2004 Annual Report

SANTA CRUZ COUNTY BANK

Put your money where your life is.

Put your money where your life is.

OUR MISSION *is to become the commercial bank of choice for individuals residing in Santa Cruz County and for local owner-operated businesses, by consistently providing our clients with experienced and committed bankers and state-of-the-art financial products.*

SANTA CRUZ COUNTY BANK is a locally owned and operated commercial bank, serving the needs of the residents and owner-operated businesses of Santa Cruz County. We believe strongly in the importance of local decision making and responsive customer service. We offer a complete line of short and intermediate term loan products, including commercial term loans and lines of credit, Small Business Administration guaranteed term loans, construction loans, mini-perm commercial real estate loans and home equity lines of credit. All our deposit products are augmented by state-of-the-art services, both personal and electronic, including online banking, bill payment, cash management, and merchant services.

Santa Cruz County Bank operates three banking offices located in Santa Cruz, Scotts Valley, and Watsonville.

Santa Cruz County Bank is the only locally owned commercial bank in Santa Cruz County.

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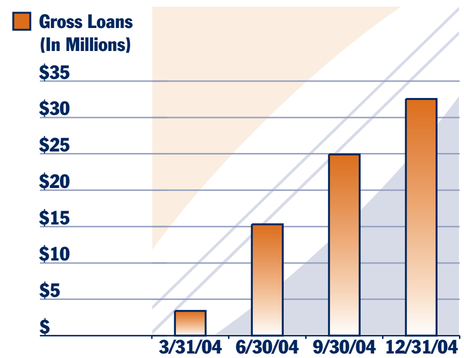

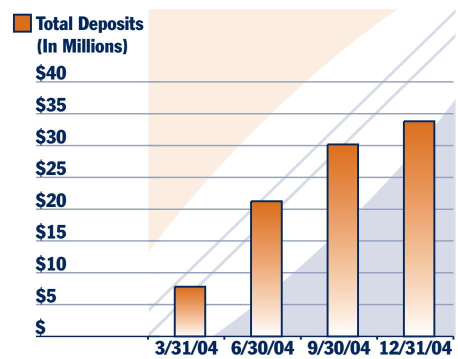

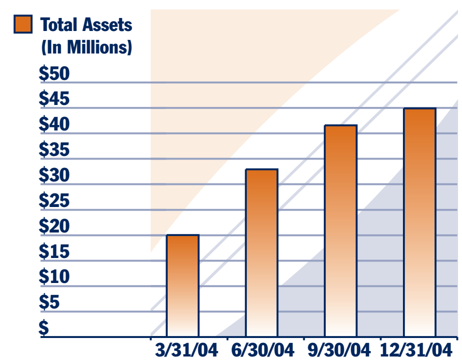

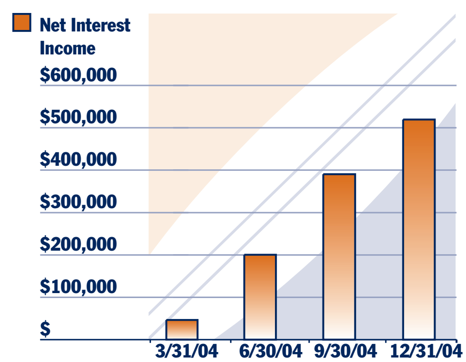

SANTA CRUZ COUNTY BANK

Put your money where your life is.

TO OUR SHAREHOLDERS, EMPLOYEES, CLIENTS, AND FRIENDS,

On February 3, 2004, Santa Cruz County once again had its own County Bank. That day marked the culmination of two years of effort by a determined band of organizers, which identified the need and defined the opportunity for a locally owned Bank, which made the pilgrimage to the regulatory headwaters (San Francisco) and waded through the red tape of the application, which assembled the executive team and shareholder group, uniting all behind a common commitment to lend both money and personal effort to the building of the Bank. So, that day marked the successful conclusion of Phase One. It also marked the beginning of Phase Two, our collective first day on the job – groundbreaking for a construction project that could take up to 10 years to complete. The goal of Phase Two is to build a mature Bank, one that is reliable, accessible, responsive, and profitable, one that serves all of Santa Cruz County.

Over our first eleven months in business, we made a good start. The Bank opened its doors with $13.2 million of capital, sixteen banking professionals, and a solid platform of banking products and systems. These included internet banking and bill pay, business courier services, 24 hour telephone banking, ATM and debit cards, night depository service, and a full line of commercial lending services. We had only one location and we compensated for this limitation by offering clients the flexibility of banking with a click, a swipe, a dial, or a smile.

At the beginning of the second quarter, we qualified our stock for listing on the Over the Counter (OTC) Bulletin Board under the symbol **SCZC**.

During the third and fourth quarters, we launched our merchant credit card services program, and lined up secondary sources of liquidity, both with federal funds lines at two correspondent banks and by securing membership in the Federal Home Loan Bank, which authorized us for secured borrowings. We also expanded our electronic interface with our business clients, launching our ***My County Cash Management*** product.

In November, we opened our Scotts Valley Banking office at 4604 Scotts Valley Drive, headed by longtime Scotts Valley veteran, Chuck Maffia.

In January 2005, we rolled out a credit card product for consumers and businesses. The consumer card allows the option of having either a MasterCard or a Visa card and both cards include Travel Reward Options.

In February 2005, the U.S. Small Business Administration in the San Francisco region awarded Santa Cruz County Bank ***Preferred Lender*** (PLP) status. As a Preferred Lender, Santa Cruz County Bank is now permitted to make decisions to grant SBA guaranteed loans unilaterally, without prior review by SBA. The PLP designation is a much coveted vote of confidence from the Small Business Administration that often takes some years to achieve. It reflects the experience and commitment of our lending staff and it will enhance our competitive positioning by allowing us to respond more quickly to client loan applications.

Also in February of 2005, we opened our Watsonville banking office, located at 595 Auto Center Drive, at the intersection of Auto Center Drive and Main Street, in Watsonville. This office represents the fulfillment of our original commitment to create anchor geographic locations at either end of our County. Two days later, on February 3, 2005 we celebrated the first anniversary of the Bank's opening.

Let us now summarize the Bank's financial performance, through 12/31/04 (reflecting just under eleven months of operations). Our most basic raw material, and the first measure of our success, is the quality and volume of our deposits. During our first eleven months of operations we made a good start at building a stable and diversified base of deposits. Deposit growth during the course of the year was as follows:

	Q-1	Q-2	Q-3	Q-4
Total Deposits	$7,827,279	$21,255,635	$30,185,754	$33,795,455

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Because our deposits are garnered with service, more so than with rate of interest, our total cost of funds for the year was a favorable 0.71% of average total deposits. This average was aided by a healthy mix of non-interest bearing deposits, which at year end totaled 25% of total deposits. At year-end, 51% of our deposit base came from consumer deposits and 49% came from commercial sources, evidencing its diversity and stability.

Loan growth mirrored deposit growth throughout the year:

	Q-1	Q-2	Q-3	Q-4
Total Gross Loans	$3,405,116	$15,325,872	$24,929,125	$32,542,668

At year-end, approximately 32% of the loan portfolio was concentrated in local market construction loans, with the balance in commercial loans to local business, usually secured by real estate. Because the Bank was able to position itself with a high loan-to-deposit ratio, we enjoyed excellent margins. Our net interest margin (interest income less interest expense, divided by average earning assets) of 5.51% for our first eleven months in business compares well, even when compared with more mature banks. As a result of these favorable margins and the Bank's steadily growing volume of loans, net interest income grew substantially by quarter (see chart on inside cover). Overhead levels (Total Non Interest Expense) ramped up in the fourth quarter from stabilized second and third quarter levels, as the Bank made ready for the Scotts Valley and, to a lesser extent, the Watsonville opening:

	Q-1	Q-2	Q-3	Q-4
Non-interest Expense	$398,151	$638,527	$659,388	$814,791

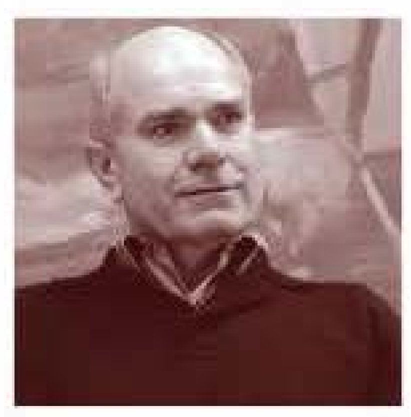
Despite the ramp-up of expenses in the fourth quarter, net losses declined throughout the last three quarters of the year. These results represented consistently favorable variances to plan throughout the year:

	Q-1	Q-2	Q-3	Q-4
Net Losses	($384,442)	($524,124)	($360,797)	($317,132)

As we enter our second year, we remain committed to building on our Scotts Valley, Santa Cruz, and Watsonville foundation, so that we may better serve the entire County. However, our primary focus for now will be on growing and stabilizing our three start-up locations, and establishing a favorable pattern of narrowing monthly losses. We appreciate all of the help and encouragement you have afforded us over the past year. Please keep the referrals coming!

George Gallucci
Chairman of the Board

John E. Rossell
President & CEO



David V. Heald
Executive Vice President & Chief Credit Officer

vtd

Vavrinek, Trine, Day & Co., LLP
Certified Public Accountants & Consultants

INDEPENDENT AUDITORS' REPORT

The Board of Directors
Santa Cruz County Bank

We have audited the statement of condition of Santa Cruz County Bank as of December 31, 2004, and the related statements of operations, changes in stockholders' equity and other comprehensive income, and cash flows for the period from February 3, 2004 (inception) through December 31, 2004. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Santa Cruz County Bank as of December 31, 2004 and the results of its operations and cash flows for the period from February 3, 2004 (inception) through December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

Vavrinek Trine Day & Co. LLP

San Jose, California
January 14, 2005

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STATEMENT OF CONDITION
December 31, 2004

Assets		
Cash and due from banks (notes 1, 11 and 13)	$	870,521
Federal funds sold		1,769,696
Total cash and cash equivalents		2,640,217
Investment securities (notes 2 and 13):		
Securities held-to-maturity		1,813,111
Securities available-for-sale, at fair value		3,704,428
Total investment securities		5,517,539
Federal Home Loan Bank stock, at cost		127,200
Loans (notes 1, 3, 11 and 13):		
Gross loans		32,542,668
Less deferred loan fees, net of costs		(184,547)
Less reserve for loan losses		(407,000)
Net loans		31,951,121
Premises and equipment, net (notes 1, 4 and 11)		1,146,322
Accrued interest receivable		126,848
Bank owned life insurance		3,090,378
Other assets		293,616
Total Assets	$	44,893,241
Liabilities and Shareholders' Equity		
Liabilities:		
Deposits (note 13):		
Noninterest-bearing demand deposits	$	8,474,162
Interest-bearing demand deposits		4,100,305
Savings and money market deposits		14,962,132
Time deposits (note 6)		6,258,856
Total deposits		33,795,455
Other liabilities		
Accrued interest payable		39,390
Other liabilities		137,320
Total Liabilities		33,972,165
Shareholders' equity:		
Common stock, no par value, 30,000,000 shares authorized:		
issued and outstanding; 1,320,000 shares (note 8)		13,123,400
Accumulated deficit		(2,180,075)
Net unrealized loss on securities available-for-sale (note 2)		(22,249)
Total shareholders' equity		10,921,076
Total liabilities and shareholders' equity	$	44,893,241

See accompanying notes to the Financial Statements

STATEMENT OF OPERATIONS

Period from February 3, 2004 (inception) to December 31, 2004

Interest income:		
Interest and fees on loans	$	1,043,173
Investment securities		174,407
Federal funds sold and other interest income		76,801
Total interest income		1,294,381
Interest expense:		
Deposits (note 6) and other borrowed funds (note 7)		136,190
Net interest income before provision for loan losses		1,157,191
Provision for loan losses (notes 1 and 3)		407,000
Net interest income after provision for loan losses		750,191
Non-interest income:		
Service charges on deposit accounts		30,206
Other non-interest income (note 14)		144,765
Total non-interest income		174,971
Non-interest expense:		
Salaries and employee benefits		1,636,533
Occupancy		212,682
Furniture and equipment		150,884
Marketing and business development		92,793
Item and data processing		76,980
Professional services		76,435
Other operating expenses (note 14)		264,550
Total non-interest expense		2,510,857
Loss before income taxes		(1,585,695)
Income taxes (note 5)		800
Net loss	$	(1,586,495)
Loss per share, basic and diluted (note 1):	$	(1.20)

See accompanying notes to the Financial Statements

STATEMENT OF SHAREHOLDERS' EQUITY

Period from February 3, 2004 (inception) to December 31, 2004

	Common Shares	Amount	Accumulated Deficit	Other Comprehensive Income	Total Share-holders' Equity
Balance at February 3, 2004	-	$ -	$ -	$ -	$ -
Pre-opening costs		-	(593,580)	-	(593,580)
Proceeds from stock offering, net					
of offering expenses of $76,600	1,320,000	13,123,400	-	-	13,123,400
Net loss		-	(1,586,495)	-	(1,586,495)
Change in unrealized losses					
on securities available-for-sale,					
net of tax effect of $0		-	-	(22,249)	(22,249)
Balances at December 31, 2004	1,320,000	$ 13,123,400	$ (2,180,075)	$ (22,249)	$ 10,921,076

See accompanying notes to the Financial Statements

STATEMENT OF CASH FLOWS

Period from February 3, 2004 (inception) to December 31, 2004

Operating Activities:		
Net loss	$	(1,586,495)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization of furniture, fixtures and equipment		161,454
Increase in cash value of bank owned life insurance		(90,378)
Provision for loan losses		407,000
Net amortization/accretion of investment discounts and premiums		15,739
Net other amortization and accretion		20,416
(Gain) on sale of available-for-sale securities		(19,503)
(Gain) on sale of SBA loans		(19,677)
Net (increase)/decrease in:		
Interest receivable		(126,848)
Other assets		(293,616)
Net increase/(decrease) in:		
Accrued interest payable		39,390
Other liabilities		137,320
Increase in deferred loan fees		184,547
Total adjustments		415,844
Net cash (used) by operating activities		(1,170,651)
Investing Activities:		
Held-to-maturity securities:		
Principal repayments		207,535
Purchases		(2,027,969)
Available-for-sale securities:		
Sales		948,394
Principal repayments		328,949
Purchases		(5,139,636)
Net proceeds from sales of loans		264,111
Purchase of bank owned life insurance		(3,000,000)
Net increase in loans		(32,788,015)
Purchase of premises and equipment		(1,307,776)
Net cash used by investing activities		(42,514,407)
Financing Activities:		
Proceeds from sale of common stock		13,123,400
Pre-opening costs		(593,580)
Increase in:		
Demand deposits		12,574,467
Savings and money market deposits		14,962,132
Time deposits		6,258,856
Net cash provided by financing activities		46,325,275
Net increase in cash and cash equivalents		2,640,217
Cash and cash equivalents at beginning of period		-
Cash and cash equivalents at end of period	$	2,640,217
Total interest paid	$	97,800
Total income taxes paid		800

Note 1. Summary of Significant Accounting Policies

Description of the Business. Santa Cruz County Bank (the Bank) is a California state chartered bank which offers a full range of commercial and personal banking services to residents and businesses in Santa Cruz County, California, through its original main office in Santa Cruz, California and a new branch office in Scotts Valley, California. The Bank was incorporated on September 10, 2003 as Santa Cruz County Bank (In Organization) and commenced banking operations on February 3, 2004 (inception), upon receipt of final approval from the California Department of Financial Institutions and the issuance of deposit insurance by the Federal Deposit Insurance Corporation. The Bank is subject to competition from other financial institutions. Additionally, the Bank is subject to regulations by the above referenced regulatory agencies and undergoes periodic examinations by those agencies.

The majority of the Bank's business is done with customers located in Northern California, specifically in Santa Cruz and adjacent counties. The Bank has 70 credit arrangements that are collateralized by real estate. Generally, the Bank maintains loan-to-value ratios no greater than 70 percent on commercial and multi-family real estate loans and no greater than 75 percent on single-family residential real estate loans. At December 31, 2004, the Bank had loans outstanding of approximately $22,599,000 that were collateralized by real estate. There were no other significant loan concentrations.

Summary of Significant Accounting Policies. The accounting and reporting policies of the Bank conform to generally accepted accounting principles in the United States of America and prevailing practices within the banking industry. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported accounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The following is a summary of significant policies used in the preparation of the accompanying consolidated financial statements.

Cash and Cash Equivalents. For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks and federal funds sold. Federal funds sold for a one day period are highly liquid investments.

Investment Securities. Marketable investment securities consist of U.S. Government Agency and mortgage-backed securities. At the time of purchase, the Bank designates securities as "held-to-maturity" or "available-for-sale" based on its investment objectives, operational needs and intent. The Bank does not engage in securities trading activities.

Held-to-maturity securities are recorded at amortized cost, adjusted for amortization or accretion of premiums or discounts. Available-for-sale securities are recorded at fair value with unrealized holding gains and losses, net of the related tax effect, reported as a separate component of shareholders' equity until realized. During the period from February 3, 2004 (inception) to December 31, 2004 there were no transfers between classifications.

Premiums and discounts are amortized or accreted over the life of the related security as an adjustment to yield using the effective interest method. Dividend and interest income are recognized on an accrual basis. Realized gains and losses for securities classified as available-for-sale and held-to-maturity are included in earnings and are derived using the specific identification method for determining the cost of securities sold.

A decline in the market value of any available-for-sale security below cost that is deemed other than temporary, results in a charge to earnings and the establishment of a new cost basis for the security. No such declines have occurred.

Loans. Loans are stated at the amount of unpaid principal, net of deferred fees, and reduced by an allowance for loan losses. Accrual of interest is discontinued on loans which are more than 90 days delinquent or when Management believes, after considering economic and business conditions and collection efforts, that the borrower's financial condition is such that collection of interest is doubtful unless the loans are well-secured and in the process of collection. When a loan is placed on non-accrual status, all interest previously accrued but not collected is charged against current period income. Income on such loans is then recognized only to the extent that cash is received and where the future collection of principal is probable.

Generally, a non-accrual loan will be restored to an accrual status when none of its principal and interest is past due, when prospects for future contractual payments are no longer in doubt and when the loan becomes well-secured and in the process of collection. The Bank had no non-accrual loans as of December 31, 2004.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement, including scheduled interest payments. Generally, the Bank identifies loans to be reported as impaired when such loans are in non-accrual status or are considered troubled debt restructurings due to the granting of a below-market rate of interest or a partial forgiveness of indebtedness on an existing loan. If the measurement of the impaired loans is less than the recorded investment in the loan, impairment is recognized by creating or adjusting an existing allocation of the allowance for loan losses. There were no impaired loans during the period February 3, 2004 (inception) to December 31, 2004.

Non-refundable fees and estimated loan origination costs are deferred net and are amortized to income over the expected life of the loan using a method that approximates the level yield method.

Loans Held for Sale. To calculate the gain (loss) on sale of loans, the Bank's investment in the loan is allocated among the retained portion of the loan, the servicing retained, the interest-only strip and the sold portion of the loan, based on the relative fair market value of each portion. The gain (loss) on the sold portion of the loan is recognized at the time of sale based on the difference between the sale proceeds and the allocated investment. As a result of the relative fair value allocation, the carrying value of the retained portion is discounted, with the discount accreted to interest income over the life of the loan. That portion of the excess servicing fees that represent contractually specified servicing fees (contractual servicing) are reflected as a servicing asset which is amortized over an estimated life using a method approximating the level yield method; in the event future prepayments exceed Management's estimates and future expected cash flows are inadequate to cover the unamortized servicing asset, additional amortization would be recognized. The portion of excess servicing fees in excess of the contractual servicing fees is reflected as interest-only (I/O) strips receivable, which are classified as interest-only strips receivable available for sale and are carried at fair value.

Allowance for Loan Losses. The allowance for loan losses is established through periodic provisions for possible loan losses. Loans are charged against the allowance for loan losses when Management believes that the collectibility of the principal is unlikely. The allowance is a reserve to provide for possible losses on existing loans that may become uncollectible, based on evaluations of the collectibility of loans and prior loan loss experience. The evaluations include consideration of changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, and current economic conditions that may affect the borrowers' ability to pay.

Management believes that the allowance for loans losses is adequate. While Management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review Bank's allowance for loan losses. Such agencies may require the Bank to recognize additions to the allowance based on their judgment of information available to them at the time of their examination.

Premises & Equipment. Premises and equipment are stated at cost less accumulated depreciation and amortization and include additions that materially extend the useful lives of existing premises and equipment. All other maintenance and repair expenditures are expensed as incurred.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, three to seven years, and are expensed to noninterest expense. Leasehold improvements are amortized over their estimated useful lives, seven years, or the initial term of the respective leases, whichever is longer.

Income Taxes. Deferred income taxes are computed using the asset and liability method, which recognizes a liability or asset representing the tax effects, based on current tax law, of future deductible or taxable amounts attributable to events that have been recognized in the consolidated financial statements. A valuation allowance is established to reduce the deferred tax asset to the level at which it is "more likely than not" that the tax asset or benefits will be realized. Realization of tax benefits of deductible temporary differences and operating loss carryforwards depends on having sufficient taxable income of an appropriate character within the carryforward periods.

Accounting Policy for Stock Options / Stock-Based Compensation. SFAS No. 123, *"Accounting for Stock-Based Compensation,"* encourages, but does not require, companies to record compensation cost for stock-based employee compensation plans at fair value. The Bank plans to account for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Board ("APB") Opinion No. 25, *"Accounting for Stock Issued to Employees,"* and related interpretations. Accordingly, compensation cost for stock options will be measured as the excess, if any, of the quoted market price of the Bank's stock at the date of the grant over the amount an employee must pay to acquire the stock. All of the Bank's stock option grants included exercise prices not less than the Bank's current market price per share; accordingly, no compensation expense was reported using the intrinsic value method of APB Opinion No. 25. See Note 8 for additional information on the Bank's stock option plan.

Had compensation cost for the Bank's stock option plans been determined based on the fair value at the grant dates for awards under those plans consistent with the method of SFAS No. 123, the Bank's net loss and loss per share would have been increased to the pro forma amounts indicated below:

	2004
Net loss:	
As reported	$ (1,586,495)
Stock-based compensation using intrinsic value method	-
Stock-based compensation that would have been reported using the fair value method of SFAS 123	(120,790)
Pro forma	$ (1,707,285)
Loss per share:	
As reported	$ (1.20)
Pro forma	(1.29)

Earnings Per Share. SFAS No. 128, *Measurement of Earnings per Share*, establishes standards for computing and reporting basic earnings per share and diluted earnings per share. Basic earnings per share are calculated by dividing net earnings for the period by the weighted-average common shares outstanding for that period. There is no adjustment to the number of outstanding shares for potential dilutive instruments, such as stock options. Diluted earnings per share takes into account the potential dilutive impact of such instruments and uses the average share price for the period in determining the number of incremental shares to add to the weighted-average number of shares outstanding. The following table summarizes the weighted average shares outstanding used to compute earnings per share:

	December 31, 2004
Net loss, as reported	$ (1,586,495)
(Loss) per share, basic and diluted	$ (1.20)
number of shares	1,320,000

Comprehensive Income. The Bank has adopted SFAS No. 130, "*Reporting Comprehensive Income*," which requires the disclosure of comprehensive income and its components. Changes in unrealized gains (losses) on available-for-sale securities are the only component of accumulated other comprehensive income for the Bank.

Pre-Opening Expenses. Prior to receipt of approval from the California Department of Financial Institutions to commence banking operations, certain pre-opening expenses were incurred by the Bank's organizers. Such expenses were funded through organizer contributions and loans to the "in organization" bank from its correspondent bank. Upon commencement of banking operations on February 3, 2004, the Bank applied to the California Department of Financial Institutions for approval to reimburse the organizers for the pre-opening expenses. The Bank made such reimbursement, amounting to approximately $594,000, subsequent to receiving such approval. The pre-opening expenses were comprised of the following:

Consulting services	$ 371,558
Legal fees	53,943
Filing fees	33,500
Business development and promotion	44,814
Occupancy	41,524
Other	48,241
Total pre-opening expenses	$ 593,580

Current Accounting Pronouncements. In December 2004, FASB revised SFAS 123 and issued it under its new name, *"Share-Based Payment".* This Statement eliminates the alternative to use Opinion 25's intrinsic value method of accounting discussed in Note 1., *Accounting Policy for Stock Options / Stock-Based Compensation.* Instead, this Statement generally requires entities to recognize the cost of employee services received in exchange for awards of stock options, or other equity instruments, based on the grant-date fair value of those awards. This cost will be recognized over the period during which an employee is required to provide service in exchange for the award, generally the vesting period.

The Bank must adopt this Statement in 2006 for all new stock option awards as well as any existing awards that are modified, repurchased or cancelled. In addition, the unvested portion of previously awarded options will also be recognized as expense. The Bank is unable to estimate the impact of this Statement on its financial condition and results of operations as the decision to grant option awards is made annually on a case-by-case basis, and, accordingly, the Bank cannot estimate the amount of stock awards that will be made in 2006.

Disclosure About Fair Value of Financial Instruments. SFAS No. 107 specifies the disclosure of the estimated fair value of financial instruments. The Bank's estimated fair value amounts have been determined by the Bank using available market information and appropriate valuation methodologies.

However, considerable judgment is required to develop the estimates of fair value. Accordingly, the estimates are not necessarily indicative of the amounts the Bank could have realized in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

Although Management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since the balance sheet date and, therefore, current estimates of fair value may differ significantly from the amounts presented in the accompanying notes.

Note 2. Investment Securities

The following table summarizes Santa Cruz County Bank's securities held-to-maturity and available-for-sale at December 31, 2004:

2004	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities available-for-sale:				
Government agency securities	$ 1,000,681	$ -	$ (9,741)	$ 990,940
Mortgage-backed securities	2,725,996	4,464	(16,972)	2,713,488
Total securities available-for-sale	$ 3,726,677	$ 4,464	$ (26,713)	$ 3,704,428
Securities held-to-maturity:				
Mortgage-backed securities	$ 1,813,111	$ -	$ (20,857)	$ 1,792,254
Total securities held-to-maturity	$ 1,813,111	$ -	$ (20,857)	$ 1,792,254

The amortized cost and estimated fair value of investment securities at December 31, 2004, by contractual maturity are shown below, except for mortgage-backed securities and other securities which are presented in total. Expected maturities on mortgage-backed securities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Securities available-for-sale		Securities held-to-maturity	
2004	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ -	$ -	$ -	$ -
Due after one year through five years	1,000,681	990,940	-	-
Mortgage-backed securities	2,725,996	2,713,488	1,813,111	1,792,254
Total	$ 3,726,677	$ 3,704,428	$ 1,813,111	$ 1,792,254

In 2004, one mortgage-backed security was sold, generating a gross realized gain of $19,503.

No investment securities were pledged to secure public deposits or for other purposes, required or permitted by law, at December 31, 2004

Note 3. Loans

Loan maturity and rate sensitivity data of the loan portfolio, in thousands, at December 31, 2004 are as follows:

	Within One Year	One to Five Years	After Five Years	Total
Real estate and construction	$ 14,361	$ 2,234	$ 1,608	$ 18,203
Consumer, other	1,343	597	526	2,466
Commercial and revolving lines	11,697	177	-	11,874
	$ 27,401	$ 3,008	$ 2,134	$ 32,543

	Within One Year	One to Five Years	After Five Years	Total
Loans at fixed interest rates	$ 255	$ 1,816	$ 2,134	$ 4,205
Loans at variable interest rates	27,146	1,192	-	28,338
	$ 27,401	$ 3,008	$ 2,134	$ 32,543

Changes in the allowance for loan losses were as follows:

Balance February 3, 2004 (inception)	$ -
Provision for loan losses	407,000
Loan charge-offs	-
Recoveries of loan charge-offs	-
Balance December 31, 2004	$ 407,000
Net loan (recoveries) charge-offs as percentage of average total loans	N/A

In general, the Bank would not recognize any interest income on loans that are classified as impaired. There were no impaired loans as of December 31, 2004.

Note 4. Premises and Equipment

The following presents the cost of premises and equipment including leasehold improvements and the related accumulated depreciation and amortization at December 31, 2004:

	December 31, 2004
Premises and leasehold improvements	$ 387,857
Furniture, fixtures and equipment	643,920
Software and capitalized data & item processing	88,251
Construction-in-progress	187,748
Total premises and equipment	1,307,776
Less accumulated depreciation and amortization	(161,454)
Premises and equipment, net	$ 1,146,322

Note 5. Income Taxes

Deferred income taxes are the result of differences between income tax accounting and accounting principles generally accepted in the United States of America, with respect to income and expense recognition. The following is a summary of the components of the net deferred tax asset accounts as of December 31, 2004:

Pre-opening expenses	$	242,400
Operating loss carryforwards		518,300
Loan loss reserve		166,200
		926,900
Valuation allowance		(926,900)
Net deferred tax asset	$	-

The valuation allowance is necessary as the Bank has not generated earnings sufficient to support the recognition of the deferred tax asset. The Bank has approximately $1.86 million in federal and state net operating loss carryforwards. The federal operating loss carryforwards will expire in 2024. The California operating loss carryforwards will expire in 2014. Income tax expense consists of the following for the period:

	2,004
Current:	
Federal	$ -
State	800
Deferred	-

Note 6. Time Deposits

The aggregate amount of time deposit accounts exceeding $100,000 was approximately $4,431,000 at December 31, 2004. At December 31, 2004 the scheduled maturities for time deposits were as follows:

(Rounded to the nearest thousand)	
Due in 2005	$ 4,682,000
Due in 2006	582,000
Due in 2007	245,000
Due in 2008	-
Due in 2009	750,000
Thereafter	-
	$ 6,259,000

Interest expense on time deposits of $100,000 or more was $44,699 in 2004.

Note 7. Borrowed Funds

The Bank has obtained federal funds borrowing guidance lines with its correspondent banks in an aggregate amount of $6 million on an unsecured basis. In addition, the Bank has established a secured borrowing arrangement, secured by its investment portfolio, with the Federal Home Loan Bank, in an amount equal to approximately 97% of the fair market value of the Bank's investment securities portfolio. Borrowing interest expense incurred in 2004 resulted from testing all those lines. The Bank had no borrowed funds at December 31, 2004.

Note 8. Stock Options

Bank has adopted a qualified stock option plan (the Plan) for employees, non-employee directors and Bank founders, under which a maximum of 396,000 shares of Bank's common stock may be issued. The Plan calls for the exercise prices of the options to be equal to or greater than the fair market value of the stock at the time of grant. During 2004, options for a total of 321,690 shares of common stock were granted with a weighted average exercise price of $10.11 per share. Options granted to Bank founders who are not also Bank directors or Bank officers were fully vested upon the date of grant. All other options shares granted have daily vesting over the first four years of the option contract. All option contracts for founders who are not also Bank directors or Bank officers have expiration dates of ten years from the date of grant. All director and employee option contracts have expiration dates on the earlier of termination of service or 10 years from the date of grant. The number of shares of common stock options exercisable at December 31, 2004 was 84,454.

The following is a summary of transactions which occurred for the period ended February 3, 2004 (inception) to December 31, 2004:

	Options Outstanding	Weighted Average Exercise Price
Options granted	321,690	$ 10.11
Exercised	-	-
Cancelled	-	-
Balance at December 31, 2004	321,690	10.11

Options Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price - Options Outstanding	Options Exercisable	Weighted Average Exercise Price - Options Exercisable
321,690	9.11 years	$ 10.11	84,454	$ 10.03

Note 9. 401(k) Employee Benefit Plan

All employees of the Bank, after completing 90 days of service, are eligible to participate in the Bank's 401(k) Plan which is a tax-deferred savings plan designed to assist employees in preparing for their retirement years. Employees may contribute to the Plan up to certain limits prescribed by the Internal Revenue Service. The Bank does not match employee contributions.

Note 10. Related Party Transactions

In the ordinary course of business, the Bank makes loans to directors, officers, shareholders and their associates on substantially the same terms, including interest rates, origination and commitment fees, and collateral, as comparable transactions with unaffiliated persons, and such loans do not involve more than the normal risk of collectibility. At December 31, 2004, no related party loans were on non-accrual or classified for regulatory reporting purposes.

Total loans and extensions of credit made to or guaranteed by the Bank's directors and officers and their related companies totaled $87,000 at December 31, 2004. Activity related to loans to directors, officers and principal shareholders and their associates for the year ended December 31, 2004 is as follows:

February 3, 2004 (inception)	$ -
New loans or disbursements	80,899
Principal repayments	79,946
Balance at December 31, 2004	$ 953

Note 11. Restrictions, Commitments, Contingencies and Other Disclosures

Restrictions on cash and due from banks. Santa Cruz County Bank is subject to Federal Reserve Act Regulation D which requires banks to maintain average reserve balances with the Federal Reserve Bank. As of December 31, 2004, the level of Santa Cruz County Bank's reservable deposits required that it maintain no reserves at the Federal Reserve Bank.

As compensation for check clearing and other services, compensating balances of approximately $10,000 were maintained with correspondent banks at December 31, 2004. The Bank maintains deposit amounts at corresponding banks that exceed federally insured limits. The Bank has not experienced any losses on amounts exceeding the insured limits.

Building lease commitments. The current operating lease for the Santa Cruz Office at 325 Soquel Avenue expires September 18, 2008, with an option to extend for three additional 5 year periods. The monthly lease payment for the Santa Cruz Office is presently $8,279 plus triple net expenses for taxes, insurance and maintenance and is subject to increases of approximately 4% annually during the initial term. The lease for the Bank's Scotts Valley Office at 4604 Scotts Valley Drive commenced on October 1, 2004, and expires on June 30, 2011, with an option to extend for two additional 5 year periods. The Scotts Valley Office lease is rent free for the first fifteen months, then $2,600 monthly for months sixteen through sixty, after which it is subject to annual CPI increases. The straight-line rent expense for the sixty month period is $1,950 per month. Triple net expenses will be incurred in addition to these lease payments. Finally, the lease for the Watsonville Office at 595 Auto Center Drive commenced on December 1, 2004, and expires January 24, 2015, with an option to extend for an additional 5 years. Base rent for the initial term of the Watsonville lease is fixed at $4,013 monthly plus triple net expenses.

Minimum rental payments for future years under these three leases are as follows at December 31, 2004:

		cash
2005	$	148,536
2006		183,876
2007		188,015
2008		167,836
2009		79,356
Thereafter		291,593
	$	1,059,212

Building rent expense for the period from February 3, 2004 (inception) to December 31, 2004, was $106,738.

Loan Commitments. The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit and financial guarantees. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The contract amounts of those instruments reflect the extent of involvement the Bank has in particular classes of financial instruments.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit and financial guarantees written is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on Management's credit evaluation. Collateral held varies but may include cash, securities, accounts receivable, inventory, property, plant and equipment, residential real estate and income-producing commercial properties.

Standby letters of credit and financial guarantees written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Financial instruments whose contract amounts represent credit risk at December 31, 2004 are as follows:

	December 31, 2004
Commitments to extend credit	$ 15,864,470
Standby letters of credit	-
Financial guarantees	-
	$ 15,864,470

Legal matters. At December 31, 2004, the Bank was not subject to any claims and/or lawsuits.

Note 12. *Bank Owned Life Insurance.*

The Bank has purchased insurance on the lives of certain senior key employees. The policies accumulate asset values to meet future liabilities including the payment of employee benefits such as deferred compensation. Increases in the cash surrender value are recorded as other non-interest income in the Statement of Operations. The cash surrender value of bank owned life insurance is reflected as a separate line item in the Statement of Condition.

Note 13. Fair Value of Financial Instruments

The following table presents the carrying amounts and estimated fair values of the Bank's financial instruments at December 31, 2004. The fair value of financial instruments does not represent actual amounts that may be realized upon any sale or liquidation of the related assets or liabilities. In addition, these values do not give effect to discounts to fair value which may occur when financial instruments are sold in larger quantities. The fair values presented represent the Bank's best estimate of fair value using the methodologies discussed below.

The respective carrying values of certain on-balance-sheet financial instruments approximated their fair values. These financial instruments include cash and due from banks, interest-bearing deposits in banks, Federal Home Loan Bank stock, federal funds sold, accrued interest receivable and accrued interest payable. Carrying values were assumed to approximate fair values for these financial instruments as they are short term in nature and their recorded amounts approximate fair values or are receivable or payable on demand. The Bank does not use derivative financial instruments.

	December 31, 2004	
	Carrying Amount	Fair Value
Financial Assets:		
Cash and cash equivalents	$ 2,640,217	$ 2,640,217
Securities available-for-sale	3,704,428	3,704,428
Securities held-to-maturity	1,813,111	1,792,254
Loans, net	31,951,121	31,734,369
Bank owned life insurance	3,090,378	3,090,378
Financial Liabilities:		
Noninterest-bearing deposits	8,474,162	8,474,162
Interest-bearing demand deposits	4,100,305	4,100,305
Money market accounts	10,276,705	10,276,705
Time certificates of deposit	6,258,856	6,296,106
Savings deposits	4,685,427	4,685,427

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Cash and cash equivalents: Carrying amount is a reasonable estimate of fair value.

Securities: The fair values of securities classified as available-for-sale and held-to-maturity are based on quoted market prices at the reporting date for those or similar investments.

Loans: The fair value of fixed rate loans is determined as the present value of expected future cash flows discounted at the interest rate currently offered by Bank, which approximates rates currently offered by local lending institutions for loans of similar terms to companies with comparable credit risk. Variable rate loans which reprice frequently with changes in approximate market rates were valued using the outstanding principal balance. The estimated fair value of loan commitments and contingent liabilities at December 31, 2004 approximate current book values.

Deposits: The fair values of demand deposits, savings deposits, and money market deposits without defined maturities were the amounts payable on demand. For substantially all deposits with defined maturities, the fair values were calculated using discounted cash flow models based on market interest rates for different product types and maturity dates. For variable rate deposits where the Bank has the contractual right to change rates, carrying value was assumed to approximate fair value. The discount rates used were based on rates for comparable deposits.

Note 14. Other Operating Income and Expense

The following is a breakdown of other non-interest income and non-interest expense in the Statement of Operations:

	2004
Other non-interest income:	
Non-interest income on bank owned life insurance	$ 90,378
Gain on sale of loans	19,677
Gain on sale of securities	19,503
Other non-interest income	15,207
Total other non-interest income	$ 144,765
Other non-interest expense:	
Stationery, supplies and printing	$ 43,998
Telephone, postage and electronic communications	32,801
Insurance and security	31,816
Loan and collection expenses	22,834
Correspondent bank charges	21,193
Shareholder related expenses	15,054
Regulatory assessments	8,997
Other non-interest expenses	87,857
Total other operating expenses	$ 264,550

Note 15. Capital Adequacy

The Bank is subject to various regulatory capital adequacy requirements administered by the banking regulatory agencies. The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) required that the federal regulatory agencies adopt regulations defining five capital tiers for depository institutions: well-capitalized, adequately capitalized, under capitalized, significantly undercapitalized, and critically undercapitalized. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, would have a direct material effect on Bank's financial statements.

Quantitative measures, established by the regulators to ensure capital adequacy, require that the Bank maintain minimum ratios (set forth in the following table) of capital to risk-weighted assets and average assets.

Management believes that, as of December 31, 2004, the Bank met all capital adequacy requirements to which they were subject.

The most recent notification from the FDIC categorized the Bank as well capitalized under the FDICIA regulatory framework for prompt corrective action. To be categorized as well capitalized, the institution must maintain a total risk-based capital ratio as set forth in the following table and not be subject to a capital directive order (such as a Formal Agreement). There are no conditions or events since that notification that Management believes has changed the Bank's risk-based capital category.

(Amount in thousands)	Actual		For Capital Adequacy Purposes:		For Regulatory Adequacy Purposes (first three years)		To Be Well Capitalized Under the FDICIA Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2004:								
Total capital (to risk-weighted assets)	$ 11,350	27.56%	$ 3,295	8.00%	$ 4,119	10.00%	$ 4,119	10.00%
Tier 1 capital (to risk-weighted assets)	$ 10,943	26.57%	$ 1,648	4.00%	$ 2,471	6.00%	$ 2,471	6.00%
Tier 1 capital (to average assets) (Leverage ratio)	$ 10,943	25.08%	$ 1,745	4.00%	$ 3,490	8.00%	$ 2,181	5.00%

(1) The leverage ratio consists of Tier 1 capital divided by quarterly average assets, excluding intangible assets and certain other items. The minimum leverage ratio guideline is 4% for banking organizations that do not anticipate significant growth and that have well-diversified risk, excellent asset quality, high liquidity, good earnings and, in general, are considered top-rated, strong banking organizations. Throughout its first three years of operation, the Bank is required to maintain a Tier 1 Leverage Ratio of not less than 8%.

Note 16. Regulatory Matters

Under the terms of approval of deposit insurance by the Federal Deposit Insurance Corporation, the Bank's Tier 1 capital-to-assets leverage ratio (as defined in the appropriate capital regulation and guidance from the Bank's primary federal regulator) shall be maintained at not less than 8% throughout the first three years of operation. Additionally, the FDIC's approval requires that the Bank operate within the parameters of the business plan submitted as part of the Bank's application for deposit insurance during the first three years of operation and that any major deviation or material changes from the plan be submitted 60 days before consummating the change.

SANTA CRUZ
COUNTY BANK

Put your money where your life is.

"Santa Cruz County has a long history of successful community banks."

A group of local business people joined to create a bank focused solely on serving the residents and businesses of Santa Cruz County when it became apparent that the last of the local independents were soon to be consumed by large out-of-area bank holding companies. Each of these people contributed time, money, and talent to the organizing effort. Today, they remain involved, serving as the Bank's ambassadors in the community.

SANTA CRUZ COUNTY BANK ORGANIZERS

Richard Alderson
Joseph Anzalone
Victor Bogard
Anthony & Rebecca Campos
Charles Canfield
0 Kenneth Chappell
Kate & Fred Chen
Marshall Delk
0 George Gallucci
0 Thomas Griffin
0 Tila Guerrero
0 William J. Hansen
0 David Heald
Mark Holcomb
0 Steve John
Mateo Lettunich
Robert Lockwood
William Moncovich
Stuart Mumm
George Ow, Jr.
Louis Rittenhouse
0 John Rossell
Frank Saveria
Robert & Bjorg Yonts

0 Directors

SANTA CRUZ COUNTY BANK

Put your money where your life is.

"We want all of our client relationships to be mutually advantageous partnerships. This means building trust and loyalty with each customer and maintaining long-term relationships."

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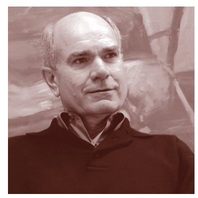
CPA, Partner, Hutchison & Bloodgood LLP

George Gallucci *(Chairman)*
Director of Client Relations for Scharf Investments

Thomas Griffin
Managing Attorney, Grunsky, Ebey, Farrar & Howell

Tila Guerrero
President & CEO, MasMac, Inc.
McDonald's Restaurants

William J. Hansen *(Vice-Chairman)*
President & CEO, Hansen Insurance



David V. Heald
Executive Vice President & Chief Credit Officer,
Santa Cruz County Bank

Steve John
President, Ocean Chevrolet

John E. Rossell
President & CEO,
Santa Cruz County Bank

STOCK LISTING

Santa Cruz County Bank's common stock is listed on the Over the Counter (OTC) Bulletin Board and trades under the ticker symbol **SCZC**.

At December 31, 2004 there were 1,320,000 shares of Santa Cruz County Bank common stock issued and outstanding and there were approximately 280 holders of record.

2004 Stock Price Range

	High	Low
First Quarter	$10.00	$10.00
Second Quarter	$15.00	$10.00
Third Quarter	$14.40	$14.80
Fourth Quarter	$14.80	$14.80

MARKET MAKER

Hoefer & Arnett
Dave Bonaccorso
800.346.5544

SHAREHOLDER RELATIONS AND INFORMATION

Shareholders with questions regarding their stockholder account, stock transfer, lost certificates or changes of address should contact their broker. In the event that certificates are held directly, shareholders should contact the transfer agent:

U.S. Stock Transfer Corporation
1745 Gardena Avenue
Glendale, California 91204-2991
818.502.1404 or 800.835.8778
www.usstock.com

For assistance with other stock related matters or to change your mailing address for quarterly shareholder communications sent directly from the bank, shareholders should contact:

Mary Anne Carson, Shareholder Relations
Santa Cruz County Bank
325 Soquel Avenue
Santa Cruz, CA 95062
831.457.5000

For financial information beyond that shown in this report, shareholders should contact:

Donald H. Soman, Chief Financial Officer
Santa Cruz County Bank
325 Soquel Avenue
Santa Cruz, CA 95062
831.457.5000

SANTA CRUZ COUNTY BANK

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BANKING OFFICES & DIRECTORY

SANTA CRUZ

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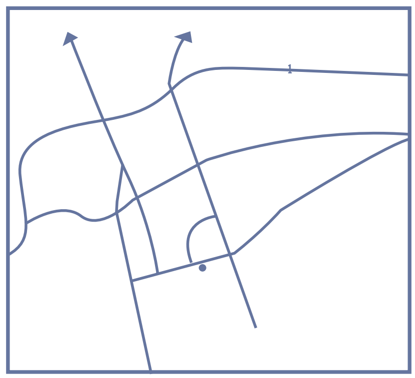
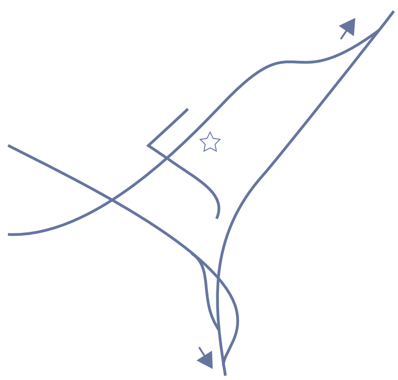


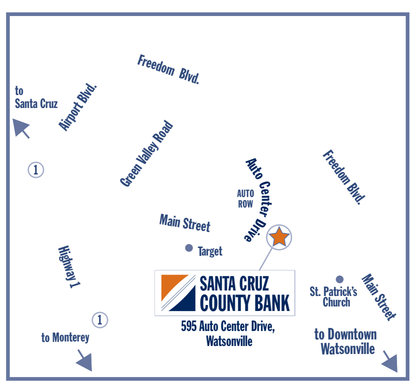
SCOTTS VALLEY

4604 Scotts Valley Drive
Scotts Valley, CA 95066
831.461.5000



WATSONVILLE

595 Auto Center Drive
Watsonville, CA 95076
831.761.7600



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