

UNITED SECURITY BANCSHARES

Form 10-Q

May 05, 2016

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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 MARCH 31, 2016

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_.

Commission file number: 000-32897

UNITED SECURITY BANCSHARES

(Exact name of registrant as specified in its charter)

CALIFORNIA

(State or other jurisdiction of incorporation or organization)

91-2112732

(I.R.S. Employer Identification No.)

2126 Inyo Street, Fresno, California

(Address of principal executive offices)

93721

(Zip Code)

Registrants telephone number, including area code (559) 248-4943

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

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 for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate 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 an accelerated filer (as defined in Rule 12b-2 of the Act).

Large accelerated filer  Accelerated filer  Non-accelerated filer  Small reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the 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, no par value

(Title of Class)

Shares outstanding as of April 30, 2016: 16,051,406

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## PART I. Financial Information

## United Security Bancshares and Subsidiaries

## Consolidated Balance Sheets – (unaudited)

March 31, 2016 and December 31, 2015

(in thousands except shares)	March 31, 2016	December 31, 2015
<b>Assets</b>		
Cash and non-interest bearing deposits in other banks	\$24,020	\$ 29,733
Cash and due from Federal Reserve Bank	101,469	96,018
Cash and cash equivalents	125,489	125,751
Interest-bearing deposits in other banks	1,530	1,528
Investment securities available for sale (at fair value)	44,394	30,893
Loans	517,678	515,318
Unearned fees and unamortized loan origination costs, net	611	58
Allowance for credit losses	(9,718	) (9,713
Net loans	508,571	505,663
Accrued interest receivable	2,741	2,220
Premises and equipment – net	10,666	10,800
Other real estate owned	12,207	12,873
Goodwill	4,488	4,488
Cash surrender value of life insurance	18,468	18,337
Investment in limited partnerships	1,012	917
Deferred tax assets - net	5,052	5,228
Other assets	7,173	6,946
<b>Total assets</b>	<b>\$741,791</b>	<b>\$ 725,644</b>
<b>Liabilities &amp; Shareholders' Equity</b>		
<b>Liabilities</b>		
<b>Deposits</b>		
Noninterest bearing	\$261,827	\$ 262,168
Interest bearing	375,500	359,637
<b>Total deposits</b>	<b>637,327</b>	<b>621,805</b>
Accrued interest payable	33	29
Accounts payable and other liabilities	5,029	5,875
Junior subordinated debentures (at fair value)	7,948	8,300
<b>Total liabilities</b>	<b>650,337</b>	<b>636,009</b>
<b>Shareholders' Equity</b>		
Common stock, no par value 20,000,000 shares authorized, 16,211,898 issued and outstanding at March 31, 2016, and 16,051,406 at December 31, 2015	53,366	52,572
Retained earnings	38,248	37,265
Accumulated other comprehensive loss	(160	) (202
<b>Total shareholders' equity</b>	<b>91,454</b>	<b>89,635</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$741,791</b>	<b>\$ 725,644</b>



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United Security Bancshares and Subsidiaries  
 Consolidated Statements of Income  
 (Unaudited)

	Three Months Ended March 31,	
(In thousands except shares and EPS)	2016	2015
Interest Income:		
Loans, including fees	\$6,631	\$ 6,279
Investment securities – AFS – taxable	189	214
Interest on deposits in FRB	124	46
Interest on deposits in other banks	2	2
Total interest income	6,946	6,541
Interest Expense:		
Interest on deposits	277	259
Interest on other borrowings	58	58
Total interest expense	335	317
Net Interest Income	6,611	6,224
(Recovery of Provision) Provision for Credit Losses	(22	) 459
Net Interest Income after (Recovery of Provision) Provision for Credit Losses	6,633	5,765
Noninterest Income:		
Customer service fees	926	833
Increase in cash surrender value of bank-owned life insurance	131	128
Gain (loss) on fair value of financial liability	358	(125
Other	146	85
Total noninterest income	1,561	921
Noninterest Expense:		
Salaries and employee benefits	2,590	2,431
Occupancy expense	1,097	940
Data processing	59	31
Professional fees	489	348
Regulatory assessments	256	246
Director fees	70	56
Correspondent bank service charges	20	19
Loss on California tax credit partnership	37	30
Net cost on operation of OREO	116	68
Other	566	539
Total noninterest expense	5,300	4,708
Income Before Provision for Taxes	2,894	1,978
Provision for Taxes on Income	1,125	750
Net Income	\$1,769	\$ 1,228
Net Income per common share		
Basic	\$0.11	\$ 0.08
Diluted	\$0.11	\$ 0.08
Shares on which net income per common shares were based		
Basic	16,211,898	16,211,898
Diluted	16,215,056	16,213,839



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United Security Bancshares and Subsidiaries  
 Consolidated Statements of Comprehensive Income  
 (Unaudited)

(In thousands)	Three Months Ended March 31, 2016	Three Months Ended March 31, 2015
Net Income	\$1,769	\$1,228
Unrealized holdings gains on securities	59	120
Unrealized gains on unrecognized post-retirement costs	12	19
Other comprehensive income, before tax	71	139
Tax expense related to securities	(24 )	(48 )
Tax expense related to unrecognized post-retirement costs	(5 )	(8 )
Total other comprehensive income	42	83
Comprehensive income	\$1,811	\$1,311



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United Security Bancshares and Subsidiaries  
 Consolidated Statements of Changes in Shareholders' Equity  
 (unaudited)

(In thousands except shares)	Common stock		Retained Earnings	Accumulated	Total
	Number of Shares	Amount		Other Comprehensive Loss	
Balance December 31, 2014	15,425,086	\$49,271	\$33,730	\$ (175 )	\$82,826
Other comprehensive income				83	83
Common stock dividends	154,249	828	(828 )		—
Stock-based compensation expense		7			7
Net income			1,228		1,228
Balance March 31, 2015	15,579,335	\$50,106	\$34,130	\$ (92 )	\$84,144
Other comprehensive loss				(110 )	(110 )
Common stock dividends	472,071	2,447	(2,447 )		—
Stock-based compensation expense		19			19
Net income			5,582		5,582
Balance December 31, 2015	16,051,406	\$52,572	\$37,265	\$ (202 )	\$89,635
Other comprehensive income				42	42
Common stock dividends	160,492	786	(786 )		—
Stock-based compensation expense		8			8
Net income			1,769		1,769
Balance March 31, 2016	16,211,898	\$53,366	\$38,248	\$ (160 )	\$91,454

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## United Security Bancshares and Subsidiaries

## Consolidated Statements of Cash Flows (unaudited)

	Three months ended	
	March 31,	
(In thousands)	2016	2015
Cash Flows From Operating Activities:		
Net Income	\$1,769	\$1,228
Adjustments to reconcile net income:to cash provided by operating activities:		
(Recovery of provision) provision for credit losses	(22	) 459
Depreciation and amortization	363	355
Amortization of investment securities	82	65
Accretion of investment securities	(10	) (6 )
Increase in accrued interest receivable	(521	) (57 )
Increase in accrued interest payable	4	2
Decrease in accounts payable and accrued liabilities	(843	) (1 )
Increase in unearned fees	(553	) (639 )
Decrease in income taxes receivable	768	801
Stock-based compensation expense	8	7
Benefit (provision) for deferred income taxes	147	(51 )
Increase in cash surrender value of bank-owned life insurance	(131	) (128 )
(Gain) loss on fair value option of financial liabilities	(358	) 125
Loss on tax credit limited partnership interest	37	30
Net increase in other assets	(979	) (126 )
Net cash (used in) provided by operating activities	(239	) 2,064
Cash Flows From Investing Activities:		
Net increase in interest-bearing deposits with banks	(2	) (1 )
Purchase of correspondent bank stock	(1	) —
Purchases of available-for-sale securities	(14,940	) —
Principal payments of available-for-sale securities	1,426	1,464
Net increase in loans	(2,491	) (34,266 )
Cash proceeds from sales of other real estate owned	824	—
Investment in limited partnership	(132	) (119 )
Capital expenditures of premises and equipment	(229	) (136 )
Net cash used in investing activities	(15,545	) (33,058 )
Cash Flows From Financing Activities:		
Net increase in demand deposits and savings accounts	11,561	13,414
Net increase (decrease) in time deposits	3,961	(519 )
Net cash provided by financing activities	15,522	12,895
Net decrease in cash and cash equivalents	(262	) (18,099 )
Cash and cash equivalents at beginning of period	125,751	103,577
Cash and cash equivalents at end of period	\$125,489	\$85,478

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United Security Bancshares and Subsidiaries - Notes to Consolidated Financial Statements - (Unaudited)

1. Organization and Summary of Significant Accounting and Reporting Policies

The consolidated financial statements include the accounts of United Security Bancshares, and its wholly owned subsidiary United Security Bank (the “Bank”) and two bank subsidiaries, USB Investment Trust (the “REIT”) and United Security Emerging Capital Fund (collectively the “Company” or “USB”). Intercompany accounts and transactions have been eliminated in consolidation.

These unaudited financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information on a basis consistent with the accounting policies reflected in the audited financial statements of the Company included in its 2015 Annual Report on Form 10-K. These interim financial statements do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of a normal, recurring nature) considered necessary for a fair presentation have been included. Operating results for the interim periods presented are not necessarily indicative of the results that may be expected for any other interim period or for the year as a whole.

Recently Issued Accounting Standards:

In March 30, 2016 FASB issued ASU 2016-09, Compensation-Stock Compensation (Topic 718). The Board is issuing this Update as part of its Simplification Initiative. The objective of the Simplification Initiative is to identify, evaluate, and improve areas of generally accepted accounting principles (GAAP) for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of financial statements. The areas for simplification in this Update were identified through outreach for the Simplification Initiative, pre-agenda research for the Private Company Council, and the August 2014 Post-Implementation Review Report on FASB No. 123(R), Share-Based Payment. We are currently evaluating the impacts of this ASU on the 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. To meet that objective, the FASB is amending the FASB Accounting Standards Codification® and creating Topic 842, Leases. This Update, along with IFRS 16, Leases, are the results of the FASB’s and the International Accounting Standards Board’s (IASB’s) efforts to meet that objective and improve financial reporting. We are currently evaluating the impacts of this ASU on the consolidated financial statements.

In January 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-01 Financial Instruments-Overall: Recognition and Measurements of Financial Assets and Financial Liabilities. This ASU requires equity investments to be measured at fair value, with changes in fair value recognized in net income. The amendment also simplifies the impairment assessment of equity investments for which fair value is not readily determinable by requiring an entity to perform a qualitative assessment to identify impairment. The ASU is effective for fiscal years beginning after December 15, 2017, and interim periods therein. We are currently evaluating the impacts of this ASU on the consolidated financial statements.

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 Company does not expect any impact on the Company's consolidated financial statements resulting from the adoption of the update.

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## 2. Investment Securities

Following is a comparison of the amortized cost and fair value of securities available-for-sale, as of March 31, 2016 and December 31, 2015:

(in 000's)

March 31, 2016

Securities available for sale:

U.S. Government agencies

U.S. Government sponsored entities &amp; agencies collateralized by mortgage obligations

Mutual Funds

Total securities available for sale

(in 000's)

December 31, 2015

Securities available for sale:

U.S. Government agencies

U.S. Government sponsored entities &amp; agencies collateralized by mortgage obligations

Mutual Funds

Total securities available for sale

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value (Carrying Amount)
U.S. Government agencies	\$ 14,003	\$ 476	\$ (109 )	\$ 14,370
U.S. Government sponsored entities & agencies collateralized by mortgage obligations	26,052	214	(96 )	26,170
Mutual Funds	4,000	—	(146 )	3,854
Total securities available for sale	\$ 44,055	\$ 690	\$ (351 )	\$ 44,394

  

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value (Carrying Amount)
U.S. Government agencies	\$ 9,778	\$ 453	\$ (108 )	\$ 10,123
U.S. Government sponsored entities & agencies collateralized by mortgage obligations	16,835	175	(52 )	16,958
Mutual Funds	4,000	—	(188 )	3,812
Total securities available for sale	\$ 30,613	\$ 628	\$ (348 )	\$ 30,893

The amortized cost and fair value of securities available for sale at March 31, 2016, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because issuers have the right to call or prepay obligations with or without call or prepayment penalties. Contractual maturities on collateralized mortgage obligations cannot be anticipated due to allowed paydowns. Mutual funds are included in the "due in one year or less" category below.

	March 31, 2016	
	Amortized Cost	Fair Value (Carrying Amount)
(in 000's)		
Due in one year or less	\$4,009	\$ 3,863
Due after one year through five years	—	—
Due after five years through ten years	963	980
Due after ten years	13,031	13,381
Collateralized mortgage obligations	26,052	26,170
	\$44,055	\$ 44,394

There were no realized gains or losses on sales of available-for-sale securities for the three month periods ended March 31, 2016 and March 31, 2015. There were no other-than-temporary impairment losses for the three month periods ended March 31, 2016 and March 31, 2015.

At March 31, 2016, available-for-sale securities with an amortized cost of approximately \$15,281,300 (fair value of \$15,770,640) were pledged as collateral for FHLB borrowings and public funds balances.

The Company had no held-to-maturity or trading securities at March 31, 2016 or December 31, 2015.

Management periodically evaluates each available-for-sale investment security in an unrealized loss position to determine if the impairment is temporary or other-than-temporary.

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The following summarizes temporarily impaired investment securities:

(in 000's)	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
March 31, 2016						
Securities available for sale:	(Carrying Amount)	(Carrying Amount)	(Carrying Amount)	(Carrying Amount)	(Carrying Amount)	(Carrying Amount)
U.S. Government agencies	\$1,980	\$ (8 )	\$76	\$ (101 )	\$2,056	\$ (109 )
U.S. Government sponsored entities & agencies collateralized by mortgage obligations	11,655	(96 )	—	—	11,655	(96 )
Mutual Funds	—	—	3,854	(146 )	3,854	(146 )
Total impaired securities	\$13,635	\$ (104 )	\$3,930	\$ (247 )	\$17,565	\$ (351 )
December 31, 2015						
Securities available for sale:						
U.S. Government agencies	\$79	\$ (108 )	\$—	\$ —	\$79	\$ (108 )
U.S. Government sponsored entities & agencies collateralized by mortgage obligations	9,913	(52 )	—	—	9,913	(52 )
Mutual Funds	—	—	3,812	(188 )	3,812	(188 )
Total impaired securities	\$9,992	\$ (160 )	\$3,812	\$ (188 )	\$13,804	\$ (348 )

Temporarily impaired securities at March 31, 2016, were comprised of one mutual fund, and two U.S. government agency securities, and four U.S. government sponsored entities and agencies collateralized by mortgage obligations.

The Company evaluates investment securities for other-than-temporary impairment (OTTI) at least quarterly, and more frequently when economic or market conditions warrant such an evaluation. The investment securities portfolio is evaluated for OTTI by segregating the portfolio into two general segments and applying the appropriate OTTI model. Investment securities classified as available-for-sale or held-to-maturity are generally evaluated for OTTI under ASC Topic 320, Investments – Debt and Equity Instruments. Certain purchased beneficial interests, including non-agency mortgage-backed securities, asset-backed securities, and collateralized debt obligations, are evaluated under ASC Topic 325-40, Beneficial Interest in Securitized Financial Assets.

In the first segment, the Company considers many factors in determining OTTI, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was affected by macroeconomic conditions, and (4) whether the Company has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to the Company at the time of the evaluation.

The second segment of the portfolio uses the OTTI guidance that is specific to purchased beneficial interests including private label mortgage-backed securities. Under this model, the Company compares the present value of the remaining cash flows as estimated at the preceding evaluation date to the current expected remaining cash flows. An OTTI is deemed to have occurred if there has been an adverse change in the remaining expected future cash flows.

Additionally, other-than-temporary-impairment occurs when the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss. If the Company intends to sell or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the other-than-temporary-impairment shall be recognized in earnings equal to the entire





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difference between the investment's amortized cost basis and its fair value at the balance sheet date. If the Company does not intend to sell the security and it is not more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis less any current-period loss, the other-than-temporary-impairment shall be separated into the amount representing the credit loss and the amount related to all other factors. The amount of the total other-than-temporary-impairment related to the credit loss is recognized in earnings, and is determined based on the difference between the present value of cash flows expected to be collected and the current amortized cost of the security. The amount of the total other-than-temporary-impairment related to other factors shall be recognized in other comprehensive (loss) income, net of applicable taxes. The previous amortized cost basis less the other-than-temporary-impairment recognized in earnings shall become the new amortized cost basis of the investment.

At March 31, 2016, the decline in market value of the impaired mutual fund, the two U.S. government agency securities, and the two U.S. government sponsored entities and agencies collateralized by mortgage obligations is attributable to changes in interest rates, and not credit quality. Because the Company does not have the intent to sell these impaired securities, and it is not more likely than not that it will be required to sell these securities before its anticipated recovery, the Company does not consider these securities to be other-than-temporarily impaired at March 31, 2016.

### 3. Loans

Loans are comprised of the following:

(in 000's)	March 31, December 31,	
	2016	2015
Commercial and Business Loans	\$57,012	\$ 54,503
Government Program Loans	2,047	1,323
Total Commercial and Industrial	59,059	55,826
Real Estate – Mortgage:		
Commercial Real Estate	178,322	182,554
Residential Mortgages	78,888	68,811
Home Improvement and Home Equity loans	778	867
Total Real Estate Mortgage	257,988	252,232
Real Estate Construction and Development	129,282	130,596
Agricultural	44,767	52,137
Installment	26,582	24,527
Total Loans	\$517,678	\$ 515,318

The Company's loans are predominantly in the San Joaquin Valley and the greater Oakhurst/East Madera County area, as well as the Campbell area of Santa Clara County. Although the Company does participate in loans with other financial institutions, they are primarily in the state of California.

Commercial and industrial loans represent 11.4% of total loans at March 31, 2016 and are generally made to support the ongoing operations of small-to-medium sized commercial businesses. Commercial and industrial loans have a high degree of industry diversification and provide working capital, financing for the purchase of manufacturing plants and equipment, or funding for growth and general expansion of businesses. A substantial portion of commercial and industrial loans are secured by accounts receivable, inventory, leases, or other collateral including real estate. The remainder are unsecured; however, extensions of credit are predicated upon the financial capacity of the borrower. Repayment of commercial loans is generally from the cash flow of the borrower.

Real estate mortgage loans, representing 49.8% of total loans at March 31, 2016, are secured by trust deeds on primarily commercial property, but are also secured by trust deeds on single family residences. Repayment of real

estate mortgage loans generally comes from the cash flow of the borrower.

Commercial real estate mortgage loans comprise the largest segment of this loan category and are available on all types of income producing and commercial properties, including: office buildings, shopping centers; apartments and motels; owner occupied buildings; manufacturing facilities and more. Commercial real estate mortgage loans can also be used to refinance existing debt. Although real estate associated with the business is the primary collateral for commercial real estate mortgage loans, the underlying real estate is not the source of repayment.

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Commercial real estate loans are made under the premise that the loan will be repaid from the borrower's business operations, rental income associated with the real property, or personal assets.

Residential mortgage loans are provided to individuals to finance or refinance single-family residences. Residential mortgages are not a primary business line offered by the Company, and a majority are conventional mortgages that were purchased as a pool. Most residential mortgages originated by the Company are of a shorter term than conventional mortgages, with maturities ranging from 3 to 15 years on average.

Home Improvement and Home Equity loans comprise a relatively small portion of total real estate mortgage loans, and are offered to borrowers for the purpose of home improvements, although the proceeds may be used for other purposes. Home equity loans are generally secured by junior trust deeds, but may be secured by 1<sup>st</sup> trust deeds.

Real estate construction and development loans, representing 25.0% of total loans at March 31, 2016, consist of loans for residential and commercial construction projects, as well as land acquisition and development, or land held for future development. Loans in this category are secured by real estate including improved and unimproved land, as well as single-family residential, multi-family residential, and commercial properties in various stages of completion. All real estate loans have established equity requirements. Repayment on construction loans generally comes from long-term mortgages with other lending institutions obtained at completion of the project.

Agricultural loans represent 8.6% of total loans at March 31, 2016 and are generally secured by land, equipment, inventory and receivables. Repayment is from the cash flow of the borrower.

Installment loans represent 5.1% of total loans at March 31, 2016 and generally consist of loans to individuals for household, family and other personal expenditures such as credit cards, automobiles or other consumer items.

In the normal course of business, the Company is party to financial instruments with off-balance sheet risk to meet the financing needs of its customers. At March 31, 2016 and December 31, 2015, these financial instruments include commitments to extend credit of \$115,270,000 and \$107,084,000, respectively, and standby letters of credit of \$3,553,000 and \$3,295,000, respectively. These instruments involve elements of credit risk in excess of the amount recognized on the consolidated balance sheet. The contract amounts of these instruments reflect the extent of the involvement the Company has in off-balance sheet financial instruments.

The Company's exposure to credit loss in the event of nonperformance by the counterparty to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amounts of those instruments. The Company uses the same credit policies 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. A majority of these commitments are at floating interest rates based on the Prime rate. Commitments generally have fixed expiration dates. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary, is based on management's credit evaluation. Collateral held varies but includes accounts receivable, inventory, leases, property, plant and equipment, residential real estate and income-producing properties.

Standby letters of credit are generally unsecured and are issued by the Company 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 loans to customers.



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## Past Due Loans

The Company monitors delinquency and potential problem loans on an ongoing basis through weekly reports to the Loan Committee and monthly reports to the Board of Directors. The following is a summary of delinquent loans at March 31, 2016 (in 000's):

March 31, 2016	Loans 30-60 Days Past Due	Loans 61-89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or More Days Past Due
Commercial and Business Loans	\$ —	\$ —	\$ —	\$ —	\$57,012	\$57,012	\$ —
Government Program Loans	—	—	—	—	2,047	2,047	—
Total Commercial and Industrial	—	—	—	—	59,059	59,059	—
Commercial Real Estate Loans	—	708	—	708	177,614	178,322	—
Residential Mortgages	62	—	389	451	78,437	78,888	—
Home Improvement and Home Equity Loans	—	—	—	—	778	778	—
Total Real Estate Mortgage	62	708	389	1,159	256,829	257,988	—
Real Estate Construction and Development Loans	—	—	—	—	129,282	129,282	—
Agricultural Loans	—	—	—	—	44,767	44,767	—
Consumer Loans	—	—	—	—	26,332	26,332	—
Overdraft Protection Lines	—	—	—	—	55	55	—
Overdrafts	—	—	—	—	195	195	—
Total Installment	—	—	—	—	26,582	26,582	—
Total Loans	\$ 62	\$ 708	\$ 389	\$ 1,159	\$516,519	\$517,678	\$ —

The following is a summary of delinquent loans at December 31, 2015 (in 000's):

December 31, 2015	Loans 30-60 Days Past Due	Loans 61-89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or More Days Past Due
Commercial and Business Loans	\$ —	\$ —	\$ —	\$ —	\$54,503	\$54,503	\$ —
Government Program Loans	13	—	—	13	1,310	1,323	—
Total Commercial and Industrial	13	—	—	13	55,813	55,826	—
Commercial Real Estate Loans	721	—	—	721	181,833	182,554	—
Residential Mortgages	62	392	—	454	68,357	68,811	—
Home Improvement and Home Equity Loans	—	39	—	39	828	867	—
Total Real Estate Mortgage	783	431	—	1,214	251,018	252,232	—
Real Estate Construction and Development Loans	—	706	—	706	129,890	130,596	—
Agricultural Loans	—	—	—	—	52,137	52,137	—
Consumer Loans	—	650	—	650	23,657	24,307	—
Overdraft Protection Lines	—	—	—	—	61	61	—
Overdrafts	—	—	—	—	159	159	—
Total Installment	—	650	—	650	23,877	24,527	—
Total Loans	\$ 796	\$ 1,787	\$ —	\$ 2,583	\$512,735	\$515,318	\$ —

Nonaccrual Loans

Commercial, construction and commercial real estate loans are placed on nonaccrual status under the following circumstances:

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- When there is doubt regarding the full repayment of interest and principal.
- When principal and/or interest on the loan has been in default for a period of 90-days or more, unless the asset is both well secured and in the process of collection that will result in repayment in the near future.
- When the loan is identified as having loss elements and/or is risk rated "8" Doubtful.

Other circumstances which jeopardize the ultimate collectability of the loan including certain troubled debt restructurings, identified loan impairment, and certain loans to facilitate the sale of OREO.

Loans meeting any of the preceding criteria are placed on nonaccrual status and the accrual of interest for financial statement purposes is discontinued. Previously accrued but unpaid interest is reversed and charged against interest income.

All other loans where principal or interest is due and unpaid for 90 days or more are placed on nonaccrual and the accrual of interest for financial statement purposes is discontinued. Previously accrued but unpaid interest is reversed and charged against interest income.

When a loan is placed on nonaccrual status and subsequent payments of interest (and principal) are received, the interest received may be accounted for in two separate ways.

Cost recovery method: If the loan is in doubt as to full collection, the interest received in subsequent payments is diverted from interest income to a valuation reserve and treated as a reduction of principal for financial reporting purposes.

Cash basis: This method is only used if the recorded investment or total contractual amount is expected to be fully collectible, under which circumstances the subsequent payments of interest are credited to interest income as received.

Loans on non-accrual status are usually not returned to accrual status unless all delinquent principal and/or interest has been brought current, there is no identified element of loss, and current and continued satisfactory performance is expected (loss of the contractual amount not the carrying amount of the loan). Return to accrual is generally demonstrated through the timely receipt of at least six monthly payments on a loan with monthly amortization.

Nonaccrual loans totaled \$8,353,000 and \$8,193,000 at March 31, 2016 and December 31, 2015, respectively. There were no remaining undisbursed commitments to extend credit on nonaccrual loans at March 31, 2016 or December 31, 2015.

The following is a summary of nonaccrual loan balances at March 31, 2016 and December 31, 2015 (in 000's).

	March 31, 2016	December 31, 2015
Commercial and Business Loans	\$648	\$ —
Government Program Loans	307	328
Total Commercial and Industrial	955	328
Commercial Real Estate Loans	1,224	1,243
Residential Mortgages	389	392
Home Improvement and Home Equity Loans	—	—

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Total Real Estate Mortgage	1,613	1,635
Real Estate Construction and Development Loans	4,808	5,580
Agricultural Loans	—	—
Consumer Loans	977	650
Overdraft Protection Lines	—	—
Overdrafts	—	—
Total Installment	977	650
Total Loans	\$8,353	\$ 8,193



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Impaired Loans

A loan is considered impaired when based on current information and events, it is probable that the Company will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the loan agreement.

The Company applies its normal loan review procedures in making judgments regarding probable losses and loan impairment. The Company evaluates for impairment those loans on nonaccrual status, graded doubtful, graded substandard or those that are troubled debt restructures. The primary basis for