash Receipts and Cash Payments)*. This ASU update addresses eight cash flow classification issues related to: debt prepayment or debt extinguishment costs; settlement of zero coupon debt instruments; contingent consideration payments made after a business combination; proceeds from the payment of insurance claims; proceeds from the settlement of corporate owned life insurance policies, including bank owned life insurance policies; distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principal. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017. The adoption of this Update is not expected to have a material impact on the Company's consolidated financial statements.

#### Earnings Analysis

Net interest income for the quarter ended September 30, 2016 was \$10,396,000, compared to \$9,200,000 for the quarter ended September 30, 2015. Net interest income for the nine months ended September 30, 2016 was \$31,634,000 compared to \$26,461,000 for the nine months ended September 30, 2015. The increase was a function of increased loan volume during the two periods.



The following tables present an analysis of net interest income and average earning assets and liabilities for the three-and nine-month periods ended September 30, 2016 compared to the three-and nine-month periods ended September 30, 2015.

TABLE 1  
NET INTEREST INCOME AND AVERAGE BALANCES  
FNB BANCORP AND SUBSIDIARY  
Three months ended September 30,

(Dollar amounts in thousands)	2016			2015		
	Average Balance	Interest	Annualized Average Yield	Average Balance	Interest	Annualized Average Yield
<b>INTEREST EARNING ASSETS</b>						
Loans, gross (1) (2)	\$ 740,218	\$ 9,301	5.00%	\$ 624,123	\$ 8,309	5.28%
Taxable securities	209,758	1,065	2.02%	195,513	924	1.88%
Nontaxable securities (3)	141,879	996	2.79%	111,790	868	3.08%
Interest time deposits in other financial institutions	205	1	1.94%	1,866	9	1.91%
Total interest earning assets	1,092,060	11,363	4.14%	933,292	10,110	4.30%
Cash and due from banks	18,115			55,116		
Premises	10,015			10,455		
Other assets	38,939			41,186		
Total noninterest earning assets	67,069			106,757		
<b>TOTAL ASSETS</b>	<b>\$ 1,159,129</b>			<b>\$ 1,040,049</b>		
Demand, int bearing	\$ 111,679	28	0.10%	\$ 91,708	28	0.12%
Money market	418,517	370	0.35%	400,035	435	0.43%
Savings	85,553	95	0.44%	77,140	34	0.17%
Time deposits	117,672	164	0.55%	110,602	139	0.50%
FHLB advances	9,953	10	0.40%	—	—	n/a
Note payable	4,425	54	4.85%	5,187	57	4.36%
Total interest bearing liabilities	747,799	721	0.38%	684,672	693	0.40%
<b>NONINTEREST BEARING LIABILITIES:</b>						
Demand deposits	281,120			242,130		
Other liabilities	17,762			12,446		
Total noninterest bearing liabilities	298,882			254,576		
<b>TOTAL LIABILITIES</b>	<b>1,046,681</b>			<b>939,248</b>		
Stockholders' equity	112,448			100,801		
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 1,159,129</b>			<b>\$ 1,040,049</b>		
<b>NET INTEREST INCOME AND MARGIN ON TOTAL EARNING ASSETS (4)</b>						
		<u>\$ 10,642</u>	3.88%		<u>\$ 9,417</u>	4.00%

(1) Interest on non-accrual loans is recognized into income on a cash received basis.

(2) Amounts of interest earned include loan fees of \$369,000 and \$400,000 for the quarters ended September 30, 2016 and 2015, respectively.

(3) Tax equivalent adjustments recorded at the statutory rate of 34% that are included in the nontaxable securities portfolio are \$246,000 and \$217,000 for the quarters ended September 30, 2016 and 2015, respectively, and were derived from nontaxable municipal interest income.

(4) The annualized net interest margin is computed by dividing net interest income by total average interest earning assets and multiplied by an annualization factor.

TABLE 2

NET INTEREST INCOME AND AVERAGE BALANCES  
FNB BANCORP AND SUBSIDIARY  
Nine months ended September 30,

(Dollar amounts in thousands)	2016			2015		
	Average Balance	Interest	Annualized Average Yield	Average Balance	Interest	Annualized Average Yield
<b>INTEREST EARNING ASSETS</b>						
Loans, gross (1) (2)	\$ 741,180	\$ 28,735	5.18%	\$ 601,098	\$ 23,874	5.31%
Taxable securities	205,935	3,044	1.97%	184,492	2,597	1.88%
Nontaxable securities (3)	134,129	2,909	2.90%	97,019	2,339	3.22%
Interest time deposits in other financial institutions	205	3	1.96%	2,377	36	2.02%
Tot interest earning assets	<u>1,081,448</u>	<u>34,691</u>	4.28%	<u>884,986</u>	<u>28,846</u>	4.36%
Cash and due from banks	23,222			36,536		
Premises	10,150			10,646		
Other assets	39,069			39,126		
Tot noninterest earning assets	<u>72,441</u>			<u>86,308</u>		
<b>TOTAL ASSETS</b>	<b><u>\$ 1,153,889</u></b>			<b><u>\$ 971,294</u></b>		
Demand, int bearing	\$ 112,793	96	0.11%	\$ 93,018	75	0.11%
Money market	429,273	1,356	0.42%	349,566	1,070	0.41%
Savings	83,089	137	0.22%	74,481	72	0.13%
Time deposits	121,796	560	0.61%	106,965	408	0.51%
FHLB advances	5,927	19	0.43%	330	2	0.81%
Note payable	4,725	167	4.72%	5,337	173	4.33%
Tot interest bearing liabilities	<u>757,602</u>	<u>2,335</u>	0.41%	<u>629,697</u>	<u>1,800</u>	0.38%
Demand deposits	270,221			229,723		
Other liabilities	16,855			12,318		
Tot noninterest bearing liabilities	<u>287,076</u>			<u>242,041</u>		
<b>TOTAL LIABILITIES</b>	<b>1,044,678</b>			<b>871,738</b>		
Stockholders' equity	109,211			99,556		
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b><u>\$ 1,153,889</u></b>			<b><u>\$ 971,294</u></b>		
<b>NET INTEREST INCOME AND MARGIN ON TOTAL EARNING ASSETS (4)</b>						
		<u>\$ 32,356</u>	4.00%		<u>\$ 27,046</u>	4.09%

(1) Interest on non-accrual loans is recognized into income on a cash received basis.

(2) Amounts of interest earned included loan fees of \$1,382,000 and \$1,081,000 for the nine months ended September 30, 2016 and 2015, respectively.

(3) Tax equivalent adjustments recorded at the statutory rate of 34% that are included in the nontaxable securities portfolio are \$722,000 and \$585,000 for the nine months ended September 30, 2016 and 2015, respectively. Tax equivalent adjustments included in the nontaxable securities portfolio were derived from nontaxable municipal interest income.

(4) The annualized net interest margin is computed by dividing net interest income by total average interest earning assets and multiplied by an annualization factor.

The various components that contributed to changes in net interest income for the three and nine months ended September 30, 2016 and 2015 are shown in Tables 1 and 2, above. The principal interest earning assets are loans, from a volume as well as from a rate or yield perspective. For the quarter ended September 30, 2016, average loans outstanding represented 68% of average earning assets. For the quarter ended September 30, 2015, they represented 67% of average earning assets. For the nine months ended September 30, 2016 and 2015, average loans outstanding represented 69% and 68%, respectively, of average earning assets.

The taxable equivalent yield on average interest earning assets for the quarter ended September 30, 2016 compared to the quarter ended September 30, 2015 decreased from 4.30% to 4.14% or 16 basis points. Average loans increased by \$116,095,000, quarter over quarter, while their yield increased from 5.28% to 5.00% or 28 basis points. Interest income on total interest earning assets for the quarter increased \$1,253,000 or 12% on a fully-taxable equivalent basis.

New customer deposits have been primarily in DDA, NOW and Money Market accounts during the first nine months of 2016 and 2015. The low rates being offered on term deposits coupled with the possible increase in short term rates by the FOMC are, in part, the underlying reason for this migration.

For the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015, interest income on interest earning assets increased \$5,845,000 on a fully-taxable equivalent basis, while average earning assets increased \$196,462,000, or 22%. Average loans increased by \$140,082,000, or 23%. Interest on loans increased \$4,861,000 or 20%, while the yield decreased 13 basis points. The cost on total interest bearing liabilities increased from 0.38% to 0.41%. Time deposit averages decreased \$14,831,000 and their yield increased 10 basis points. Money Market deposit average balances increased \$79,707,000, or 23%, and their cost increased \$286,000.

For the three and nine month periods ended September 30, 2016 and September 30, 2015, respectively, the following tables show the dollar amount of change in interest income and expense and the dollar amounts attributable to: (a) changes in volume (changes in volume at the current year rate), and b) changes in rate (changes in rate times the prior year's volume). In this table, the dollar change in rate/volume is prorated to volume and rate proportionately.

Table 3

FNB BANCORP AND SUBSIDIARY  
RATE/VOLUME VARIANCE ANALYSIS

(Dollar amounts in thousands)

	Three Months Ended September 30, 2016 Compared to 2015		
	Interest Income/Expense	Variance Attributable to Rate      Volume	
<b>INTEREST EARNING ASSETS</b>			
Loans	\$ 992	\$ (466)	\$ 1,458
Taxable securities	141	69	72
Nontaxable securities (1)	128	(83)	211
Interest on time deposits with other financial institutions	(8)	—	(8)
Total	<u>\$ 1,253</u>	<u>\$ (480)</u>	<u>\$ 1,733</u>
<b>INTEREST BEARING LIABILITIES</b>			
Demand deposits	\$ —	\$ —	\$ —
Money market	65	85	(20)
Savings deposits	(61)	(52)	(9)
Time deposits	(25)	(16)	(9)
FHLB advances	(10)	—	(10)
Note payable	3	(6)	9
Total	<u>\$ (28)</u>	<u>\$ 11</u>	<u>\$ (39)</u>
<b>NET INTEREST INCOME</b>	<u>\$ 1,225</u>	<u>\$ (469)</u>	<u>\$ 1,694</u>

(1) Includes tax equivalent adjustment of \$246,000 and \$217,000 in the three months ended September 30, 2016 and September 30, 2015, respectively.

Table 4

FNB BANCORP AND SUBSIDIARY  
RATE/VOLUME VARIANCE ANALYSIS

(Dollar amounts in thousands)

	Nine Months Ended September 30, 2016 Compared to 2015		
	Interest Income/Expense	Variance Attributable to Rate      Volume	
<b>INTEREST EARNING ASSETS</b>			
Loans	\$ 4,861	\$ (730)	\$ 5,591
Taxable securities	447	143	304
Nontaxable securities (1)	570	(237)	807
Interest on time deposits with other financial institutions	(33)	—	(33)
Total	<u>\$ 5,845</u>	<u>\$ (824)</u>	<u>\$ 6,669</u>
<b>INTEREST BEARING LIABILITIES</b>			
Demand deposits	\$ (21)	\$ (5)	\$ (16)
Money market	(284)	(39)	(245)
Savings deposits	(65)	(51)	(14)
Time deposits	(152)	(95)	(57)
FHLB advances	(17)	—	(17)
Note payable	4	(18)	22
Total	<u>\$ (535)</u>	<u>\$ (208)</u>	<u>\$ (327)</u>
<b>NET INTEREST INCOME</b>	<u>\$ 5,310</u>	<u>\$ (1,032)</u>	<u>\$ 6,342</u>

(1) Includes tax equivalent adjustment of \$722,000 and \$585,000 in the nine months ended September 30, 2016 and September 30, 2015, respectively

Noninterest income

The following table shows the principal components of noninterest income for the periods indicated.

Table 5

	NONINTEREST INCOME			
	Three months ended September 30,		Variance	
(Dollar amounts in thousands)	2016	2015	Amount	Percent
Service charges	\$ 623	\$ 618	\$ 5	0.8%
Net gain on sale of available-for-sale securities	140	29	111	382.8%
Bank owned life insurance earnings	94	90	4	4.4%
Other income	250	287	(37)	-12.9%
Total noninterest income	<u>\$ 1,107</u>	<u>\$ 1,024</u>	<u>\$ 83</u>	<u>8.1%</u>

(Dollar amounts in thousands)	Nine months ended September 30,		Variance	
	2016	2015	Amount	Percent
Service charges	\$ 1,862	\$ 1,854	\$ 8	0.4%
Net gain on sale of available-for-sale securities	381	250	131	52.4%
Bank-owned life insurance policy earnings	299	261	38	14.6%
Other income	764	1,002	(238)	-23.8%
Total noninterest income	\$ 3,306	\$ 3,367	\$ (61)	-1.8%

Noninterest income consists mainly of service charges on deposits and earnings on bank owned life insurance policy earnings. During the third quarter of 2016, the Bank sold or had called \$14,038,000 of investment securities for a pre-tax gain of \$140,000. During the same period in 2015, the Bank sold or had called \$3,187,000 of investment securities for a pre-tax gain of \$29,000. During the nine months of 2016, the Bank sold \$35,400,000 in investment securities for a pre-tax gain of \$381,000. During the nine months of 2015, the Bank sold \$11,463,000 in investment securities for a pre-tax gain of \$250,000.

#### Noninterest expense

The following table shows the principal components of noninterest expense for the periods indicated.

**Table 6**

(Dollar amounts in thousands)	NONINTEREST EXPENSE		Variance	
	Three months ended September 30,		Amount	Percent
	2016	2015		
Salaries and employee benefits	\$ 4,821	\$ 4,100	\$ 721	17.6%
Occupancy expense	645	592	53	9.0%
Equipment expense	445	718	(273)	-38.0%
Professional fees	298	334	(36)	-10.8%
FDIC assessment	150	150	0	0.0%
Telephone, postage and supplies	300	237	63	26.6%
Advertising	104	112	(8)	-7.1%
Data processing expense	147	659	(512)	-77.7%
Low income housing expenses	71	70	1	1.4%
Surety insurance	88	122	(34)	-27.9%
Directors expense	72	72	0	0.0%
Other expense	372	313	59	18.8%
Total noninterest expense	\$ 7,513	\$ 7,479	\$ 34	0.5%

(Dollars in thousands)	Nine months ended September 30,		Variance	
	2016	2015	Amount	Percent
Salaries and employee benefits	\$ 14,635	\$ 12,513	\$ 2,122	17.0%
Occupancy expense	1,893	1,906	(13)	-0.7%
Equipment expense	1,317	1,533	(216)	-14.1%
Professional fees	979	1,075	(96)	-8.9%
FDIC assessment	450	450	0	0.0%
Telephone, postage and and supplies	901	782	119	15.2%
Advertising	404	381	23	6.0%
Data processing expense	479	940	(461)	-49.0%
Low income housing expenses	213	212	1	0.5%
Surety insurance	262	298	(36)	-12.1%
Directors expense	216	216	0	0.0%
Other real estate owned expense (income) net	(10)	(6)	(4)	66.7%
Other expense	1,210	911	299	32.8%
Total noninterest expense	<u>\$ 22,949</u>	<u>\$ 21,211</u>	<u>\$ 1,738</u>	8.2%

Noninterest expense consists mainly of salaries and employee benefits. For the three months ended September 30, 2016 compared to three months ended September 30, 2015, it represented 64% and 55% of total noninterest expenses. For 2015, the ACB employee separation costs are included in the year to date figure. For the nine months ended September 30, 2016 and 2015, it was 64% and 59%, respectively, of total noninterest expenses. The third quarter of 2015 included acquisition expenses of \$1,045,000 related to the acquisition of America California Bank in September 2015. Acquisition costs include system and estimated system costs, lease termination costs, and other post acquisition related expenses.

#### Provision for Loan Losses

There was a provision for loan losses of \$0 and \$150,000 for the three and nine months ended September 30, 2016, respectively, and a provision of \$75,000 and \$225,000 for the three and nine months of 2015.

The allowance for loan losses was \$10,092,000 or 1.34% of total gross loans at September 30, 2016, compared to \$9,940,000 or 1.41% of total gross loans at September 30, 2015. The allowance for loan losses is maintained at a level that management considered adequate to provide for probable loan losses inherent in the loan portfolio as of September 30, 2016.

#### Income Taxes

The effective tax rate for the quarter ended September 30, 2016 was 38.7% compared to a 16.1% effective tax rate benefit for the quarter ended September 30, 2015. The effective tax rate for the nine months ended September 30, 2016 and September 30, 2015, was an effective tax rate of 37.0% and 27.2%, respectively. Tax preference items which have a significant effect on our effective tax rate include changing amounts invested in tax-advantaged securities, available Low Income Housing Credits, and amounts of interest income on tax advantaged municipal debt securities. During the third quarter of 2015, the Company recorded a tax benefit of \$535,000 related to the settlement with the Franchise Tax Board regarding outstanding Enterprise zone net Interest Deductions claimed between 2005 and 2013.

## Asset and Liability Management

Ongoing management of the Company's interest rate sensitivity limits interest rate risk through monitoring the mix and maturity of loans, investments and deposits. Management regularly reviews the Company's position and evaluates alternative sources and uses of funds as well as changes in external factors. Various methods are used to achieve and maintain the desired interest rate sensitivity position including the sale or purchase of assets and product pricing.

In order to ensure that sufficient funds are available for loan growth and deposit withdrawals, as well as to provide for general needs, the Company must maintain an adequate level of liquidity. Asset liquidity comes from the Company's ability to convert short-term investments into cash and from the maturity and repayment of loans and investment securities. Liability liquidity comes from the Company's customer base, which provides core deposit growth. The overall liquidity position of the Company is closely monitored and evaluated regularly. Management believes the Company's liquidity sources at September 30, 2016, are adequate to meet its operating needs in 2016 and our liquidity positions are sufficient to meet our liquidity needs in the near term.

## Financial Condition

Assets. Total assets increased to \$1,177,548,000 at September 30, 2016 from \$1,124,349,000 at December 31, 2015. The increases were primarily \$29,670,000 in securities-available-for-sale and \$18,660,000 in net loans.

Loans. The Bank was able to grow the loan portfolio during the nine months ended September 30, 2016. The loan portfolio breakdown as of September 30, 2016 and December 31, 2015 was as follows:

	<b>LOAN PORTFOLIO</b>			
	September 30 2016	Percent	December 31 2015	Percent
(Dollar amounts in thousands)				
Commercial real estate	\$ 404,964	54%	\$ 399,993	54%
Real estate construction	38,163	5%	44,816	7%
Real estate multi family	83,944	11%	63,597	9%
Real estate-1 to 4 family	173,441	23%	171,964	22%
Commercial & industrial	50,871	7%	52,033	9%
Consumer loans	1,630	—	1,574	—
Gross loans	753,013	100%	733,977	100%
Net deferred loan fees	(1,514)	—	(1,260)	—
Total	\$ 751,499	100%	\$ 732,717	100%



Allowance for loan losses. Management of the Company is responsible for assessing the overall risks within the Bank's loan portfolio, assessing the specific loss expectancy, and determining the adequacy of the allowance for loan losses. The level of the allowance is determined by internally generating credit quality ratings, reviewing economic conditions in the Company's market area, and considering the Company's historical loan loss experience. The Company's management considers changes in national and local economic conditions, as well as the condition of various market segments. It also reviews any changes in the nature and volume of the portfolio. Management monitors for the existence and effect of any concentrations of credit, and changes in the level of such concentrations. It also reviews the effect of external factors, such as competition and legal and regulatory requirements. Finally, the Company is committed to maintaining an adequate allowance, identifying credit weaknesses by consistent review of loans, and maintaining the ratings and changing those ratings in a timely manner as circumstances change.

A summary of activity in the allowance for loan losses for the nine months ended September 30, 2016 and September 30, 2015, respectively, is as follows:

(Dollar amounts in thousands)	ALLOWANCE FOR LOAN LOSSES	
	Nine months ended September 30,	
	2016	2015
Balance, beginning of period	\$ 9,970	\$ 9,700
Provision for loan losses	150	225
Recoveries	167	94
Amounts charged off	(195)	(79)
Balance, end of period	\$ 10,092	\$ 9,940

During the nine months ended September 30, 2016, there was a provision for loan losses of \$150,000, compared to \$225,000 for the same period in 2015.

In management's judgment, the allowance was adequate to absorb losses currently inherent in the loan portfolio at September 30, 2016. However, changes in prevailing economic conditions in the Company's markets or in the financial condition of its customers could result in changes in the level of nonperforming assets and charge-offs in the future and, accordingly, changes in the allowance.

The allowance is affected by a number of factors, and does not necessarily move in tandem with the level of gross loans outstanding. Management continues to monitor the factors that affect the allowance, and is prepared to make adjustments as they become necessary.

Nonperforming assets. Nonperforming assets consist of nonaccrual loans, loans that are 90 days or more past due but are still accruing interest and other real estate owned. At September 30, 2016, there was \$8,249,000 in nonperforming assets, compared to \$8,941,000 at December 31, 2015. Nonaccrual loans were \$6,903,000 at September 30, 2016, compared to \$7,915,000 at December 31, 2015. There were no loans past due 90 days and still accruing at either date.

Management intends to aggressively market our Other Real Estate Owned. While management believes the property will sell, there can be no assurance that the property will sell quickly given the current real estate market, nor can the expected sales price be accurately predicted.

Deposits. Total deposits at September 30, 2016, were \$1,003,457,000 compared to \$983,189,000 on December 31, 2015. Of these totals, noninterest-bearing demand deposits were \$285,767,000 or 28.5% of the total on September 30, 2016, and \$263,822,000 or 26.8% on December 31, 2015. Time deposits were \$116,496,000 on September 30, 2016, and \$125,430,000 on December 31, 2015.

The following table sets forth the maturity schedule of the time certificates of deposit on September 30, 2016:

**TABLE 9**

(Dollar amounts in thousands)

<u>Maturities</u>	Under \$250,000	\$250,000 or more	Total
Three months or less	\$ 16,021	\$ 24,531	\$ 40,552
Over three through six months	15,020	8,920	23,940
Over six through twelve months	18,782	10,997	29,779
Over twelve months	20,140	2,085	22,225
Total	<u>\$ 69,963</u>	<u>\$ 46,533</u>	<u>\$ 116,496</u>

Regulatory Capital. The following table shows the risk-based capital ratios and leverage ratios at September 30, 2016 and December 31, 2015 for the Bank:

**TABLE 10**

<u>Regulatory Capital Ratios</u>	September 30, 2016	December 31, 2015	Minimum "Well Capitalized" Requirement
Total Risk-Based Capital Ratio	13.06%	13.35%	≥ 10.00%
Tier 1 Risk-Based Capital Ratio	11.92%	12.14%	≥ 8.00%
Tier 1 Leverage Capital Ratio	9.36%	9.08%	≥ 5.00%
Common Equity Tier 1 Capital Ratio	11.92%	12.14%	≥ 6.50%

Liquidity. Liquidity is a measure of the Company's ability to convert assets into cash with minimal loss. As of September 30, 2016, liquid assets were \$376,423,000, or 32.0% of total assets. As of December 31, 2015, liquid assets were \$341,726,000, or 30.4% of total assets. Liquidity consists of cash and due from banks, federal funds sold, and securities available-for-sale. The Company's primary uses of funds are loans, and the primary sources of funds are deposits. The Company also has federal funds borrowing facilities totaling \$30,000,000, a Federal Home Loan Bank line up to 30% of total eligible assets, and a Federal Reserve Bank borrowing facility.

The relationship between total net loans and total deposits is a useful additional measure of liquidity. A higher loan to deposit ratio may lead to a loss of liquid assets in the future. This must be balanced against the fact that loans represent the highest interest earning assets. A lower loan to deposit ratio means lower potential income. For additional information see the Consolidated statements of Cash Flows in Item 1 of this Form 10-Q.

TABLE 11

(Dollar amounts in thousands)	Payments Due by Period				
	Total	1 year or less	Over 1 to 3 years	Over 3 to 5 years	Over 5 years
Contractual Obligations					
Operating Leases	\$ 3,437	\$ 1,141	\$ 1,146	\$ 247	\$ 903
Salary Continuation Agreements	6,259	233	1,416	1,536	3,074
Total Contractual Cash Obligations	\$ 5,086	\$ 1,374	\$ 2,562	\$ 247	\$ 903

(Dollar amounts in thousands)	Amount of Commitment Expirations Per Period				
	Total Amounts Committed	1 year or less	Over 1 to 3 years	Over 3 to 5 years	Over 5 years
Other Commercial Commitments					
Lines of Credit	\$ 91,102	\$ 53,438	\$ 14,026	\$ 20,222	\$ 3,416
Standby Letters of Credit	6,271	6,271	—	—	—

The Company has certain ongoing commitments under operating leases. These commitments do not significantly impact operating results. As of September 30, 2016 and December 31, 2015, commitments to extend credit and letters of credit were the only financial instruments with off-balance sheet risk. The Company has not entered into any contracts for financial derivative instruments such as futures, swaps, options or similar instruments. Loan commitments and letters of credit were \$175,701,000 and \$167,254,000 at September 30, 2016 and December 31, 2015, respectively. As a percentage of net loans, these off-balance sheet items represent 23.7% and 23.1% respectively. The Company does not expect all commitments to be funded.

### Item 3. Quantitative and Qualitative Disclosures about Market Risk.

Market risk is the risk of loss to future earnings, to fair values of assets or to future cash flows that may result from changes in the price or value of a financial instrument. The value of a financial instrument may change as a result of changes in interest rates and other market conditions. Market risk is attributed to all market risk sensitive financial instruments, including loans, investment securities, deposits and borrowings. The Company does not engage in trading activities or participate in foreign currency transactions for its own account. Accordingly, exposure to market risk is primarily a function of asset and liability management activities and of changes in market rates of interest.

Changes in rates can cause or require increases in the rates paid on deposits that may take effect more rapidly or may be greater than the increases in the interest rates that the Company is able to charge on loans and the yields that it can realize on its investments. The extent of that market risk depends on a number of variables including the sensitivity to changes in market interest rates and the maturities of the Company's interest earning assets and deposits.

#### **Item 4. Controls and Procedures.**

- (a) *Disclosure Controls and Procedures.* The Company conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) or 15d-15(e) under the Exchange Act of 1934 (the “Act”) as of the end of the Company’s fiscal quarter ended September 30, 2016. This evaluation was carried out under the supervision and with the participation of the Company’s Chief Executive Officer (principal executive officer) Chief Financial Officer (principal financial and accounting officer) and other members of the Company’s senior management. The Company’s Chief Executive Officer (principal executive officer) and Chief Financial Officer (principal financial and accounting officer) concluded that the Company’s disclosure controls and procedures are effective in ensuring that material information required to be disclosed by the Company in the reports it files and submits under the Exchange Act is recorded, processed, summarized and reported as and when required and that such information is communicated to the Company’s management, including the principal executive officer and the principal financial officer, to allow timely decisions required disclosures. The evaluation did not identify any change in the Company’s internal control over financial reporting that occurred during the quarter ended September 30, 2016 that has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.

Management of FNB Bancorp (the “Company”) is responsible for establishing and maintaining adequate internal control over financial reporting, and for reporting an assessment of the effectiveness of the internal control over financial reporting as of September 30, 2016. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparations of financial statements for external purposes in accordance with generally accepted accounting principles. The Company’s system of internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transaction and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of Management and Directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company’s assets that could have a material effect on the financial statements.

### **PART II—OTHER INFORMATION**

#### **Item 1. Legal Proceedings**

There are no material legal proceedings adverse to the Company or First National Bank to which any director, officer, affiliate of the Company, or 5% stockholder of the Company, or any associate of any such director, officer, affiliate or 5% stockholder of the Company are a party, and none of the foregoing persons has a material interest adverse to the Company or First National Bank. From time to time, the Company and/or First National Bank are a party to claims and legal proceedings arising in the ordinary course of business. The Company’s management is not aware of any material pending legal proceedings to which either it or First National Bank may be a party or has recently been a party, which will have a material adverse effect on the financial condition or results of operations of the Company and First National Bank, taken as a whole.

**Item 1A. Risk Factors**

During the course of normal operations, the Bank and the Company manage a variety of risks including, but not limited to, credit risk, operational risk, interest rate risk and regulatory compliance risk. For a more complete discussion of the risk factors facing the Bank and the Company, please refer to the section entitled “Item 1A – Risk Factors” in the Company’s December 31, 2015 Form 10-K.

On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Act”) was signed into law. The purpose of this legislation was to bring about regulatory changes and oversight that would help stop past abuses from recurring in the future. This legislation gives new powers to the FDIC and the Federal Reserve Bank that they may use in the execution of their duties as regulators and overseers of the banking industry. It also created a new federal consumer protection agency named the Consumer Financial Protection Bureau (“CFPB”).

All existing consumer laws and regulations were transferred to the CFPB. This Act is expected to enable regulators to issue numerous new banking regulations and requirements that have not yet been fully developed or promulgated. The ultimate effect the Act has on the Company’s operations will ultimately be determined by the significance of the new banking regulations that are issued as a result of the Act.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

None.

**Item 3. Default upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

Not Applicable.

**Item 5. Other Information**

None.

**Item 6. Exhibits**

**Exhibits**

31: Rule 13a-14(a)/15d-14(a) Certifications

32: Section 1350 Certifications

**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 hereunto duly authorized.

**FNB BANCORP**  
(Registrant)

Dated:

November 7, 2016.

By: /s/ Thomas C. McGraw

Thomas C. McGraw  
Chief Executive Officer  
(Authorized Officer)  
(Principal Executive Officer)

By: /s/ David A. Curtis

David A. Curtis  
Senior Vice President  
Chief Financial Officer  
(Principal Financial and Accounting Officer)

**Rule 13a-14(a)/15d-14(a) Certifications**

I, Thomas C. McGraw, certify that:

1. I have reviewed this quarterly report on Form 10-Q of FNB Bancorp;
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 we 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 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:
  - 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 7, 2016.

/s/ Thomas C. McGraw  
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Thomas C. McGraw  
Chief Executive Officer

**Rule 13a-14(a)/15d-14(a) Certifications**

I, David A. Curtis, certify that:

1. I have reviewed this quarterly report on Form 10-Q of FNB Bancorp;
2. Based on my knowledge, this quarterly 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-15e)) 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 instruments 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 registrant's board of directors:
  - 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 7, 2016.

/s/ David A. Curtis

David A Curtis,  
Senior Vice President and  
Chief Financial Officer



**Section 1350 Certifications**

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), each of the undersigned officers of FNB Bancorp, a California corporation (the "Company"), does hereby certify that:

1. The Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2016 (the "Form 10-Q") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. Information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: November 7, 2016.

/s/ Thomas C. McGraw

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Thomas C. McGraw  
Chief Executive Officer

Dated: November 7, 2016.

/s/ David A. Curtis

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David A. Curtis  
Senior Vice President and Chief Financial Officer

A signed original of this statement required by Section 906 has been provided to FNB Bancorp and will be retained by FNB Bancorp and furnished to the Securities and Exchange Commission or its staff upon request.