FLOWSERVE CORP
Form 4
July 14, 2005

FORM 4

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

OMB APPROVAL

OMB Number:	3235-0287
Expires:	January 31, 2005
Estimated average burden hours per response...	0.5

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STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

(Print or Type Responses)

1. Name and Address of Reporting Person *
SHUFF RONALD F

(Last) (First) (Middle)

5215 N. O'CONNOR BLVD., SUITE 2300

(Street)

IRVING, TX 75039

(City) (State) (Zip)

2. Issuer Name **and** Ticker or Trading Symbol
FLOWSERVE CORP [FLS]

3. Date of Earliest Transaction (Month/Day/Year)
07/13/2005

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

_____ Director _____ 10% Owner
__X__ Officer (give title below) _____ Other (specify below)
VP, Secretary and Gen. Counsel

6. Individual or Joint/Group Filing(Check Applicable Line)
_X_ Form filed by One Reporting Person
___ Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1.Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Common Stock ($1.25 par value per share)	07/13/2005		A		4,000	A	$ 30.95	24,060	D	
Common Stock ($1.25 par value per share)								4,179	I	See Footnote (1)
Common Stock								30,123	I	See Footnote

($1.25 par value per share)			(2)
Common Stock ($1.25 par value per share)	2,684	I	401(k)

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474 (9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned
(*e.g.*, puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)		5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)		6. Date Exercisable and Expiration Date (Month/Day/Year)		7. Title and Amount o Underlying Securities (Instr. 3 and 4)	
				Code	V	(A)	(D)	Date Exercisable	Expiration Date	Title	Amoun or Numbe of Shares
Stock option (right-to-buy)	$ 19.15							(3)	07/17/2013	Common Stock	9,00
Stock option (right-to-buy)	$ 24.84							(4)	07/17/2012	Common Stock	9,00
Stock option (right-to-buy)	$ 27.12							(5)	07/18/2011	Common Stock	9,00
Stock option (right-to-buy)	$ 17.81							(6)	08/22/2010	Common Stock	7,80
Stock option (right-to-buy)	$ 17							(7)	08/03/2009	Common Stock	5,60
Stock option (right-to-buy)	$ 18.5							(8)	11/02/2008	Common Stock	8,34
Stock option (right-to-buy)	$ 30							(9)	10/23/2007	Common Stock	9,00
Stock option (right-to-buy)	$ 26.5							(10)	10/23/2006	Common Stock	7,00

Stock option (right-to-buy)	$ 27.56							(11)	10/19/2005	Common Stock	7,00
Stock option (right-to-buy)	$ 22.9							(12)	07/15/2014	Common Stock	8,50
Restricted Common Stock ($1.25 par value per share)	$ 0 (13)							(14)	(15)	Restricted Common Stock	5,00
Restricted Common Stock ($1.25 par value per share)	$ 0 (13)							(16)	(15)	Restricted Common Stock	5,00
Stock Option (right-to-buy)	$ 24.9							(17)	02/16/2015	Common Stock	8,50
Stock Option (right-to-buy)	$ 30.95	07/13/2005		A		6,500		(18)	07/13/2015	Common Stock	6,50

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
SHUFF RONALD F 5215 N. O'CONNOR BLVD. SUITE 2300 IRVING, TX 75039			VP, Secretary and Gen. Counsel	

Signatures

/s/ Ronald F. Shuff	07/14/2005
**Signature of Reporting Person	Date

Explanation of Responses:

* If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).

** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

(1) Beneficial interest in the Issuer's Dividend Reinvestment Plan.

(2) Beneficial interest in the Issuer's Deferred Compensation Plan.

(3) The option shares vest in three (3) equal annual installments which commences on July 17, 2004.

(4) The option shares vest in two (2) equal annual installments which commences on July 17, 2004.

(5) Option shares are fully vested and exercisable.

(6) Option shares are fully vested and exercisable.

(7) Option shares are fully vested and exercisable.

(8) Option shares are fully vested and exercisable.

(9) Option shares are fully vested and exercisable.

(10) Option shares are fully vested and exercisable.

(11) Option shares are fully vested and exercisable.

(12) Option shares vest in three (3) equal annual installments beginning on July 15, 2005, with the remaining thirds vesting on July 15, 2006 and July 15, 2007, respectively.

(13) The shares of Restricted Common Stock shall be valued at the fair market value upon each vesting date. A conversion or exercise price is not applicable.

(14) One-third of the shares of Restricted Common Stock vests on July 15, 2005, with the remaining thirds vesting on July 15, 2006 and July 15, 2007, respectively.

(15) The lapses of the restrictions on the shares of Restricted Common Stock is contingent upon continued employment with the Issuer. An expiration date is not applicable.

(16) One-third of the shares of Restricted Common Stock vests on February 16, 2006 and the remaining thirds vest on February 16, 2007 and February 16, 2008, respectively.

(17) The option shares vest and become exercisable in three (3) equal annual installments commencing on February 16, 2006, February 16, 2007 and February 16, 2008, respectively.

(18) The option shares vest and become exercisable in three (3) equal annual installments commencing on July 14, 2006, July 14, 2007 and July 14, 2008, respectively.

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *see* Instruction 6 for procedure.
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9,436

Multifamily

1

714

1

192

2

906

Construction and land

2

1,741

—

—

2

1,741

Home Mortgage

1

457

2

305

3

762

Installment

2

66

—

—

2

66

Total

20

$

8,270

16

$

5,309

36

$

13,579

	December 31, 2012					
	Accrual Status		Nonaccrual Status		Total Modifications	
	#	$	#	$	#	$
Commercial mortgage	2	$ 670	—	$ —	2	$ 670
Commercial loans & lines	16	5,051	13	4,784	29	9,835
Multifamily	1	716	1	203	2	919
Construction	2	1,761	—	—	2	1,761

Home mortgage	1		465	3		350	4		815
Installment	2		3	—		—	2		3
Total	24	$	8,666	17	$	5,337	41	$	14,003

The Bank’s policy is that loans placed on nonaccrual status will typically remain on nonaccrual status until all principal and interest payments are brought current and the prospect for future payment performance in accordance with the loan agreement appear relatively certain. The Bank’s policy generally refers to six months of payment performance as sufficient to warrant a return to accrual status.

The following tables present newly restructured loans that occurred during the three months ended March 31, 2013 and 2012, respectively.

	Three months ended March 31, 2013											
	Term Modifications			Rate Modifications			Combo Modifications			Total Modifications		
	#		$	#		$	#		$	#		$
	(in thousands)											
Pre-modification outstanding recorded investment:												
Commercial loans & lines	—	$	—	—	$	—	—	$	—	—	$	—
Commercial mortgage	—		—	—		—	—		—	—		—
Multifamily	—		—	—		—	—		—	—		—
Construction and land	—		—	—		—	—		—	—		—
Home mortgage	—		—	—		—	—		—	—		—
Installment	1		63	—		—	—		—	1		63
Total	1	$	63	—	$	—	—	$	—	1	$	63

	Three months ended March 31, 2013											
	Term Modifications			Rate Modifications			Combo Modifications			Total Modifications		
	#		$	#		$	#		$	#		$
	(in thousands)											
Post-modification outstanding recorded investment:												
Commercial loans & lines	—	$	—	—	$	—	—	$	—	—	$	—
Commercial mortgage	—		—	—		—	—		—	—		—
Multifamily	—		—	—		—	—		—	—		—
Construction and land	—		—	—		—	—		—	—		—
Home mortgage	—		—	—		—	—		—	—		—
Installment	1		63	—		—	—		—	1		63
Total	1	$	63	—	$	—	—	$	—	1	$	63

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	Three months ended March 31, 2012							
	Term Modifications		Payment Modifications		Combo Modifications		Total Modifications	
	#	$	#	$	#	$	#	$
	(in thousands)							
Pre-modification outstanding recorded investment:								
Commercial loans & lines	3	$ 1,986	—	$ —	1	$ 74	4	$ 2,060
Commercial mortgage	—	—	—	—	1	26	1	26
Multifamily	—	—	—	—	1	237	1	237
Home mortgage	—	—	—	—	2	538	2	538
Installment	—	—	—	—	1	4	1	4
Total	3	$ 1,986	—	$ —	6	$ 879	9	$ 2,865

	Three months ended March 31, 2012							
	Term Modifications		Payment Modifications		Combo Modifications		Total Modifications	
	#	$	#	$	#	$	#	$
	(in thousands)							
Post-modification outstanding recorded investment:								
Commercial loans & lines	3	$ 1,986	—	$ —	1	$ 74	4	$ 2,060
Commercial mortgage	—	—	—	—	1	26	1	26
Multifamily	—	—	—	—	1	237	1	237
Home mortgage	—	—	—	—	2	538	2	538
Installment	—	—	—	—	1	4	1	4
Total	3	$ 1,986	—	$ —	6	$ 879	9	$ 2,865

During the three months ended March 31, 2013 and 2012, no loans modified as a troubled debt restructuring had a payment default occurring within 12 months of the restructure date.

NOTE 5 – COVERED LOANS AND FDIC SHARED-LOSS ASSET

Covered assets consist of loans receivable and foreclosed property that we acquired in the FDIC-assisted SLTB and WCB acquisitions for which we entered into shared-loss agreements with the FDIC. The Bank will share in the losses with the FDIC, which begin with the first dollar of loss incurred on the loan pools (including single-family residential mortgage loans, commercial loans and foreclosed property) covered under our shared-loss agreements. We refer to all other loans not covered under our shared-loss agreements as non-covered loans.

Pursuant to the terms of the shared-loss agreements, the FDIC is obligated to reimburse the Bank for 80 percent of eligible losses with respect to covered assets. The Bank has a corresponding obligation to reimburse the FDIC for 80 percent of eligible recoveries with respect to covered loans. The shared-loss agreements for commercial and single-family residential mortgage loans are in effect for five years and ten years, respectively, from the acquisition date and the loss recovery provisions are in effect for eight years and ten years, respectively, from the acquisition date.

The following table reflects the estimated fair value of the acquired loans at the acquisition dates.

	Western Commercial November 5, 2010	San Luis Trust Bank February 18, 2011	Total
Home mortgage	$2,484	$64,524	$67,008
Commercial mortgage	25,920	15,948	41,868
Construction and land loans	7,599	23,395	30,994
Multifamily	—	18,450	18,450
Commercial loans and lines of credit	19,486	2,353	21,839
Home equity loans and lines of credit	—	13,669	13,669
Installment and credit card	—	453	453
Total	$55,489	$138,792	$194,281

In estimating the fair value of the covered loans at the acquisition date, we (a) calculated the amount and timing of contractual undiscounted principal and interest payments and (b) estimated the amount and timing of undiscounted expected principal and interest payments. The difference between these two amounts represents the nonaccretable difference. On the acquisition date, the amount by which the undiscounted expected cash flows exceed the estimated fair value of the acquired loans is the “accretable yield.” The accretable yield is then measured at each financial reporting date and represents the difference between the remaining undiscounted expected cash flows and the current carrying value of the loans.

The following tables present the changes in the accretable yield for the three months ended March 31, 2013 and 2012 for each respective acquired loan portfolio.

	Three months ended March 31, 2013		
	Western Commercial	San Luis Trust Bank	Total
Balance, beginning of period	$7,741	$32,578	$40,319
Accretion to interest income	(464)	(2,938)	(3,402)
Reclassifications (to)/from nonaccretable difference	(83)	964	881
Balance, end of period	$7,194	$30,604	$37,798

	Three months ended March 31, 2012		
	Western Commercial	San Luis Trust Bank	Total
Balance, beginning of period	$9,399	$55,318	$64,717
Accretion to interest income	(1,081)	(3,095)	(4,176)
Reclassifications (to)/from nonaccretable difference	637	(5,449)	(4,812)
Balance, end of period	$8,955	$46,774	$55,729

The following table sets forth the composition of the covered loan portfolio by type.

Covered loans by property type (in thousands)	At March 31, 2013	At December 31, 2012
Home mortgage	$29,577	$29,896
Commercial mortgage	27,868	28,079
Construction and land loans	17,177	19,699
Multifamily	8,842	9,699
Commercial loans and lines of credit	7,282	8,167
Home equity loans and lines of credit	6,937	6,891
Total covered loans	$97,683	$102,431

The FDIC shared-loss asset represents the present value of the amounts we expect to receive from the FDIC under our shared-loss agreements. We accrete/amortize into noninterest income over the life of the FDIC shared-loss asset the difference between the present value and the undiscounted cash flows we expect to collect from the FDIC. The FDIC shared-loss asset was $40.9 million at March 31, 2013 and $45.3 million at December 31, 2012.

The FDIC shared-loss asset was initially recorded at fair value, which represented the present value of the estimated cash payments from the FDIC for future losses on covered assets. The ultimate collectability of this asset is dependent upon the performance of the underlying covered assets, the passage of time and claims paid by the FDIC. The following table presents the changes in the FDIC shared-loss asset for the three months ended March 31, 2013.

	Three months ended March 31, 2013		
(in thousands)	WCB	SLTB	Total

Balance, beginning of period	$5,466	$39,879	$45,345
FDIC share of additional losses	14	61	75
Cash payments to (from) FDIC	47	(2,857)	(2,810)
Net (amortization) accretion	(222)	(1,485)	(1,707)
Balance, end of period	$5,305	$35,598	$40,903

Forty-five days following the tenth anniversary of the WCB and SLTB acquisition dates, the Company will be required to perform a calculation and determine if a payment to the FDIC is necessary. The payment amount will be 50 percent of the excess, if any, of (i) 20 percent of the intrinsic loss estimate minus (ii) the sum of (a) 20 percent of the net loss amount, plus (b) 25 percent of the asset discount bid, plus (c) 3.5 percent of total loss share assets at acquisition. The Company's estimate for the present value of this liability was $4.0 million at March 31, 2013 and $3.9 million at December 31, 2012.

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We evaluated each of the acquired loans under ASC 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality, or ASC 310-30, to determine loans for which 1) there was evidence of credit deterioration since origination and 2) it was probable that we would not collect all contractually required payments receivable. We determined the best indicator of such evidence was an individual loan's accrual status. Therefore, an individual loan on nonaccrual at the acquisition date (generally 90 days or greater contractually past due) was deemed to be non-performing credit impaired and therefore within the scope of ASC 310-30. Acquired loans that were accruing at the acquisition date were separately identified and labeled performing credit impaired loans.

Pursuant to an AICPA letter dated December 18, 2009, the AICPA summarized the SEC Staff's view regarding the accounting in subsequent periods for discount accretion associated with non-credit impaired loans acquired in a business combination or asset purchase. Regarding the accounting for such loans, in the absence of further standard setting, the AICPA understands that the SEC Staff would not object to an accounting policy based on contractual cash flows or an accounting policy based on expected cash flows. We believe analogizing to ASC 310-30 is an appropriate method to follow in accounting for the credit-related portion of the fair value discount on the performing credit impaired loans. By doing so, these loans, which are labeled performing credit impaired, are only being accreted up to the cash flows that we expected to receive at acquisition of the loan. Given the lending practices of the institution from which the loans were acquired, and in estimating the expected cash flows for each designated pool, all loans acquired were recognized to have some degree of credit impairment.

On the acquisition dates, the amounts by which the undiscounted expected cash flows exceeded the estimated fair value of the acquired loans is the accretable yield. The accretable yield is taken into interest income over the life of the loans using the effective yield method. The accretable yield changes over time due to both accretion and as actual and expected cash flows vary from the acquisition date estimated cash flows. The accretable yield is then measured at each financial reporting date and represents the difference between the remaining undiscounted expected cash flows and the current carrying value of the loans. The remaining undiscounted expected cash flows are calculated at each financial reporting date based on information then currently available. Increases in expected cash flows over those originally estimated increase the carrying value of the pool and are recognized as interest income prospectively. Decreases in expected cash flows compared to those originally estimated decrease the carrying value of the pool and are recognized by recording a provision for credit losses and establishing an allowance for credit losses. As the accretable yield increases due to cash flow expectations, the offset is a change to the nonaccretable difference.

The acquired covered loans are and will continue to be subject to the Bank's internal and external credit review and monitoring practices. The covered loans have the same credit quality indicators, such as risk grade and classification, as the non-covered loans, to enable the monitoring of the borrower's credit and the likelihood of repayment. If credit deteriorates beyond the respective acquisition date fair value amount of covered loans under ASC 310-30, such deterioration will be reserved for and a provision for credit losses will be charged to earnings with a partially offsetting noninterest income item reflected in the increase of the FDIC shared-loss asset.

At March 31, 2013 and December 31, 2012, there was no allowance for the covered loans accounted for under ASC 310-30 related to deterioration, as the credit quality deterioration was not beyond the acquisition date fair value amounts of the covered loans.

Loans are tracked by the number of days borrower payments are past due. The tables below present an age analysis of nonaccrual and past due covered loans, segregated by class of loan, as of March 31, 2013 and December 31, 2012.

	At March 31, 2013						
	Accruing loans 30-59	Accruing loans 60-89	Accruing loans 90+	Total Accruing past due	Nonaccrual past due loans	Current loans	Total

	days past due	days past due	days past due	loans			
				(in thousands)			
Commercial loans and lines	$ —	$ 7	$ —	$ 7	$ 1,500	$ 5,775	$ 7,282
Commercial mortgage	61	—	—	61	2,442	25,365	27,868
Multifamily	158	—	—	158	120	8,564	8,842
Construction and land	—	—	—	—	2,760	14,417	17,177
Home mortgage	—	531	—	531	4,806	24,240	29,577
Home equity loans and lines	368	—	—	368	87	6,482	6,937
Total	$ 587	$ 538	$ —	$ 1,125	$ 11,715	$ 84,843	$ 97,683

	At December 31, 2012						
	Accruing loans 30-59 days past due	Accruing loans 60-89 days past due	Accruing loans 90+ days past due	Total Accruing past due loans (in thousands)	Nonaccrual past due loans	Current loans	Total
Commercial loans and lines	$38	$—	$—	$38	$1,537	$6,592	$8,167
Commercial mortgage	163	1,244	—	1,407	860	25,812	28,079
Multifamily	149	—	—	149	867	8,683	9,699
Construction and land	146	—	—	146	5,642	13,911	19,699
Home mortgage	270	—	—	270	5,187	24,439	29,896
Home equity loans and lines	368	—	—	368	86	6,437	6,891
Total	$1,134	$1,244	$—	$2,378	$14,179	$85,874	$102,431

The table below presents the covered loan portfolio by credit quality indicator as of March 31, 2013.

	Pass	Special Mention	Substandard (in thousands)	Doubtful	Loss	Total
Home mortgage	$ 8,226	$ 3,985	$ 17,366	$ —	$ —	$ 29,577
Commercial mortgage	16,650	5,130	6,088	—	—	27,868
Construction and land	2,988	4,389	9,800	—	—	17,177
Multifamily	4,997	—	3,845	—	—	8,842
Commercial loans and lines of credit	3,292	1,521	2,423	46	—	7,282
Home equity loans and lines	5,538	647	752	—	—	6,937
	$ 41,691	$ 15,672	$ 40,274	$ 46	$ —	$ 97,683

The table below presents the covered loan portfolio by credit quality indicator as of December 31, 2012.

	Pass	Special Mention	Substandard (in thousands)	Doubtful	Loss	Total
Home mortgage	$ 8,675	$ 3,718	$ 17,503	$ —	$ —	$ 29,896
Commercial mortgage	17,067	5,022	5,942	48	—	28,079
Construction and land	3,580	7,121	8,998	—	—	19,699
Multifamily	5,109	—	4,590	—	—	9,699
Commercial loans and lines of credit	4,429	1,162	2,576	—	—	8,167
Home equity loans and lines	5,199	647	1,045	—	—	6,891

	$ 44,059	$ 17,670	$ 40,654	$ 48	$ —	$ 102,431

NOTE 6 – FORECLOSED PROPERTY

Non-covered foreclosed property at March 31, 2013 consists of a $10.4 million completed office complex project consisting of 12 buildings in Ventura County and $2.8 million of unimproved property consisting of 161 acres located in an unincorporated section of western Los Angeles County known as Liberty Canyon. The remainder represents one multifamily property and one single-family residence.

The following table presents the activity of our non-covered foreclosed property for the periods indicated.

	Three months ended March 31,			
	2013		2012	
	# of Properties	$ Amount	# of Properties	$ Amount
	(dollars in thousands)			
Beginning balance	4	$ 14,895	7	$ 20,349
New properties added	—	—	—	—
Valuation allowances	—	—	—	—
Partial sale proceeds received	—	(730)	—	—
Sales of properties	—	—	(2)	(1,640)
Ending balance	4	$ 14,165	5	$ 18,709

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Covered foreclosed property was $2.9 million at March 31, 2013 and $3.9 million at December 31, 2012. We acquired these properties as part of the FDIC-assisted WCB and SLTB acquisitions.

The following table presents the activity of our covered foreclosed property for the periods indicated.

	Three months ended March 31,			
	2013		2012	
	# of Properties	$ Amount	# of Properties	$ Amount
	(dollars in thousands)			
Beginning balance	11	$ 3,900	49	$ 14,616
New properties added	2	341	5	3,907
Sales of properties	(3)	(1,322)	(20)	(5,655)
Ending balance	10	$ 2,919	34	$ 12,868

NOTE 7 – GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill was $60.7 million at March 31, 2013 and at December 31, 2012. No impairment loss was recognized for the three-month periods ended March 31, 2013 and March 31, 2012.

Core deposit intangibles, net of accumulated amortization, were $4.9 million at March 31, 2013 and $5.2 million at December 31, 2012. Amortization expense for the three months ended March 31, 2013 was $276,000 and for the three months ended March 31, 2012 was $331,000.

Trade name intangible, net of accumulated amortization, was $1.6 million at March 31, 2013 and $1.7 million at December 31, 2012. Amortization expense for the three months ended March 31, 2013 and 2012 was $100,000 in each period.

NOTE 8 – DERIVATIVES AND HEDGING ACTIVITY

Risk Management Objective of Using Derivatives

The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. The Company manages economic risks, including interest rate, liquidity, and credit risk, primarily by managing the amount, sources, and duration of its assets and liabilities and through the use of derivative financial instruments. Specifically, the Company enters into derivative financial instruments to manage exposures that arise from business activities that result in the receipt or payment of future known and uncertain cash amounts, the value of which are determined by interest rates. The Company's derivative financial instruments are used to manage differences in the amount, timing, and duration of the Company's known or expected cash receipts and its known or expected cash payments principally related to certain variable-rate loan assets and borrowings. The Company does not use derivatives for trading or speculative purposes.

Fair Values of Derivative Instruments on the Balance Sheet

The table below presents the fair value of the Company's derivative financial instruments as well as their classification on the balance sheets as of March 31, 2013 and December 31, 2012.

Tabular Disclosure of Fair Values of Derivative Instruments

	Asset Derivatives				Liability Derivatives			
	As of March 31, 2013		As of December 31, 2012		As of March 31, 2013		As of December 31, 2012	
(in thousands)	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments								
Interest rate products	Other Assets	$ 31	Other Assets	$ 30	Other Liabilities	$ —	Other Liabilities	$ —
Total derivatives designated as hedging instruments		$ 31		$ 30		$ —		$ —
Derivatives not designated as hedging instruments								
Interest rate products	Other Assets	$ 72	Other Assets	$ 76	Other Liabilities	$ —	Other Liabilities	$ —
Total derivatives not designated as hedging instruments		$ 72		$ 76		$ —		$ —

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Cash Flow Hedges of Interest Rate Risk

The Company’s objectives in using interest rate derivatives are to add stability to interest income and expense and to manage its exposure to interest rate movements. To accomplish this objective, the Company primarily uses interest rate caps as part of its interest rate risk management strategy. For hedges of the Company’s variable-rate borrowings, interest rate caps designated as cash flow hedges involve the receipt of variable amounts from a counterparty if interest rates rise above the strike rate on the contract in exchange for an up-front premium. As of March 31, 2013, the Company had three interest rate caps with a notional amount of $37.1 million that were designated as cash flow hedges associated with the Company’s variable-rate borrowings. One of the caps is forward-starting and was not in effect during the three months ended March 31, 2013.

The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges is recorded in Other Comprehensive Income and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. The ineffective portion of the change in fair value of the derivatives is recognized directly in earnings. During 2013 and 2012, such derivatives were used to hedge the forecasted variable cash outflows associated with subordinated debt related to trust preferred securities. No hedge ineffectiveness was recognized during the three months ended March 31, 2013 and 2012.

Amounts reported in Other Comprehensive Income related to derivatives will be reclassified to interest expense as interest payments are made on the Company’s variable-rate liabilities. During the next twelve months, the Company estimates that an additional $116,893 will be reclassified as an addition to interest expense.

Non-designated Hedges

Derivatives not designated as hedges are not speculative and are utilized as part of the Company’s overall interest rate risk management strategy. As of March 31, 2013, the Company had twelve interest rate caps with an aggregate notional amount of $240 million and hedge accounting does not apply; therefore, all changes in the fair value of the caps are recognized in earnings each period.

Effect of Derivative Instruments on the Statement of Operations

The tables below present the effect of the Company’s derivative financial instruments on the statement of operations for the three months ended March 31, 2013 and 2012.

Derivatives in Cash Flow Hedging Relationships	Amount of Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)		Location of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Amount of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)		Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion)	Amount of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion)	
	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012		Three Months Ended March 31, 2013	Three Months Ended March 31, 2012		Three Months Ended March 31, 2013	Three Months Ended March 31, 2012
				(in thousands)			(in thousands)	
						Other non-		

				Interest					interest		
Interest Rate Products	$—	$(14	)	income	$(26	)	$(12	)	income	$—	$—
Total	$—	$(14	)		$(26	)	$(12	)		$—	$—

Derivatives Not Designated as Hedging Instruments	Location of Gain or (Loss) Recognized in Income on Derivative	Amount of Gain or (Loss) Recognized in Income on Derivative Three Months Ended March 31, 2013		2012	
Interest Rate Products	Other non-interest income	$	(3)	$	(111)
Total		$	(3)	$	(111)

Credit-risk-related Contingent Features

The Company has agreements with certain of its derivative counterparties that contain a provision where if the Company defaults on any of its indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender, then the Company could also be declared in default on its derivative obligations. Similarly, the Company could be required to settle its obligations under certain of its agreements if the Company fails to maintain its status as a well or adequately capitalized institution. As of March 31, 2013, the Company did not have any derivatives that were in a net liability position related to these agreements.

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NOTE 9–EARNINGS PER SHARE

Basic earnings per share, or EPS, excludes dilution and is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if common shares were issued pursuant to the exercise of common stock options under the Company's stock option plans and if common shares were issued from the conversion of the convertible preferred stock. For the three months ended March 31, 2013 and 2012, common stock equivalents totaling approximately 254,706 and 583,790 shares, respectively, were excluded from the calculation of diluted earnings per share, as their impact would be anti-dilutive. The following table illustrates the computations of basic and diluted EPS for the periods indicated:

	Three months ended March 31,			
	2013		2012	
(in thousands, except per share data)	Diluted	Basic	Diluted	Basic
Net income as reported	$391	$391	$2,585	$2,585
Less preferred stock dividend declared	(313)	(313)	(313)	(313)
Net income available to common shareholders	$78	$78	$2,272	$2,272
Weighted average common shares outstanding-Basic	29,227	29,227	29,236	29,236
Stock options	80	—	—	—
Restricted stock	—	—	410	—
Convertible preferred stock	343	—	328	—
Weighted average common shares outstanding-Diluted	29,650	29,227	29,974	29,236
Net income per common share – basic and diluted	$0.00	$0.00	$0.08	$0.08

NOTE 10 – FAIR VALUE MEASUREMENT

FASB accounting standards codification related to fair value measurements defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurement. This standard applies to all financial assets and liabilities that are being measured and reported at fair value on a recurring and non-recurring basis.

As defined in the FASB accounting standards codification, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The following table presents information about the Company's assets and liabilities measured at fair value on a recurring and non-recurring basis as of March 31, 2013 and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value. In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) for identical instruments that are highly liquid, observable and actively traded in over-the-counter markets. Fair values determined by Level 2 inputs utilize inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-derived valuations whose inputs are observable and can be corroborated by market data. Level 3 inputs are unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

The Company uses fair value to measure certain assets and liabilities on a recurring basis when fair value is the primary measure for accounting. This is done primarily for available-for-sale securities and derivatives. Fair value is used on a nonrecurring basis to measure certain assets when applying lower of cost or market accounting or when adjusting carrying values, such as for loans held-for-sale, impaired loans, and foreclosed property. Fair value is also used when evaluating impairment on certain assets, including securities, goodwill, core deposit and other intangibles, for valuing assets and liabilities acquired in a business combination and for disclosures of financial instruments as required by the FASB accounting standards codification related to fair value disclosure reporting. The following tables present information on the assets measured and recorded at fair value on a recurring and nonrecurring basis at March 31, 2013.

	Fair value at Mar. 31, 2013	Financial Assets Measured at Fair Value on a Recurring Basis at March 31, 2013, Using Quoted prices in active markets for identical assets (Level 1)	Other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
		(in thousands)		
U.S. government agency notes	$32,578	$—	$32,578	$—
U.S. government agency mortgage-backed securities	159,652	—	159,652	—
U.S. government agency collateralized mortgage obligations	116,600	—	116,600	—
Municipal securities	6,738	—	6,738	—
Other domestic debt securities	2,720	—	—	2,720
Interest rate caps	103	—	103	—
Total assets measured at fair value	$318,391	$—	$315,671	$2,720

	Fair value at Mar. 31, 2013	Financial Assets Measured at Fair Value on a Non-Recurring Basis at March 31, 2013, Using Quoted prices in active markets for identical assets (Level 1)	Other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total losses
			(in thousands)		
Non-covered impaired loans	$23,796	$—	$—	$ 23,796	$29
Non-covered foreclosed property	14,165	—	—	14,165	—
Covered foreclosed property	2,919	—	—	2,919	—
Total assets measured at fair value	$40,880	$—	$—	$ 40,880	$29

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The following tables present information on the assets measured and recorded at fair value on a recurring and nonrecurring basis at and for the year ended December 31, 2012.

	Fair value at December 31, 2012	Financial Assets Measured at Fair Value on a Recurring Basis at December 31, 2012, Using		
		Quoted prices in active markets for identical assets (Level 1)	Other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
	(in thousands)			
U.S. Treasury notes/bills	$8,011	$—	$8,011	$—
U.S. government agency notes	32,608	—	32,608	—
U.S. government agency mortgage-backed securities	166,749	—	166,749	—
U.S. government agency collateralized mortgage obligations	163,054	—	163,054	—
Municipal securities	7,892	—	7,892	—
Other domestic debt securities	2,727	—	—	2,727
Interest rate caps	106	—	106	—
Total assets measured at fair value	$381,147	$—	$378,420	$2,727

	Fair value at December 31, 2012	Financial Assets Measured at Fair Value on a Non-Recurring Basis at December 31, 2012, Using			Total losses
		Quoted prices in active markets for identical assets (Level 1)	Other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
	(in thousands)				
Non-covered impaired loans	$13,472	$—	$—	$ 13,472	$(524)
Non-covered foreclosed property	14,895	—	—	14,895	(1,732)
Covered foreclosed property	3,900	—	—	3,900	—
Total assets measured at fair value	$32,267	$—	$—	$ 32,267	$(2,256)

There were no significant transfers of assets into or out of Level 1, Level 2 or Level 3 of the fair value hierarchy during the quarter ended March 31, 2013. There have been no changes in valuation techniques for the quarter ended March 31, 2013 and such techniques are consistent with techniques used in prior periods.

The following methods were used to estimate the fair value of each class of financial instrument above:

Available-for-sale securities—Fair values for securities are based on quoted market prices of identical securities, where available (Level 1). When quoted prices of identical securities are not available, the fair value estimate is based on quoted market prices of similar securities, adjusted for differences between the securities (Level 2). Adjustments may include amounts to reflect differences in underlying collateral, interest rates, estimated prepayment speeds, and counterparty credit quality. In determining the fair value the securities categorized as Level 2, the Company obtains a report from a nationally recognized broker-dealer detailing the fair value of each security in our portfolio as of each reporting date. The broker-dealer uses observable market information to value our securities, with the primary source being a nationally recognized pricing service. The Company reviews the market prices provided by the broker-dealer for our securities for reasonableness based upon our understanding of the marketplace and we consider any credit issues relating to the bonds. As the Company has not made any adjustments to the market quotes provided to us and they are based on observable market data, they have been categorized as Level 2 within the fair value hierarchy.

Interest rate caps—The fair values of interest rate caps are estimated using the market standard methodology of discounting the future expected cash receipts that would occur if variable interest rates rise above the strike rate of the caps. The variable interest rates used in the calculations of projected receipts on the caps are based on an expectation of future interest rates derived from observable market interest rates curves and volatilities. In addition, the Company incorporates credit valuation adjustments to appropriately reflect nonperformance risk in the fair value measurements of its derivatives. The credit valuation adjustments are calculated by determining the total expected exposure of the derivatives (which incorporates both the current and potential future exposure) and then applying the counterparties' credit spreads to the exposure. The total expected exposure of a derivative is derived using market-observable inputs, such as yield curves and volatilities. For the counterparties' credit spreads, the credit spreads over LIBOR used in the calculations represent implied credit default swap spreads obtained from a third party credit data provider. In adjusting the estimated fair value of its derivative contracts for the effect of nonperformance risk, the Company has considered the impact of netting and any applicable credit enhancements. The Company made an accounting policy election to measure the credit risk of its derivative financial instruments that are subject to master netting agreements on a net basis by counterparty portfolio.

Impaired loans—Impaired loans are measured and recorded at the fair value of the loan's collateral on a nonrecurring basis as the impaired loans shown are collateral dependent. The fair value of each loan's collateral is generally based on estimated market prices from an independently prepared appraisal, which is then adjusted for the cost related to liquidating such collateral; such valuation inputs result in a nonrecurring fair value measurement that is categorized as a Level 3 measurement.

Foreclosed property—Foreclosed property is initially measured at fair value at acquisition and carried at the lower of this new cost basis or fair value on a nonrecurring basis. The foreclosed property shown is collateral dependent and, accordingly, is measured based on the fair value of such collateral. The fair value of collateral is generally based on estimated market prices from an independently prepared appraisal, which is then adjusted for the estimated cost related to liquidating such collateral; such valuation inputs result in a nonrecurring fair value measurement that is categorized as a Level 3 measurement.

The Company is required to disclose estimated fair values for our financial instruments during annual and interim reporting periods. Fair value estimates, methods and assumptions, set forth below for our financial instruments, are made solely to comply with the requirements of the disclosures regarding fair value of financial instruments. The following describes the methods and assumptions used in estimating the fair values of financial instruments, excluding financial instruments already recorded at fair value as described above.

Cash and cash equivalents— The carrying amounts of cash and interest bearing deposits at other banks is assumed to be the fair value given the liquidity and short-term nature of these deposits.

Loans—Loans are not measured at fair value on a recurring basis. Therefore, the following valuation discussion relates to estimating the fair value to be disclosed under fair value disclosure requirements. Loans were divided into four major groups. The loan groups included (1) loans that mature or re-price in three months or less, (2) loans that amortize or mature in more than three months, (3) impaired loans, and (4) loans acquired in the Western Commercial Bank and San Luis Trust Bank acquisitions. We estimated the fair value of the loans that mature or re-price within three months, impaired loans and loans acquired in the Western Commercial Bank and San Luis Trust Bank acquisitions at their carrying value. We used discounted cash flow methodology to estimate the fair value of loans that amortize or mature in more than three months. We developed pools of these loans based on similar characteristics such as underlying type of collateral, fixed or adjustable rate of interest, payment or amortization method, credit risk categories and other factors. We projected monthly principal and interest cash flows based on the contractual terms of the loan, adjusted for assumed prepayments and defaults, and discounted these at a rate that considered funding costs, a market participant's required rate of return and adjusted for servicing costs and a liquidity discount. Loans are not normally purchased and sold by the Company, and there are no active trading markets for much of this portfolio.

FDIC shared-loss asset—The fair value of the FDIC shared-loss asset represents the present value of the amounts we expect to receive from the FDIC under our shared-loss agreements and is based upon estimated cash flows from our covered assets discounted by a rate reflective of the creditworthiness of the FDIC as would be required by market participants.

Bank owned life insurance assets—Fair values of insurance policies owned are based on the insurance contract's cash surrender value.

Deposits—The fair values disclosed for demand deposits are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). The carrying amounts of variable-rate money market accounts and fixed-term certificates of deposit (CDs) approximate their fair values at the reporting date. Fair values for fixed-rate CDs are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

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Federal Home Loan Bank advances and other borrowings—The fair value of the FHLB advances and other borrowings is estimated using a discounted cash flow analysis based on the Company's current incremental borrowing rates for similar types of borrowing arrangements.

Junior subordinated debentures—The fair value of the debentures is estimated using a discounted cash flow analysis based on current incremental borrowing rates for similar types of borrowing arrangements.

Off-balance sheet instruments—Off-balance sheet instruments include unfunded commitments to extend credit and standby letters of credit. The fair value of these instruments is not considered practicable to estimate because of the lack of quoted market prices and the inability to estimate fair value without incurring excessive costs.

The following table estimates fair values and the related carrying amounts of the Company's financial instruments:

As of March 31, 2013	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Fair Value
			(in thousands)		
Financial assets:					
Cash, due from banks and interest-bearing deposits with other banks	$117,900	$117,900	$—	$ —	$117,900
Securities available-for-sale	318,288	—	315,568	2,720	318,288
FHLB and other stock	10,774	—	—	10,774	10,774
Bank owned life insurance assets	13,198	13,198	—	—	13,198
Non-covered loans, net	1,011,896	—	—	937,663	937,663
Covered loans	97,683	—	—	110,407	110,407
FDIC shared-loss asset	40,903	—	—	21,319	21,319
Interest rate cap	103	—	—	103	103
Financial liabilities:					
Demand deposits, money market and savings	1,102,731	$1,102,731	$—	$ —	1,102,731
Time certificates of deposit	255,837	—	257,923	—	257,923
FHLB advances and other borrowings	107,026	—	111,522	—	111,522
Junior subordinated debentures	26,805	—	—	14,462	14,462
FDIC shared-loss liability	4,027	—	—	4,027	4,027

As of December 31, 2012	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Fair Value

	(in thousands)				
Financial assets:					
Cash, due from banks and interest-bearing deposits with other banks	$ 166,874	$ 166,874	$ —	$ —	$ 166,874
Securities available-for-sale	381,041	—	378,314	2,727	381,041
FHLB and other stock	10,784	—	—	10,784	10,784
Bank owned life insurance assets	13,097	13,097	—	—	13,097
Non-covered loans, net	1,043,021	—	—	966,505	966,505
Covered loans	102,431	—	—	116,141	116,141
FDIC shared-loss asset	45,345	—	—	24,129	24,129
Interest rate cap	106	—	—	106	106
Financial liabilities:					
Demand deposits, money market and savings	$ 1,239,272	$ 1,239,272	$ —	$ —	$ 1,239,272
Time certificates of deposit	268,560	—	270,778	—	270,778
FHLB advances and other borrowings	107,054	—	110,767	—	110,767
Junior subordinated debentures	26,805	—	—	14,462	14,462
FDIC shared-loss liability	3,900	—	—	3,900	3,900

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These fair value disclosures represent the Company's best estimates based on relevant market information and information about the financial instruments. Fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of the various instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in the above methodologies and assumptions could significantly affect the estimates.

NOTE 11 – COMMITMENTS AND CONTINGENCIES

In the normal course of business to meet the financing needs of its customers, the Company is a party to financial instruments with off-balance sheet risk. These financial instruments include commitments to extend credit and the issuance of letters of credit. These instruments involve, to varying degrees, elements of credit risk in excess of the amounts recognized in the balance sheets. The contract amounts of those instruments reflect the extent of involvement the Company has in particular classes of financial instruments.

The Company's exposure to credit loss, in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and letters of credit written, is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The Company may or may not require collateral or other security to support financial instruments with credit risk, depending on its loan underwriting guidelines.

The following summarizes the Company's outstanding commitments:

	March 31, 2013	December 31, 2012
	(in thousands)	
Financial instruments whose contract amounts contain credit risk:		
Commitments to extend credit	$162,591	$161,395
Commercial and standby letters of credit	5,472	1,651
	$168,063	$163,046

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, total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if deemed necessary by the Company upon an extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property and equipment, and income-producing properties.

Letters of credit written are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing, and similar transactions. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Company holds cash, marketable securities, or real estate as collateral supporting those commitments for which collateral is deemed necessary.

The allowance for losses on undisbursed commitments was $86,000 at March 31, 2013 and December 31, 2012. The reserve is included in accrued interest payable and other liabilities on the balance sheets.

The nature of the Company’s business causes it to be involved in ordinary routine legal proceedings from time to time. Although the ultimate outcome and amount of liability, if any, with respect to these legal proceedings to which we are currently a party cannot presently be ascertained with certainty, in the opinion of management, based upon information currently available to us, except as described below, any resulting liability is not likely to have a material adverse effect on the Company’s consolidated financial condition, results of operations or cash flow.

Nine lawsuits have been filed in the Superior Court of the State of California, County of Los Angeles by various former clients of political campaign and non-profit organization treasurer Kinde Durkee. The lawsuits are entitled (i) Wardlaw, et al. v. First California Company, et al. (Case No. SC114232) (the “Wardlaw Action”), filed September 23, 2011; (ii) Lou Correa for State Senate, et al. v. First California Company, et al. (Case No. BC479872) (the “Correa Action”), filed February 29, 2012; (iii) Committee to Re-elect Lorreta Sanchez, et al. v. First California Company, et al. (Case No. BC479873) (the “Sanchez Action”), filed February 29, 2012, (iv) Holden for Assembly v. First California Company, et al. (Case No. BC 489604) (“Holden Action”), filed August 3, 2012; (v) Latino Diabetes Ass’n v. First California Company, et al. (Case No. BC 489605) (“LDA Action”), filed August 3, 2012; (vi) Jose Solorio Assembly Officeholder Committee, et al. v. First California Company, et al. (Case No. 492855) (“Solorio Action”), filed September 27, 2012; (vii) Foster for Treasurer 2014, et al. v. First California Company, et al. (Case No. BC 492878) (“Foster Action”), filed September 27, 2012; (viii) Los Angeles County Democratic Central Committee, et al. v. First California Company, et al. (Case No. BC 492854) (“LACDCC Action”), filed September 27, 2012; and (ix) National Popular Vote, et al. v. First California Bank, et al. (Case No. BC501213) (“NPV Action”), filed February 19, 2013. Plaintiffs in each of the cases claim, among other things, that the Company aided and abetted a fraud and unlawful conversion by Ms. Durkee and/or her affiliated company of funds held in accounts at the Company. Based largely on the same alleged conduct, plaintiffs also assert claims for an alleged violation of California Business & Professions Code Section 17200 and for declaratory relief. Plaintiffs seek compensatory and punitive damages, as well as various forms of equitable and declaratory relief.

Each of the cases is pending before the same judge, who is coordinating their progress. Except for the NPV Action, the Company has answered each of the complaints in the cases in which the Company has been served, and the parties are engaged in discovery. A trial date has not yet been scheduled in any of the actions.

On September 23, 2011, the Company filed a Complaint-in-Interpleader in the Superior Court of the State of California, County of Los Angeles (Case No. BC470182), pursuant to which the Company interplead the sum of $2,539,049 as the amounts on deposit in accounts at the Company that were controlled by Ms. Durkee on behalf of the several hundred named defendants (the “Interpleader Action”). The Company seeks an order requiring the defendants to interplead and litigate their respective claims, discharging the Company from any and all liability, and restraining proceedings or actions against the Company by the defendants. The Company also seeks its costs and reasonable attorneys’ fees. The Interpleader Action has been related to the other actions, described above, and is pending before the same judge.

On June 18, 2012, the Company moved for summary judgment in the Interpleader Action. At hearings held on October 3, 2012, November 2, 2012, and January 25, 2013, the Court entered summary judgment with respect to a majority of the accounts at issue.

On November 20, 2012, a purported stockholder of the Company filed a lawsuit in connection with the proposed merger between the Company and PacWest announced on November 6, 2012. Captioned Paul Githens v. C.G. Kum, et al., Case No. BC496018, the suit was filed in the Superior Court of the State of California, Los Angeles County, against the Company, its directors, and PacWest. It is brought as a putative class action and alleges that the Company’s directors breached certain alleged fiduciary duties to the Company’s stockholders by approving the merger agreement pursuant to an allegedly unfair process and at an allegedly unfair price. It alleges that PacWest aided and abetted those breaches. The suit seeks, among other things, to enjoin consummation of the merger. On January 24, 2013, the plaintiff filed an amended complaint, adding claims that the defendants failed to disclose material information concerning the merger. On March 4, 2013, the court sustained the defendants’ demurrers to the plaintiff’s complaint with leave to amend. On March 14, 2013, the plaintiff filed an amended complaint.

On March 17, 2013, the Company and PacWest entered into a memorandum of understanding with the plaintiff in the suit regarding the settlement of the suit. In connection with the settlement of the suit, we made supplemental disclosures to the Company’s Definitive Proxy Statement on Schedule 14A filed with the SEC on February 13, 2013, by filing a Form 8-K filed with the SEC on March 18, 2013. The memorandum of understanding also contemplates that the parties will enter into a stipulation of settlement. The stipulation of settlement will be subject to customary conditions, including court approval following notice to the Company’s stockholders. In the event that the parties enter into a stipulation of settlement, a hearing will be scheduled at which the Superior Court of the State of California will consider the fairness, reasonableness and adequacy of the settlement. If the settlement is finally approved by the court, it will resolve and release all claims in all actions that were or could have been brought challenging any aspect of the proposed merger, the merger agreement and any disclosure made in connection therewith, pursuant to terms that will be disclosed to the Company’s stockholders prior to final approval of the settlement. In addition, in connection with the settlement, the parties contemplate that plaintiff’s counsel will file a petition in the Superior Court of the State of California for an award of attorneys’ fees and expenses to be paid by the Company or its successor. The settlement will not affect the consideration that the Company’s stockholders are entitled to receive in the merger. There can be no assurance that the parties will enter into a stipulation of settlement, or that the court will approve any proposed settlement. In such event, the proposed settlement as contemplated by the memorandum of understanding may be terminated.

Merchant card processing guarantees represent the Bank’s indirect obligations in connection with the processing of credit and debit card transactions on behalf of merchants. The EPS division provides transaction processing services to various merchants through an independent third party vendor (“ISO”) with respect to credit and debit cards and has potential liability for card transaction processing services. The nature of the liability arises as a result of a billing dispute (“chargeback”) between a merchant and a cardholder that is ultimately resolved in the cardholder’s favor. The merchant is liable to refund the amount to the cardholder. In general, if the ISO is unable to collect this amount from the merchant, the ISO bears the loss for the amount of the chargeback refund paid to the cardholder. If the ISO and merchant are insolvent or incapable of paying the chargeback, the Bank bears the risk and responsibility to pay the chargeback.

Our risk of loss is mitigated as the cash flows between the Bank and the merchant are settled on a net basis with the networks (Visa, MasterCard and Discover) directly through the Bank, and the Bank has the right to offset any payments with cash flows otherwise due to the merchant. Additionally, the Bank retains cash reserve accounts on balance to offset risk for merchants and the ISO. To further mitigate this risk the Bank may delay settlement. The Bank may require at any time an increase to reserve account balances. The Bank also maintains an insurance policy of $10.0 million for losses due to fraud.

The Bank's maximum potential contingent liability related to merchant card processing services is estimated to be the total volume of card transactions that meet the requirements to be valid chargeback transactions at any given time. However, the Bank believes that the maximum exposure is not representative of the actual potential loss exposure based on the Bank's historical experience. The Bank assesses the probability and amount of its contingent liability related to merchant card processing based on the financial strength of the ISO, the extent and nature of unresolved charge-backs and its historical loss experience. For the three months ended March 31, 2013 and 2012, the Bank incurred no losses related to merchant card processing activities.

Prepaid card services guarantees represent the Bank's indirect obligations in connection with the processing of prepaid card transactions on cards issued by the Bank. The EPS division provides card issuing and sponsorship services through various third party service providers ("Program Managers"), who are considered third-party affiliates of the Bank, with respect to various prepaid card programs and has potential liability for prepaid card processing services. The nature of the liability arises from possible non-compliance with legal and regulatory requirements related to the prepaid card programs. The prepaid card programs are subject to federal, state and local laws and regulations including anti-money laundering laws, escheatment laws, privacy and safeguard laws, banking regulations and consumer protection laws. These laws are continuously evolving and sometimes ambiguous or inconsistent, and the extent to particular practices of the Bank and its Program Managers is at times unclear. Any failure to comply with applicable law, either by us or our Program Managers could result in restrictions on our ability to provide our products and services, as well as the imposition of civil fines, restitution to customers and other penalties.

If the Bank is subject to monetary losses, such as payment of restitution to prepaid card customers, related to prepaid card services, the contracts between the Bank and the Program Managers require the Program Managers to provide indemnification to the Bank. However, based on the financial strength of the Program Managers or other factors, the Bank may potentially be liable for the payment of the fines or penalties because we are the issuing bank of the cards. If a Program Manager is required to pay restitution to its customers, based on the financial strength of the Program Manager or other factors, the Bank may potentially be liable for the payment of the restitution because we are the issuing bank of the cards.

The Bank assesses the probability and amount of its contingent liability related to prepaid card services based on the financial strength of the Program Managers, the extent and nature of known violations of laws and regulations and historical trends in loss experience. The Company requires the Program Managers to maintain a specific cash reserve accounts on deposit the Company to mitigate risk. The Bank may require at any time an increase to reserve account balances. The Bank also maintains an insurance policy of $10.0 million for losses due to fraud. For the three months ended March 31, 2013 and 2012, the Bank incurred no material losses related to prepaid card services.

NOTE 12 – SUBSEQUENT EVENT

In April 2013, the FDIC notified the Bank that it planned to take formal enforcement action against the Bank, to which the Bank has agreed in principle. The FDIC alleged that the Bank engaged in unsafe and unsound banking practices through its EPS Division, and among other things, violated Section 5 of the Federal Trade Commission Act by engaging in certain deceptive and unfair practices in connection with its oversight of prepaid debit card programs offered by various third-party providers, for which the Bank serves as card issuer. The FDIC has also alleged that, in connection with such prepaid card programs, the Bank violated a Treasury Department regulation governing the use of the Automated Clearing House system to deliver federal benefit payments to prepaid debit cards. The Bank understands that the formal enforcement action is likely to include certain actions to address the allegations, including making changes to certain of the Bank's practices and products and establishing accruals for, among other costs, a civil money penalty and restitution obligations of third-party providers to certain prepaid card holders to the extent that such third-party providers are unable to satisfy such obligations.

As previously disclosed, the Board of Directors of the Company and the Bank committed to a plan to wind down the EPS division and targeted December 31, 2013 for a substantial completion of such wind down. There was no net income for this discontinued operation for the three months ended March 31, 2013 because revenues were $2.0 million and expenses were $2.0 million. Expenses included costs associated with the wind down of the division and the planned enforcement action.

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

Forward-Looking Statements

This discussion contains certain forward-looking statements about us; we intend these statements to fall under the safe harbor for "forward-looking statements" provided by the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact are forward-looking statements. Such statements involve inherent risks and uncertainties, many of which are difficult to predict and are generally beyond our control. We caution readers that a number of important factors could cause actual results to differ materially from those expressed in, implied or projected by, such forward-looking statements. Risks and uncertainties include, but are not limited to:

- risks related to our proposed merger with PacWest;
- revenues are lower than expected;
- credit quality deterioration, which could cause an increase in the provision for loan losses;
- competitive pressure among depository institutions increases significantly;
- changes in consumer spending, borrowings and savings habits;
- our ability to successfully integrate acquired entities or to achieve expected synergies and operating efficiencies within expected time-frames or at all;
- a slowdown in construction activity;
- technological changes;
- the cost of additional capital is more than expected;
- the resolution of pending legal matters;
- a change in the interest rate environment reduces interest margins;
- asset/liability repricing risks and liquidity risks;
- general economic conditions, particularly those affecting real estate values, either nationally or in the market areas in which we do or anticipate doing business are less favorable than expected;
- legislative, accounting or regulatory requirements or changes adversely affecting our business;
- the effects of and changes in monetary and fiscal policies and laws, including the interest rate policies of the Board of Governors of the Federal Reserve, or the Federal Reserve Board;
- recent volatility in the credit or equity markets and its effect on the general economy;
- the costs and effects of legal, accounting and regulatory developments;
- regulatory approvals for acquisitions cannot be obtained on the terms expected or on the anticipated schedule; and

- demand for the products or services of First California and the Bank, as well as their ability to attract and retain qualified people.

If any of these risks or uncertainties materializes, or if any of the assumptions underlying such forward-looking statements proves to be incorrect, our results could differ materially from those expressed in, implied or projected by, such forward-looking statements. For information with respect to factors that could cause actual results to differ from the expectations stated in the forward-looking statements, see “Risk Factors” under Part I, Item 1A in our 2012 Annual Report on Form 10-K. We urge investors to consider all of these factors carefully in evaluating the forward-looking statements contained in this Quarterly Report on Form 10-Q. We make these forward-looking statements as of the date of this document and we do not intend, and assume no obligation, to update the forward-looking statements or to update the reasons why actual results could differ from those expressed in, or implied or projected by, the forward-looking statements. All forward-looking statements contained in this document and all subsequent written and oral forward-looking statements attributable to us or any other person acting on our behalf, are expressly qualified by these cautionary statements.

Overview

First California Financial Group, Inc., or First California, or the Company, is a bank holding company which serves the comprehensive banking needs of businesses and consumers in Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Luis Obispo and Ventura counties through our wholly-owned subsidiary, First California Bank, or the Bank. The Bank is a state chartered commercial bank that provides traditional business and consumer banking products through 15 full-service branch locations. The Company also has two unconsolidated statutory business trust subsidiaries, First California Capital Trust I and FCB Statutory Trust I, which raised capital through the issuance of trust preferred securities.

At March 31, 2013, we had consolidated total assets of $1.7 billion, total loans of $1.1 billion, deposits of $1.4 billion and shareholders' equity of $233.5 million. At December 31, 2012, we had consolidated total assets of $1.9 billion, total loans of $1.1 billion, deposits of $1.5 billion and shareholders' equity of $234.1 million.

For the first quarter of 2013, we had net income from continuing operations of $0.4 million, compared with net income from continuing operations of $2.4 million for the first quarter of 2012. The decrease in net income for the first quarter of 2013 was due principally to lower net interest revenues from lower yields on interest-earning assets, higher FDIC shared-loss asset amortization and higher legal, audit and other professional expenses compared to the comparable quarter of 2012.

For the first quarter of 2013, we had net income from discontinued operations of $0.0 million, compared with net income from discontinued operations of $0.2 million for the first quarter of 2012. Revenues from our discontinued EPS division were $2.0 million for the first quarter of 2013 compared with $1.2 million for the same quarter last year. Expenses from our discontinued EPS division were $2.0 million for the first quarter of 2013 compared with $0.8 million for the 2012 first quarter. Revenues increased because of higher transaction volumes compared to the prior period. Expenses increased because of costs associated with the wind down of the division and the planned enforcement action in the 2013 period.

After a dividend payment on our Series C preferred shares of $312,500 in the first quarter of 2013, our net income per diluted common share was $0.00. For the 2012 first quarter, our net income per diluted common share was $0.08 after a dividend payment on our Series C preferred shares of $312,500.

Proposed Merger with PacWest

On November 6, 2012, First California entered into the Merger Agreement with PacWest. Under the terms of the Merger Agreement, the Company will merge with and into PacWest, with PacWest as the surviving corporation, which we refer to as the PacWest Merger. The Merger Agreement also provides that, simultaneously with the PacWest Merger, the Bank will merge with and into Pacific Western Bank, a wholly owned subsidiary of PacWest, with Pacific Western Bank continuing as the surviving bank.

Pursuant to the Merger Agreement, in the PacWest Merger, each outstanding share of common stock of the Company, other than shares held by the Company as treasury stock or by PacWest, will be cancelled and converted into the right to receive a fractional share of PacWest common stock equal to the quotient (which we refer to as the Exchange Ratio) obtained by dividing $8.00 by the volume weighted average closing price of PacWest common stock for a specified period, or the Average PacWest Common Stock Price. However, if the Average PacWest Common Stock Price is greater than or equal to $27.00, then the Exchange Ratio will be 0.2963, and if the Average PacWest Common Stock Price is less than or equal to $20.00, then the Exchange Ratio will be 0.4000.

Immediately prior to the effective time of the PacWest Merger, each option to purchase First California common stock will become fully vested and be cancelled in exchange for the right to receive a cash payment calculated based on the Exchange Ratio, and each share of First California restricted stock will vest and will be converted into the right to receive a number of shares of PacWest common stock equal to the Exchange Ratio.

First California and PacWest have each made customary representations and warranties in the Merger Agreement and agreed to customary covenants, including covenants regarding the operation of the business of First California and its subsidiaries prior to the closing and covenants prohibiting First California from soliciting, providing information or entering into discussions concerning proposals relating to alternative business combination transactions, except in limited circumstances relating to unsolicited proposals that constitute, or are reasonably capable of becoming, a superior proposal.

Consummation of the PacWest Merger is subject to customary closing conditions, including approval of regulatory agencies. The Merger Agreement may be terminated under certain circumstances, including by either party if the PacWest Merger has not occurred by August 6, 2013, if an order is entered prohibiting or making illegal the transaction and the order has become final and non-appealable, or upon a material uncured breach by the other party that would cause the closing conditions not to be satisfied.

The Merger Agreement provides certain termination rights for both First California and PacWest and further provides that upon termination of the Merger Agreement under certain circumstances, PacWest will be obligated to pay First California a termination fee of $5,000,000 and under certain circumstances, First California will be obligated to pay PacWest a termination fee of $10,000,000.

Upon consummation of the PacWest Merger, the Board of Directors of PacWest will consist of the directors serving on the Board of Directors of PacWest prior to the effective time of the PacWest Merger plus two independent directors designated by the Board of Directors of First California and approved by the Compensation, Nominating and Governance Committee of PacWest.

On February 13, 2013, the Board of Directors of the Company and the Board of Directors of the Bank committed to a plan to wind down the EPS division. The Company previously announced on November 6, 2012, that the Company and PacWest entered into a Merger Agreement pursuant to which the Company would merge with and into PacWest, with PacWest as the surviving corporation. As previously disclosed in the amended Registration Statement on Form S-4 of PacWest, PacWest concluded that the EPS division was not suited to PacWest's commercial banking business model and PacWest would proceed to exit the EPS division upon completion of the PacWest Merger. In connection with the plan to discontinue the EPS division, we evaluated the core deposit intangible and customer relationship intangible assets related to the EPS division and determined that the full amount of both intangible assets was not recoverable and we recorded a pre-tax impairment charge of $4.8 million in December 2012. We have targeted December 31, 2013 for substantial completion of the wind down of the EPS division. Therefore, we present the results of operations of the EPS division as "discontinued operations" for all periods presented.

Critical accounting policies

We base our discussion and analysis of our consolidated results of operations and financial condition on our unaudited consolidated interim financial statements and our audited consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities, income and expense, and the related disclosures of contingent assets and liabilities at the date of these consolidated financial statements. We believe these estimates and assumptions to be reasonably accurate; however, actual results may differ from these estimates under different assumptions or circumstances. The following are our critical accounting policies and estimates.

Allowance for loan losses

We establish the allowance for loan losses through a provision charged to expense. We charge-off loan losses against the allowance when we believe that the collectability of the loan is unlikely. The allowance is an amount that we believe will be adequate to absorb probable losses on existing loans that may become uncollectible, based on evaluations of the collectability of loans and prior loan loss experience. Our evaluation includes an assessment of the following factors: any external loan review and any regulatory examination, estimated probable loss exposure on each pool of loans, concentrations of credit, value of collateral, the level of delinquent and nonaccrual loans, trends in the portfolio volume, effects of any changes in the lending policies and procedures, changes in lending personnel, present economic conditions at the local, state and national levels, the amount of undisbursed off-balance sheet commitments, and a migration analysis of historical losses and recoveries for the prior twenty quarters. We also evaluate individual loans for impairment and if a portion of a loan is impaired, we charge-off the impaired amount or allocate a specific reserve for that loan. Various regulatory agencies, as a regular part of their examination process, periodically review our allowance for loan losses. Such agencies may require us to recognize additions to the allowance based on their judgment of information available to them at the time of their examinations. The allowance for loan losses was $18.3 million at March 31, 2013 and was $18.2 million at December 31, 2012.

Non-covered foreclosed property

We acquire, through foreclosure or through full or partial satisfaction of a loan, real or personal property. At the time of foreclosure, the Company obtains an appraisal of the property and records the property at its estimated fair value less costs to sell. We charge the allowance for loan losses for the loan amount in excess of the fair value of the foreclosed property received; we credit earnings for the fair value amount of the foreclosed property in excess of the loan due. Subsequent to foreclosure, the Company periodically assesses our disposition efforts and the estimated fair value of the foreclosed property. The Company establishes a valuation allowance through a charge to earnings for estimated declines in fair value subsequent to foreclosure. Operating income and operating expense related to foreclosed property is included in earnings as are any ultimate gains or losses on the sale of the foreclosed property. Our recognition of gain is however dependent on the buyer's initial investment in the purchase of foreclosed property meeting certain criteria. The estimated lower of cost or market value of non-covered foreclosed property was $14.2 million at March 31, 2013 and $14.9 million at December 31, 2012.

Covered foreclosed property

All foreclosed property acquired in FDIC-assisted acquisitions that are subject to a FDIC shared-loss agreement are referred to as "covered foreclosed property" and reported separately in our consolidated balance sheets. We report covered foreclosed property exclusive of expected reimbursement cash flows from the FDIC. We transfer foreclosed covered loan collateral into covered foreclosed property at the collateral's net realizable value, less estimated selling costs. We initially recorded covered foreclosed property at its estimated fair value on the acquisition date based on similar market comparable valuations less estimated selling costs. We charge any subsequent valuation adjustments due to declines in fair value to non-interest expense, and we recognize a corresponding increase to the FDIC shared-loss asset for the reimbursable loss amount.

We credit any recoveries of previous valuation adjustments to non-interest expense, and we recognize a corresponding increase to the FDIC shared-loss asset for the portion of the recovery due to the FDIC. The estimated fair value of covered foreclosed property was $2.9 million at March 31, 2013 and $3.9 million at December 31, 2012.

Deferred income taxes

We recognize deferred tax assets subject to our judgment that realization of such assets are more-likely-than-not. A valuation allowance is established when the Company determines that the realization of income tax benefits may not occur in future years. There was no valuation allowance at March 31, 2013 or December 31, 2012. There were net deferred tax assets of $1.5 million at March 31, 2013 and $1.4 million at December 31, 2012.

FDIC shared-loss asset

We initially recorded the FDIC shared-loss asset at fair value, based on the discounted value of expected future cash flows under the shared-loss agreements. We accrete into noninterest income over the life of the FDIC shared-loss asset the difference between the present value and the undiscounted cash flows the Company expects to collect from the FDIC. Subsequent to initial recognition, we review quarterly the FDIC shared-loss asset and adjust for any changes in expected cash flows based on recent performance and expectations for future performance of the covered portfolio. We measure these adjustments on the same basis as the related covered loans, at a pool level, and covered foreclosed property. Generally, any increases in cash flow of the covered assets over those previously expected will result in prospective increases in the loan pool yield and amortization of the FDIC shared-loss asset. Any decreases in cash flow of the covered assets under those previously expected will trigger impairments on the underlying loan pools and will result in a corresponding gain on the FDIC shared-loss asset. We record increases and decreases to the FDIC shared-loss asset as adjustments to non-interest income. The FDIC shared-loss asset was $40.9 million at March 31, 2013 and $45.3 million at December 31, 2012.

FDIC shared-loss liability

Forty-five days following the tenth anniversary of the WCB and SLTB acquisition dates, we will be required to perform a calculation and determine if a payment to the FDIC is necessary. The payment amount will be 50 percent of the excess, if any, of (i) 20 percent of the intrinsic loss estimate minus (ii) the sum of (a) 20 percent of the net loss amount, plus (b) 25 percent of the asset discount bid, plus (c) 3.5 percent of total loss share assets at acquisition. Our estimate for the present value of this liability was $4.0 million at March 31, 2013 and $3.9 million at December 31, 2012.

Derivative instruments and hedging

For derivative instruments designated in cash flow hedging relationships, we assess the effectiveness of the instruments in offsetting changes in the overall cash flows of the designated hedged transactions on a quarterly basis. We recognize the unrealized gains or losses of derivative instruments directly in current period earnings to the extent these instruments are not effective. At March 31, 2013, we had $37.1 million notional interest rate caps to limit the variable interest rate payments on our $26.8 million junior subordinated debentures. Our 2013 first quarter effectiveness assessment indicated that these instruments were effective.

At March 31, 2013, the Bank had $240 million notional interest rate caps that do not meet the criteria for hedge accounting to manage the interest rate risk associated with its fixed rate securities and loans. Derivatives not designated as hedges are marked-to-market each period through earnings. The estimated fair value of these interest rate caps was $72,000 at March 31, 2013 and $76,000 at December 31, 2012.

Assessments of impairment

We assess goodwill for impairment on an annual basis as of December 31, or at interim periods if an event occurs or circumstances change which may indicate a change in the implied fair value of the goodwill. We estimate the implied fair value of goodwill by comparing the estimated fair value of the Company to the estimated fair value of the Company's individual assets, liabilities, and identifiable intangible assets. Impairment exists when the carrying amount of goodwill exceeds this implied fair value. No events occurred or circumstances changed since December 31, 2012, which indicated there was a change in the implied fair value of the goodwill.

We also undertake an impairment analysis on our debt and equity securities each quarter. When we do not intend to sell, and it is more likely than not that we are not required to sell, a debt security before recovery of its cost basis, we separate other-than-temporary impairment into (a) the amount representing credit loss and (b) the amount related to other factors. We recognize in earnings the amount of the other-than-temporary impairment related to credit loss. We recognize in other comprehensive income the amount of other-than-temporary impairment related to other factors. Our assessment of other-than-temporary declines in fair value considers the duration the security has been in a continuous unrealized loss position, the severity of the decline in value, the rating of the security, and the long-term financial outlook of the issuer. In addition, we consider the expected future cash flows from the security and our ability and intent to hold the security until the fair value recovers.

There was no other-than-temporary impairment loss for the three months ended March 31, 2013. For the three months ended March 31, 2012, we recognized a permanent impairment loss of $28,000 on a $1.0 million community development-related equity investment.

Results of operations – for the three months ended March 31, 2013 and 2012

Net interest income

Our earnings are derived predominantly from net interest income, which is the difference between interest and fees earned on loans, securities and federal funds sold (these asset classes are commonly referred to as interest-earning assets) and the interest paid on deposits, borrowings and debentures (these liability classes are commonly referred to as interest-bearing funds). The net interest margin is net interest income divided by average interest-earning assets.

Our net interest income for the three months ended March 31, 2013 decreased to $14.0 million from $16.2 million for the same period last year. The decrease in net interest income for the three month period reflects lower yields on interest-earning assets. Interest income on loans for the 2013 first quarter was $15.3 million, down $1.7 million from $17.0 million for the 2012 first quarter. Interest expense for the 2013 first quarter was $1.8 million, down $0.8 million from $2.6 million for the 2012 first quarter. The decrease in interest expense for the three month period was due to lower average balances of interest-bearing liabilities and lower rates paid on interest-bearing deposits and borrowings.

Our net interest margin (tax equivalent) for the first quarter of 2013 was 3.58 percent compared with 4.14 percent for the same quarter last year. The decline in our first quarter net interest margin was due primarily to a decline in the yields on interest-earning assets. The yield on interest-earning assets for the first quarter of 2013 was 4.04 percent, down 76 basis points from 4.80 percent for the first quarter a year ago. The cost of our interest-bearing liabilities was 0.75 percent for the 2013 first quarter, down 20 basis points from 0.95 percent for the first quarter a year ago.

The following tables present the distribution of our average assets, liabilities and shareholders' equity in combination with the total dollar amounts of interest income from average interest earning assets and the resultant yields, and the dollar amounts of interest expense and average interest bearing liabilities, expressed in both dollars and rates for the three months ended March 31, 2013 and 2012.

Average Balance Sheet and Analysis of Net Interest Income

	Three months ended March 31,					
	2013			2012		
(dollars in thousands)	Average Balance	Interest Income/ Expense	Weighted Average Yield/Rate	Average Balance	Interest Income/ Expense	Weighted Average Yield/Rate
Loans (1)	$1,145,353	$15,280	5.41 %	$1,097,748	$16,990	6.22 %
Securities	372,636	521	0.58 %	445,698	1,771	1.66 %
Federal funds sold and deposits with banks	76,687	59	0.31 %	37,359	36	0.39 %
Total earning assets	1,594,676	$15,860	4.04 %	1,580,805	$18,797	4.80 %
Non-earning assets	226,856			276,047		
Total average assets	$1,821,532			$1,856,852		

Interest bearing checking	$115,323	$48	0.17	%	$105,684	$54	0.21	%
Savings and money market	460,804	452	0.40	%	493,472	659	0.54	%
Certificates of deposit	261,861	553	0.86	%	347,503	658	0.76	%
Total interest bearing deposits	837,988	1,053	0.51	%	946,659	1,371	0.58	%
Borrowings	107,089	612	2.32	%	131,104	944	2.90	%
Junior subordinated debentures	26,805	149	2.21	%	26,805	313	4.67	%
Total borrowed funds	133,894	761	2.29	%	152,625	1,257	3.19	%
Total interest bearing liabilities	971,882	$1,814	0.75	%	1,104,568	$2,628	0.95	%
Noninterest checking	605,498				502,340			
Other liabilities	10,112				24,366			
Shareholders' equity	234,040				225,578			
Total liabilities and shareholders' equity	$1,821,532				$1,856,852			
Net interest income		$14,046				$16,169		
Net interest margin (tax equivalent) (2)			3.58	%			4.14	%

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(1) Yields and amounts earned on loans include loan fees and discount/premium accretion of $1.1 million and $1.6 million for the three months ended March 31, 2013 and 2012, respectively. Yields and amounts earned on loans include interest income (discount accretion) on covered loans of $3.4 million and $4.2 million for the three months ended March 31, 2013 and 2012, respectively. The average loan balance includes nonaccrual loans; however, there is no interest income related to nonaccrual loans in the amount earned on loans. Average nonaccrual loans were $16.2 million and $14.5 million for the respective periods.

(2) Includes tax equivalent adjustments primarily related to tax-exempt income on securities.

Our net interest income changes with the level and mix of average interest-earning assets and average interest-bearing funds. We call the changes between periods in interest-earning assets and interest-bearing funds balance changes. We measure the effect on our net interest income from balance changes by multiplying the change in the average balance between the current period and the prior period by the prior period average rate.

Our net interest income also changes with the average rate earned or paid on interest-earning assets and interest-bearing funds. We call the changes between periods in average rates earned and paid rate changes. We measure the effect on our net interest income from rate changes by multiplying the change in average rates earned or paid between the current period and the prior period by the prior period average balance.

We allocate the change in our net interest income attributable to both balance and rate on a pro rata basis to the change in average balance and the change in average rate. The following table presents the change in our interest income and interest expense.

Increase (Decrease) in Net Interest Income/Expense Due to Change in Average Volume and Average Rate (1)

	Three months ended March 31, 2013 to 2012 due to:		
(in thousands)	Rate	Volume	Total
Interest income			
Interest on loans (2)	$(2,449)	$739	$(1,710)
Interest on securities	(960)	(290)	(1,250)
Interest on Federal funds sold and deposits with banks	(15)	38	23
Total interest income	(3,424)	487	(2,937)
Interest expense			
Interest on deposits	162	156	318
Interest on borrowings	161	171	332
Interest on junior subordinated debentures	164	—	164
Total interest expense	487	327	814
Net interest income	$(2,937)	$814	$(2,123)

(1) We allocated the change in interest income or interest expense that is attributable to both changes in average balance and average rate to the changes due to (i) average balance and (ii) average rate in proportion to the

relationship of the absolute amounts of changes in each.

(2) Table does not include interest income that would have been earned on nonaccrual loans.

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Provision for loan losses

There was no provision for loan losses for the three months ended March 31, 2013 compared with $0.5 million for the same period in 2012. The provision for loan losses declined from the prior period because of the improvement in the mix of loans and credit quality. The provision for loan losses relates to the non-covered loan portfolio; there was no provision required for the covered loan portfolio for the three months ended March 31, 2013 or 2012 as there was no credit deterioration beyond that estimated at the date of acquisition.

Noninterest income

Noninterest income was negative $0.1 million for the 2013 first quarter compared with $1.2 million for the same period a year ago. The decrease for the three-month period was largely due to increased amortization of the FDIC shared-loss asset.

The following table presents a summary of noninterest income:

	For the three months ended March 31,			
	2013		2012	
	(in thousands)			
Service charges on deposit accounts	$	800	$	831
Loan sales and commissions		34		50
Earnings on cash surrender value of life insurance		101		107
Net gain on sale of securities		450		1
Impairment loss on securities		—		(28)
Loss on non-hedged derivatives		(3)		(111)
(Amortization) accretion of FDIC shared-loss asset		(1,707)		191
Other income		233		194
Total noninterest income	$	(92)	$	1,235

Our service charges on deposit accounts for the three months ended March 31, 2013 was $0.8 million, the same amount as for the three months ended March 31, 2012.

In the first quarter of 2013, we sold $0.4 million of U.S. Small Business Administration, or SBA, loans and realized gains of $34,000. For the first quarter of 2012, we sold $0.5 million of SBA loans and realized gains of $50,000.

In the first quarter of 2013, we sold $53.2 million of securities and realized net gains of $450,000. In the first quarter of 2012, we sold $8.0 million of securities and realized net gains of $1,000.

There was no other-than-temporary impairment loss on securities for the three months ended March 31, 2013. For the three months ended March 31, 2012, we recognized an impairment loss of $28,000 on a $1.0 million community development-related equity investment. We will continue to evaluate our securities portfolio for other-than-temporary impairment at each reporting date and we can provide no assurance there will not be other impairment losses in future periods.

At the end of the 2013 first quarter, the Bank had a $240 million notional amount portfolio of one-year interest rate caps. At March 31, 2013, $210 million were forward-starting and not yet effective. The estimated fair value of these interest rate caps were $72,000 at March 31, 2013 and $76,000 at December 31, 2012. We recognized a loss on non-hedged derivatives of $3,000 in the three months ended March 31, 2013 and a loss of $111,000 on non-hedged derivatives in the first three months of 2012.

Amortization of the FDIC shared-loss asset was $1.7 million for the three months ended March 31, 2013 compared with accretion of $0.2 million for the comparable period in 2012. The increased amortization in 2013 was the result of lower estimated claims to be paid by the FDIC related to our shared-loss agreements.

Other income for the three months ended March 31, 2013 and March 31, 2012 was $0.2 million.

Noninterest expense

Our noninterest expense for the three months ended March 31, 2013 was $13.3 million compared to $13.0 million for the three months ended March 31, 2012.

Salaries and employee benefits for the 2013 first quarter decreased $0.7 million, or 9 percent, to $6.8 million from $7.5 million for the 2012 first quarter. The decrease primarily reflects workforce reductions from the closing of four branches at the beginning of the 2012 third quarter. Full-time equivalent employees were 263 at March 31, 2013 compared with 296 at March 31, 2012.

Legal, audit and other professional expense for the 2013 first quarter increased $1.0 million, or 113 percent, to $1.9 million from $0.9 million for the 2012 first quarter. The increase primarily reflects increased legal and professional expense related to our pending merger with PacWest and increased compliance costs.

The following table presents a summary of noninterest expense:

	For the three months ended March 31,	
	2013	2012
	(in thousands)	
Salaries and employee benefits	$6,786	$7,486
Premises and equipment	1,388	1,504
Data processing	937	790
Legal, audit, and other professional services	1,946	915
Printing, stationery, and supplies	33	77
Telephone	202	210
Directors' expense	116	129
Advertising, marketing and business development	268	459
Postage	45	56
Insurance and regulatory assessments	583	452
Net (gain) loss on and expense of foreclosed property	(334)	(245)
Amortization of intangible assets	376	431
Other expenses	934	721
Total noninterest expense	$13,280	$12,985

Our efficiency ratio was 92 percent for the first quarter of 2013 compared with 72 percent for the first quarter of 2012. The efficiency ratio is the percentage relationship of noninterest expense, excluding amortization of intangibles, (gain) loss on and expense of foreclosed property and integration/conversion expenses, to the sum of net interest income and noninterest income, excluding gains or losses on securities and gains on acquisitions.

Income taxes

The income tax provision was $0.3 million for the three months ended March 31, 2013 compared with $1.6 million for the same period in 2012. The combined federal and state effective tax rate for the three months ended March 31, 2013 was 42.0 percent compared with 40.0 percent for the same period in 2012.

Financial position – March 31, 2013 compared with December 31, 2012

Lending and credit risk

We provide a variety of loan and credit-related products and services to meet the needs of borrowers primarily located in the seven Southern California counties where our branches are located. Business loans, represented by commercial real estate loans, commercial loans and construction loans comprise the largest portion of the loan portfolio. Consumer or personal loans, represented by home mortgage, home equity and installment loans, comprise a smaller portion of the loan portfolio.

Credit risk is the risk to earnings or capital arising from an obligor's failure to meet the terms of any contract with us or otherwise to perform as agreed. All activities in which success depends on counterparty, issuer, or borrower performance have credit risk. Credit risk is present any time we extend, commit or invest funds; whenever we enter into actual or implied contractual agreements for funds, whether on or off the balance sheet, credit risk is present.

All categories of loans present credit risk. Major risk factors applicable to all loan categories include changes in international, national and local economic conditions such as interest rates, inflation, unemployment levels, consumer and business confidence and the supply and demand for goods and services.

Commercial real estate loans rely upon the cash flow originating from the underlying real property. Commercial real estate is a cyclical industry; general economic conditions and local supply and demand affect the commercial real estate industry. In the office sector, the demand for office space is highly dependent on employment levels. Consumer spending and confidence affect the demand for retail space and the levels of retail rents in the retail sector. The industrial sector has exposure to the level of exports, defense spending and inventory levels. Vacancy rates, location and other factors affect the amount of rental income for commercial property. Tenants may relocate, fail to honor their lease or go out of business. In the multifamily residential sector, the affordability of ownership housing, employment conditions and the vacancy of existing inventory heavily influences the demand for apartments. Population growth or decline and changing demographics, such as increases in the level of immigrants or retirees, are also factors influencing the multifamily residential sector.

Construction loans provide developers or owners with funds to build or improve properties; developers ultimately sell or lease these properties. Generally, construction loans involve a higher degree of risk than other loan categories because they rely upon the developer's or owner's ability to complete the project within specified cost and time limits. Cost overruns can cause the project cost to exceed the project sales price or exceed the amount of the committed permanent funding. Any number of reasons, such as poor weather, material or labor shortages, labor difficulties, or redoing substandard work to pass inspection, can delay construction projects. Furthermore, changes in market conditions or credit markets may affect a project's viability once completed.

Commercial loans rely upon the cash flow originating from the underlying business activity of the enterprise. The manufacture, distribution or sale of goods or sale of services are not only affected by general economic conditions but also by the ability of the enterprise's management to adjust to local supply and demand conditions, maintain good labor, vendor and customer relationships, as well as market, price and sell their goods or services for a profit. Customer demand for goods and services of the enterprise may change because of competition or obsolescence.

Home mortgages and home equity loans and lines of credit use first or second trust deeds on a borrower's real estate property, typically their principal residence, as collateral. These loans depend on a person's ability to regularly pay the principal and interest due on the loan and, secondarily, on the value of real estate property that serves as collateral for the loan. Generally, home mortgages involve a lower degree of risk than other loan categories because of the relationship of the loan amount to the value of the residential real estate and a person's reluctance to forego their principal place of residence. General economic conditions and local supply and demand, however, affect home real estate values. Installment loans and credit card lines also depend on a person's ability to pay principal and interest on a loan; however, generally these are unsecured loans or, if secured, the collateral value can rapidly decline, as is the case for automobiles. A person's ability to service debt is highly dependent upon their continued employment or financial stability. Job loss, divorce, illness and bankruptcy are just a few of the risks that may affect a person's ability to service their debt.

We obtain appraisals when extending credit for real estate secured loans as follows:

1. All business loans in excess of $1,000,000 where real estate will be taken as collateral but where the sale or rental of the real estate is not the primary source of repayment;

2. All business loans in excess of $250,000 where real estate will be taken as collateral and where the sale or rental of the real estate is the primary source of repayment; and

3. All other real estate secured loans in excess of $250,000.

All real estate secured loans, at the time of origination, renewal or extension, require a current appraisal. A current appraisal is an appraisal with an "as of" date not more than six months before the date of funding or renewal or extension. We also obtain updated appraisals when the useful life of the appraisal ceases. Under the Uniform Standards of Professional Appraisal Practice guidelines, the useful life of an appraisal, regardless of the dollar amount, is the life of the loan. However, useful life ends when (a) there has been a deterioration in the borrower's performance and there is an increasing likelihood of a forced liquidation of the property and the existing appraisal is older than two years old, or (b) there has been deterioration in the property's value due to a significant depreciation in local real estate values, lack of maintenance, change in zoning, environmental contamination or other circumstances.

Since the risks in each category of loan changes based on a number of factors, it is not possible to state whether a particular type of lending carries with it a greater or lesser degree of risk at any specific time in the economic cycle. Generally, in a stabilized economic environment, home mortgage loans have the least risk, followed by home equity loans, multifamily property loans, commercial property loans, commercial loans and lines and finally construction loans. However, this ordering may vary from time to time and the degree of risk from the credits with the least risk to those with the highest risk profile may expand or contract with the general economy.

We manage credit risk through Board-approved policies and procedures. At least annually, the Board of Directors reviews and approves these policies. Lending policies provide us with a framework for consistent loan underwriting and a basis for sound credit decisions. Lending policies specify, among other things, the parameters for the type or purpose of the loan, the required debt service coverage and the required collateral requirements. Credit limits are also established. Management’s Loan Committee meets regularly to approve certain loans, monitors delinquencies and reports quarterly to the Director’s Credit Review Committee on compliance with policies. The Directors’ Audit Committee also engages a third party to perform a credit review of the loan portfolio to ensure compliance with policies and assist in the evaluation of the credit risk inherent in the loan portfolio.

Non-covered Loans

Non-covered loans decreased $31.0 million, or 3 percent, to $1.0 billion at March 31, 2013 from $1.1 billion at December 31, 2012. Commercial loans and lines and home mortgage loans experienced the largest declines for the period.

(in thousands)	At March 31, 2013	At December 31, 2012
Commercial mortgage	$449,747	$447,689
Multifamily mortgage	210,185	217,158
Commercial loans and lines of credit	152,812	168,325
Home mortgage	136,941	149,954
Construction and land development	39,119	36,772
Home equity loans and lines of credit	37,206	36,709
Installment and credit card	4,157	4,586
Total loans	1,030,167	1,061,193
Allowance for loan losses	(18,271)	(18,172)
Loans, net	$1,011,896	$1,043,021

The loan categories above are derived from bank regulatory reporting standards for loans secured by real estate; however, a portion of the mortgage loans above are loans that we consider to be a commercial loan for which we have taken real estate collateral as additional support or from an abundance of caution. In these instances, we are not looking to the real property as its primary source of repayment, but rather as a secondary or tertiary source of repayment.

Commercial mortgage loans, the largest segment of our portfolio, were 44 percent of total non-covered loans at March 31, 2013, compared to 42 percent at December 31, 2012. Our commercial mortgage portfolio consisted of 420 loans with an average balance of $1,071,000 at March 31, 2013. Many different commercial property types collateralize our commercial mortgage loans. Our top three categories have historically been office, industrial, and retail. In addition, most of our commercial property lending is in the seven Southern California counties where our branches are located. The following is a table of our non-covered commercial mortgage lending by county.

Non-covered commercial mortgage loans by region/county (in thousands)	At March 31, 2013	At December 31, 2012
Southern California		
Los Angeles	$202,234	$204,256
Orange	31,626	32,291
Ventura	121,936	117,785
Riverside	34,730	35,398
San Bernardino	13,939	13,977
San Diego	17,248	15,696
Santa Barbara	7,571	7,613
Total Southern California	429,284	427,016

Northern California		
Alameda	338	339
Contra Costa	236	329
Fresno	2,361	2,364
Imperial	312	317
Kern	114	133
Madera	500	505
Placer	588	591
Sacramento	311	314
San Luis Obispo	15,168	15,244
Solano	256	257
Tulare	279	280
Total Northern California	20,463	20,673
Total non-covered commercial mortgage loans	$449,747	$447,689

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The following table shows the distribution of our non-covered commercial mortgage loans by property type.

Non-covered commercial mortgage loans by property type (in thousands)	At March 31, 2013	At December 31, 2012
Industrial/warehouse	$106,191	$106,288
Office	100,262	97,316
Retail	84,351	85,862
Mixed use	29,262	29,468
Medical	23,324	23,543
Hotel	18,046	18,167
Self storage	14,751	14,814
Restaurant	11,351	11,448
Assisted living	6,925	6,967
All other	55,284	53,816
Total non-covered commercial mortgage loans	$449,747	$447,689

The following table shows the maturity of our non-covered commercial mortgage loans by origination year.

Non-covered commercial mortgage loans by origination year/maturity year
(in thousands)

	Year of maturity					
Origination Year	2013	2014	2015	2016	2017 and Thereafter	Total
2009 and earlier	$9,263	$29,936	$3,822	$3,404	$189,211	$235,636
2010	21	—	2,750	—	24,820	27,591
2011	51	—	—	—	48,359	48,410
2012	4,423	519	—	—	122,820	127,762
2013	263	—	—	88	9,997	10,348
Total	$14,021	$30,455	$6,572	$3,492	$395,207	$449,747

We generally underwrite commercial mortgage loans with a maximum loan-to-value of 60 percent and a minimum debt service coverage ratio of 1.25. The weighted average loan-to-value percentage of our commercial real estate portfolio was 59.3 percent and the weighted average debt service coverage ratio was 1.91 at March 31, 2013. We focus on cash flow; consequently, regardless of the value of the collateral, the commercial real estate project must provide sufficient cash flow, or alternatively the principals must supplement the project with other cash flow, to service the debt. We generally require the principals to guarantee the loan. We also "stress-test" commercial mortgage loans to determine the potential effect changes in interest rates, vacancy rates, and lease or rent rates would have on the cash flow of the project. Additionally, at least on an annual basis, we require updates on the cash flow of the project and, where practicable, we visit the properties.

Multifamily mortgage loans represent the next largest category of non-covered loans and were 20 percent of total non-covered loans at March 31, 2013, the same as at December 31, 2012. Our multifamily loan portfolio consisted of 186 loans with an average balance of $1,116,000 at March 31, 2013. Apartments mostly located in our seven-county market area serve as collateral for our multifamily mortgage loans. We underwrite multifamily mortgage loans in a fashion similar to commercial mortgage loans previously described. The weighted average loan-to-value percentage was 61.8 percent and the weighted average debt service coverage ratio was 1.49 for our multifamily portfolio at March

31, 2013. Below is a table of our non-covered multifamily mortgage loans by county.

Non-covered multifamily mortgage loans by region/county (in thousands)	At March 31, 2013	At December 31, 2012
Southern California		
Los Angeles	$116,678	$122,292
Orange	5,445	5,472
Ventura	11,693	11,757
Riverside	1,363	1,368
San Bernardino	6,216	6,242
San Diego	17,968	18,976
Santa Barbara	4,077	4,095
Total Southern California	163,440	170,202
Northern California		
Alameda	2,825	2,837
Calaveras	1,330	1,330
Contra Costa	600	602
Fresno	231	233
Kern	2,420	2,444
Merced	635	638
Monterey	366	368
Mono	218	219
Napa	14,857	14,925
San Francisco	5,638	5,664
San Mateo	1,361	1,369
Santa Clara	15,934	15,996
Santa Cruz	330	331
Total Northern California	46,745	46,956
Total non-covered multifamily mortgage loans	$210,185	$217,158

The following table shows the maturity of our non-covered multifamily mortgage loans by origination year.

Non-covered multifamily mortgage loans by origination year/maturity year
(in thousands)

Origination Year	Year of maturity 2013	2014	2015	2016	2017 and Thereafter	Total
2009 and earlier	$1,078	$1,090	$—	$—	$70,501	$72,669
2010	—	—	—	—	8,246	8,246
2011	—	—	—	—	63,462	63,462
2012	763	—	—	—	63,413	64,176
2013	—	—	—	—	1,632	1,632
Total	$1,841	$1,090	$—	$—	$207,254	$210,185

Commercial loans represent the next largest category of loans and were 15 percent of total non-covered loans at March 31, 2013, down from 16 percent at December 31, 2012. Our commercial loan portfolio consisted of 682 loans with an average balance of $223,000 at March 31, 2013. Unused commitments on commercial loans were $131.9 million at March 31, 2013 compared with $127.6 million at December 31, 2012. Working capital, equipment purchases or business expansion are the typical purposes for commercial loans. Commercial loans may be unsecured or secured by assets such as equipment, inventory, accounts receivables, and real property. Personal guarantees of the business owner may also be present. These loans may also have partial guarantees from the SBA or other federal or state agencies. Broadly diversified business sectors with the largest sectors in real estate/construction, finance and insurance, healthcare, manufacturing and professional services comprise the commercial loan portfolio. We also participate in larger credit facilities known as shared national credits. At March 31, 2013, five loans under these facilities had outstanding balances of $12.7 million. These loans consist of motion picture and video production loan participations. Below is a table of our non-covered commercial loans by business sector.

Non-covered commercial loans by industry/sector (in thousands)	At March 31, 2013	At December 31, 2012
Real estate	$50,545	$54,164
Services	39,304	40,428
Information	21,434	27,509
Manufacturing	17,705	15,365
Trade	12,895	17,641
Healthcare	8,973	11,066
Transportation and warehouse	1,852	2,152
Other	104	—
Total non-covered commercial loans	$152,812	$168,325

We generally underwrite commercial loans with maturities not to exceed seven years and we generally require full amortization of the loan within the term of the loan. We underwrite traditional working capital lines for a 12 month period and have a 30-day out-of-debt requirement. Accounts receivable and inventory financing revolving lines of credit have an annual maturity date, a maximum advance rate, and an annual field audit for lines of $200,000 or more. Third-party vendors perform field audits for our accounts receivable and inventory financing revolving lines of credit. The maximum advance rate for accounts receivable is 80 percent and the maximum advance rate for eligible inventory is 25 percent.

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Explanation of Responses:

Construction and land loans represent 4 percent of total non-covered loans at March 31, 2013, up from 3 percent at December 31, 2012. Our construction and land portfolio consisted of 29 loans with an average commitment of $1,788,000 at March 31, 2013. Construction loans represent single-family, multifamily and commercial building projects as well as land development loans. Construction loans are typically short term, with maturities ranging from 12 to 18 months. The maximum loan-to-value is 70 percent for both commercial and residential projects. The weighted average loan-to-value ratio for our construction and land portfolio was 70.3 percent at March 31, 2013. At the borrower's expense, we use a third party vendor for funds control, lien releases and inspections. In addition, we regularly monitor the marketplace and the economy for evidence of deterioration in real estate values.

Below is a table of our non-covered construction and land loans by county.

Non-covered construction/land loans by county (in thousands)	At March 31, 2013 Commitment	At March 31, 2013 Outstanding	At December 31, 2012 Commitment	At December 31, 2012 Outstanding
Los Angeles	$25,138	$16,941	$25,363	$14,692
Orange	4,064	1,164	1,215	1,068
Ventura	17,979	17,046	22,407	17,888
Riverside	3,297	2,583	2,545	1,732
San Luis Obispo	150	145	22,184	149
Santa Barbara	1,238	1,240	1,872	1,243
Total non-covered construction and land loans	$51,866	$39,119	$75,586	$36,772

The table below illustrates the weighted average distribution of our non-covered loan portfolio by loan size at March 31, 2013. We distributed all loans by loan balance outstanding except for construction loans, which we distributed by loan commitment. At March 31, 2013, 37 percent of our loans were less than $1 million and 82 percent of our loans were less than $5 million. We believe the high number of smaller-balance loans aids in the mitigation of credit risk; however, a prolonged and deep recession can affect a greater number of borrowers.

At March 31, 2013	Less than $ 500,000	$ 500,000 to $ 999,999	$ 1,000,000 to $ 2,999,999	$ 3,000,000 to $ 4,999,999	$ 5,000,000 to $ 9,999,999	$ 10,000,000 to $ 12,500,000
Commercial mortgage	10 %	16 %	37 %	16 %	16 %	5 %
Commercial loans and lines of credit	30 %	17 %	30 %	14 %	9 %	– %
Construction and land development	4 %	10 %	20 %	13 %	53 %	– %
Multifamily mortgage	8 %	23 %	44 %	5 %	14 %	6 %
Home mortgage	41 %	32 %	19 %	– %	8 %	– %
Home equity loans and lines of credit	33 %	12 %	17 %	8 %	– %	30 %
Installment and credit card	85 %	15 %	– %	– %	– %	– %
Weighted average totals	18 %	19 %	34 %	11 %	14 %	4 %
Number	1,864	277	213	32	22	4

Allowance for non-covered loan losses

We maintain an allowance for loan losses to provide for inherent losses in the non-covered loan portfolio. We establish the allowance through a provision charged to expense. We charge-off all loans judged uncollectible against the allowance while we credit any recoveries on loans to the allowance. We charge-off commercial and real estate loans – construction, commercial mortgage, and home mortgage – by the time their principal or interest becomes 120 days delinquent unless the loan is well-secured and in the process of collection. We charge-off consumer loans when they become 90 days delinquent unless they too are well secured and in the process of collection. We also charge-off deposit overdrafts when they become more than 60 days old.

We evaluate impaired loans on a case-by-case basis to determine the ultimate loss potential to us after considering the proceeds realizable from a sale of collateral. In those cases where the collateral value is less than the loan, we charge-off the loan to reduce the balance to a level equal to the net realizable value of the collateral. We consider a loan impaired when, based on current information and events, we do not expect to be able to collect all amounts due according to the loan contract, including scheduled interest payments.

Our loan policy provides procedures designed to evaluate and assess the risk factors associated with our loan portfolio, to enable us to assess such risk factors prior to granting new loans and to evaluate the sufficiency of the allowance for non-covered loan losses. We assess the allowance on a monthly basis and undertake a more critical evaluation quarterly. At the time of the monthly review, the Board of Directors will examine and formally approve the adequacy of the allowance. The quarterly evaluation includes an assessment of the following factors: any external loan review and any regulatory examination, estimated probable loss exposure on each pool of loans, concentrations of credit, value of collateral, the level of delinquency and nonaccruals, trends in the portfolio volume, effects of any changes in the lending policies and procedures, changes in lending personnel, present economic conditions at the local, state and national level, the amount of undisbursed off-balance sheet commitments, and a migration analysis of historical losses and recoveries for the prior twenty quarters.

Our evaluation of the adequacy of the allowance for loan losses includes a review of individual non-covered loans to identify specific probable losses and assigns estimated loss factors to specific groups or types of non-covered loans to calculate possible losses. In addition, we estimate the probable loss on previously accrued but unpaid interest. We refer to these as quantitative considerations. Our evaluation also considers subjective factors such as changes in local and regional economic and business conditions, financial improvement or deterioration in business sectors and industries, changes in lending practices, changes in personnel, changes in the volume and level of past due and nonaccrual non-covered loans and concentrations of credit. We refer to these as qualitative considerations.

Our 2013 first quarter evaluation of the adequacy of the allowance for non-covered loan losses considered, among other things, estimated loss factors assigned to specific types of loans, changes and trends in the level of delinquencies, non-covered loans classified as substandard, doubtful and loss, non-covered nonaccrual loans and non-covered loan charge-offs, changes in the value of collateral, changes in the local and regional economic and business conditions, and the judgment of the bank regulatory agencies at the conclusion of their examination process with respect to information available to them during such examination process. Finally, we considered the weakness of the economic recovery and the impact it might have on our borrowers, especially our small business borrowers. More specifically, we did not change our estimated loss factors in our qualitative considerations and revised downward our estimated loss factors in our quantitative considerations.

The allowance for non-covered loan losses increased to $18.3 million at March 31, 2013 from $18.2 million at December 31, 2012. There was no provision to increase the allowance for non-covered loan losses for the three months ended March 31, 2013 and $0.5 million for the three months ended March 31, 2012. The ratio of the allowance for non-covered loan losses to non-covered loans was 1.77 percent at March 31, 2013 compared with 1.71 percent at December 31, 2012.

We believe that our allowance for non-covered loan losses was adequate at March 31, 2013; however, the determination of the allowance for non-covered loan losses is a highly judgmental process and we cannot assure you that we will not further increase or decrease the allowance or that bank regulators will not require us to increase or decrease the allowance in future periods.

The following table presents activity in the allowance for non-covered loan losses:

Three Months

(dollars in thousands)	Ended March 31, 2013	2012
Beginning balance	$18,172	$17,747
Provision for non-covered loan losses	—	500
Loans charged-off	(39)	(218)
Recoveries on loans charged-off	138	125
Ending balance	$18,271	$18,154
Allowance to non-covered loans	1.77%	1.80%
Net non-covered loans charged-off to average non-covered loans (annualized)	-0.04%	0.04%

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The following table presents the net non-covered loan charge-offs (recoveries) by loan type for the periods indicated.

(in thousands)	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012
Home mortgage	$(18)	$ 98
Commercial loans & lines	15	(41)
Commercial mortgage	(101)	9
Installment	5	27
Total	$(99)	$ 93

Net non-covered loan recoveries for the three months ended March 31, 2013 were $0.1 million compared with net charge-offs of $0.1 million for the same period last year. Net non-covered loan charge-offs to average non-covered loans for the 2013 first quarter were -0.04 percent compared with 0.04 percent for the 2012 first quarter.

The following table presents the allocation of the allowance for non-covered loan losses to each loan category and the percentage relationship of non-covered loans in each category to total non-covered loans:

	March 31, 2013		December 31, 2012	
(in thousands)	Allocation of the allowance by loan category	Percent of Loans in Category to Total loans	Allocation of the allowance by loan category	Percent of Loans in Category to Total loans
Commercial mortgage	$ 7,261	44%	$ 5,749	42%
Multifamily mortgage	3,263	20%	2,851	21%
Commercial loans	4,678	15%	6,388	16%
Construction loans	546	4%	498	3%
Home equity loans and lines	538	4%	412	3%
Home mortgage	1,927	13%	2,223	14%
Installment and credit card	58	—	51	1%
Total	$ 18,271	100%	$ 18,172	100%

The amounts or proportions displayed above do not imply that charges to the allowance will occur in those amounts or proportions.

The allowance for losses on undisbursed commitments was $86,000 at March 31, 2013, and at December 31, 2012. The allowance for losses on undisbursed commitments is included in “accrued interest payable and other liabilities” on the consolidated balance sheets.

We had thirty-six non-covered restructured loans for $13.6 million at March 31, 2013; of these, nineteen restructured loans for $7.7 million were current at March 31, 2013, one restructured loan for $0.6 million was included in the accruing loans past due 30 – 89 days category and sixteen restructured loans for $5.3 million were included in the nonaccrual loan category shown below. We had forty-one non-covered restructured loans for $14.0 million at December 31, 2012; of these, twenty-two restructured loans for $7.8 million were current at December 31, 2012, two restructured loans for $0.9 million were included in the accruing loans past due 30 to 89 days category shown below and seventeen restructured loans for $5.3 million were included in the nonaccrual loan category shown below.

The following table presents non-covered past due and nonaccrual loans at the dates indicated.

(dollars in thousands)	March 31, 2013		December 31, 2012	
Accruing non-covered loans past due 30 - 89 days	$7,093		$11,062	
Accruing non-covered loans past due 90 days or more	$128		$—	
Nonaccrual non-covered loans	$21,124		$14,610	
Ratios:				
Accruing loans past due 90 days or more to non-covered loans	0.01	%	—	
Non-covered nonaccrual loans to non-covered loans	2.05	%	1.38	%

Non-covered accruing loans past due 30 to 89 days decreased to $7.1 million at March 31, 2013 from $11.1 million at December 31, 2012. This category of loans historically has had the most fluctuation from period to period.

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Non-covered nonaccrual loans and loans past due 90 days or more and accruing increased to $21.3 million at March 31, 2013 from $14.6 million at December 31, 2012.

Our largest non-covered nonaccrual loan was a $6.3 million single-family mortgage loan on a custom residence in Beverly Hills, California, which was greater than 90 days delinquent at March 31, 2013. We estimated a specific loss allowance of $0.2 million for this loan at March 31, 2013.

Our next largest non-covered nonaccrual facility was a revolving credit facility to purchase and develop a film library with a balance of $4.8 million at March 31, 2013. This balance is after charge-offs of $3.4 million. The charge-off represented the excess of the loan advances over the value of the film library. This loan is a participation in a credit facility also known as a shared national credit. We estimated at March 31, 2013, a specific loss allowance of $0.4 million for this loan.

Our next largest non-covered nonaccrual loan was a $1.0 million commercial business loan to a commercial contractor. The borrower filed for Chapter 11 bankruptcy; however, this loan was performing in accordance with modified loan terms at March 31, 2013. We estimated a specific loss allowance of $0.5 million for this loan at March 31, 2013.

All other non-covered nonaccrual loans were individually under $1 million at March 31, 2013.

The following table presents the activity in our non-covered nonaccrual loan category for the periods indicated.

	Three months ended March 31,			
	2013		2012	
(dollars in thousands)	# of Loans	$ Amount	# of Loans	$ Amount
Beginning balance	33	$ 14,610	29	$ 13,860
New loans added	6	8,723	5	1,143
Advances on existing loans	—	179	—	—
Loans returned to accrual status	(2)	(27)	(1)	(37)
Payoffs on existing loans	(3)	(1,108)	(2)	(305)
Payments on existing loans	—	(1,247)	—	(30)
Charge offs on existing loans	—	—	(1)	(64)
Partial charge-offs on existing loans	—	(6)	—	(14)
Ending balance	34	$ 21,124	30	$ 14,553

We consider a loan impaired when, based on current information and events, we do not expect to be able to collect all amounts due according to the loan contract, including scheduled interest payments. Due to the size and nature of the loan portfolio, we determine impaired loans by periodic evaluation on an individual loan basis. The average investment in non-covered impaired loans was $23.9 million and $14.8 million for the three months ended March 31, 2013 and 2012, respectively. Non-covered impaired loans were $29.7 million and $23.0 million at March 31, 2013 and December 31, 2012, respectively. Of the $29.7 million of non-covered impaired loans at March 31, 2013, $26.7 million had specific reserves of $2.9 million. Of the $23.0 million of non-covered impaired loans at December 31, 2012, $18.5 million had specific reserves of $5.0 million.

Non-covered foreclosed property

Non-covered foreclosed property at March 31, 2013 consists of a $10.4 million completed office complex project consisting of 12 buildings ($11.1 million and 13 buildings at December 31, 2012) in Ventura County and $2.8 million of unimproved property comprised of 161 acres located in an unincorporated section of western Los Angeles County known as Liberty Canyon. The remainder represents one multifamily property and one single-family residence individually less than $1 million.

The following table presents the activity of our non-covered foreclosed property for the periods indicated.

	Three months ended March 31,			
	2013		2012	
	# of Properties	$ Amount	# of Properties	$ Amount
	(dollars in thousands)			
Beginning balance	4	$ 14,895	7	$ 20,349
New properties added	—	—	—	—
Valuation allowances	—	—	—	—
Partial sale proceeds received	—	(730)	—	—
Sales of properties	—	—	(2)	(1,640)
Ending balance	4	$ 14,165	5	$ 18,709

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Covered loans and FDIC shared-loss asset

We acquired loans in the WCB and SLTB acquisitions for which we entered into shared-loss agreements with the FDIC, or covered loans. We will share in the losses, which begin with the first dollar of loss incurred, on the loan pools (including single-family residential mortgage loans, commercial loans and foreclosed property) covered ("covered assets") under the shared-loss agreements. We refer to all other loans in our loan portfolio not acquired from WCB or SLTB as non-covered loans.

Pursuant to the terms of the shared-loss agreements, the FDIC is obligated to reimburse us for 80 percent of eligible losses with respect to covered assets. We have a corresponding obligation to reimburse the FDIC for 80 percent of eligible recoveries with respect to covered assets. The shared-loss agreements for commercial and single-family residential mortgage loans are in effect for five years and ten years, respectively, from the acquisition dates and the loss recovery provisions are in effect for eight years and ten years, respectively, from the acquisition dates.

The covered loan portfolio decreased to $97.7 million at March 31, 2013 from $102.4 million at December 31, 2012. The following table sets forth the composition of the covered loan portfolio by type.

Covered loans by property type (in thousands)	At March 31, 2013	At December 31, 2012
Home mortgage	$29,577	$29,896
Commercial mortgage	27,868	28,079
Construction and land loans	17,177	19,699
Multifamily	8,842	9,699
Commercial loans and lines of credit	7,282	8,167
Home equity loans and lines of credit	6,937	6,891
Total covered loans	$97,683	$102,431

The acquired covered loans are and will continue to be subject to the Bank's internal and external credit review and monitoring practices. The covered loans have the same credit quality indicators, such as risk grade and classification, as the non-covered loans, to enable the monitoring of the borrower's credit and the likelihood of repayment. If credit deteriorates beyond the respective acquisition date fair value amount of covered loans we will establish an allowance for credit losses through a charge to earnings.

The FDIC shared-loss asset represents the present value of the amounts we expect to receive from the FDIC under the shared-loss agreements as well as expenses incurred in the collection and resolution of the covered assets reimbursable to us from the FDIC. The FDIC shared-loss asset was $40.9 million at March 31, 2013 and $45.3 million at December 31, 2012. The decrease in the FDIC shared-loss asset was due primarily to cash received from the FDIC under the shared-loss agreements.

We recorded at fair value the FDIC shared-loss asset, which represented the present value of the estimated cash payments from the FDIC for future losses on covered assets. The ultimate collectability of this asset is dependent upon the performance of the underlying covered assets, the passage of time and claims paid by the FDIC. The following table presents the changes in the FDIC shared-loss asset for the three months ended March 31, 2013.

	Three months ended March 31, 2013		
(in thousands)	WCB	SLTB	Total

Balance, beginning of period	$5,466	$39,879	$45,345
FDIC share of additional losses	14	61	75
Cash payments to(from) FDIC	47	(2,857)	(2,810)
Net amortization	(222)	(1,485)	(1,707)
Balance, end of period	$5,305	$35,598	$40,903

Forty-five days following the tenth anniversary of the WCB and SLTB acquisition dates, we will be required to perform a calculation and determine if a payment to the FDIC is necessary. The payment amount will be 50 percent of the excess, if any, of (i) 20 percent of the intrinsic loss estimate minus (ii) the sum of (a) 20 percent of the net loss amount, plus (b) 25 percent of the asset discount bid, plus (c) 3.5 percent of total loss share assets at acquisition. Our estimate for the present value of this liability was $4.0 million at March 31, 2013 and $3.9 million at December 31, 2012.

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Covered foreclosed property

Covered foreclosed property at March 31, 2013 was $2.9 million and $3.9 million at December 31, 2012. These are foreclosed properties from the Western Commercial Bank and San Luis Trust Bank covered loan portfolios.

The following table presents the activity of our covered foreclosed property for the periods indicated.

	Three months ended March 31,			
	2013		2012	
	# of Properties	$ Amount	# of Properties	$ Amount
	(dollars in thousands)			
Beginning balance	11	$ 3,900	49	$ 14,616
New properties added	2	341	5	3,907
Sales of properties	(3)	(1,322)	(20)	(5,655)
Ending balance	10	$ 2,919	34	$ 12,868

Investing, funding and liquidity risk

Liquidity risk is the risk to earnings or capital arising from the inability to meet obligations when they come due without incurring unacceptable losses. Liquidity risk includes the inability to manage unplanned decreases or changes in funding sources as well as the failure to recognize or address changes in market conditions that affect the ability to liquidate assets quickly and with minimal loss in value.

We manage bank liquidity risk through Board approved policies and procedures. The Directors review and approve these policies at least annually. Liquidity risk policies provide us with a framework for consistent evaluation of risk and establish risk tolerance parameters. Management’s Asset and Liability Committee meets regularly to evaluate liquidity risk, review and establish deposit interest rates, review loan and deposit in-flows and out-flows and reports quarterly to the Directors’ Balance Sheet Management Committee on compliance with policies. The Directors’ Audit Committee also engages a third party to perform a review of management’s asset and liability practices to ensure compliance with policies.

We enjoy a large base of core deposits (representing checking, savings and small balance retail certificates of deposit). At March 31, 2013, core deposits were $1.0 billion, down 15 percent from $1.2 billion at December 31, 2012. The decrease reflects the decrease in deposits from our EPS division due to the ongoing wind down of this division’s operations. EPS deposits were $202.9 million at March 31, 2013, down from $289.7 million at December 31, 2012. Core deposits represent a significant low-cost source of funds that support our lending activities and represent a key part of our funding strategy. We seek and stress the importance of both loan and deposit relationships with customers in our business plans.

Alternative funding sources include large balance certificates of deposits, brokered deposits, prepaid debit cards, federal funds purchased from other institutions, securities sold under agreements to repurchase and borrowings. Total alternative funds used at March 31, 2013 increased to $441.9 million from $406.1 million at December 31, 2012. The increase in alternative funds was mainly due to the increase in prepaid debit cards during the period.

In addition, we have lines of credit with other financial institutions providing for federal funds facilities up to a maximum of $30.0 million. The lines of credit support short-term liquidity needs and we cannot use them for more than 30 consecutive days. These lines are unsecured, have no formal maturity date and can be revoked at any time by the granting institutions. There were no borrowings under these lines of credit at March 31, 2013 or December 31,

2012. We also have a $14.4 million secured borrowing facility with the Federal Reserve Bank of San Francisco, or the Reserve Bank, which had no balance outstanding at March 31, 2013 or December 31, 2012. In addition, we had approximately $394.6 million of available borrowing capacity on the Bank's secured FHLB borrowing facility at March 31, 2013.

The primary sources of liquidity for the Company, on a stand-alone basis, include the dividends from the Bank and, historically, our ability to issue trust preferred securities and secure outside borrowings. The ability of the Company to obtain funds for its cash requirements, including payments on the junior subordinated debentures underlying our outstanding trust preferred securities and the dividend on our series C preferred stock, is largely dependent upon the Bank's earnings. The Bank is subject to restrictions under certain federal and state laws and regulations, which limit its ability to transfer funds to the Company through intercompany loans, advances or cash dividends. The California Department of Financial Institutions, or DFI, under its general supervisory authority as it relates to a bank's capital requirements regulates dividends paid by state banks, such as the Bank. A state bank may declare a dividend without the approval of the DFI as long as the total dividends declared in a calendar year do not exceed either the retained earnings or the total of net profits for three previous fiscal years less any dividends paid during such period. At March 31, 2013, there were $42.9 million of dividends available for payment under the method described. For the first three months of 2013, we received a $1 million dividend from the Bank. The Company had $1.0 million in cash on deposit with the Bank at March 31, 2013.

In order to meet our deposit, borrowing and loan obligations when they come due, we maintain a portion of our funds in liquid assets. Liquid assets include cash balances at the Reserve Bank, interest bearing deposits with other financial institutions, and federal funds sold to other financial institutions. We also manage liquidity risk with readily saleable debt securities and debt securities that serve as collateral for borrowings.

At March 31, 2013, we had cash balances at the Reserve Bank of $43.2 million compared with $39.3 million at December 31, 2012. Interest bearing deposits with the Reserve Bank and other financial institutions decreased to $68.0 million at March 31, 2013 from $120.9 million at December 31, 2012. The $52.9 million decrease reflects the decrease in deposits. We believe that these sources of liquidity will be sufficient for the Company to meet its liquidity needs over the next twelve months.

As disclosed in the Condensed Consolidated Statements of Cash Flows, net cash used by operating activities was $1.4 million during the three months ended March 31, 2013. The difference between cash used by operating activities and net income largely consisted of non-cash items including the change in the FDIC shared-loss asset, amortization of net premiums on securities and stock-based compensation expense.

Net cash of $155.6 million provided by investing activities consisted principally of $36.7 million of net cash collections of loans, $86.7 million of proceeds from sales, repayments and maturities of securities available-for-sale and a $52.8 million decrease in federal funds sold and interest bearing deposits, partially offset by $25.8 million of purchases of securities available-for-sale.

Net cash of $150.4 million used by financing activities primarily consisted of a $149.3 million decrease in net deposits.

Securities

We classify securities as “available-for-sale” for accounting purposes and, as such, report them at their fair, or market, values in our balance sheets. We use quoted market prices for fair values. We report as “other comprehensive income or loss”, net of tax, changes in the fair value of our securities (that is, unrealized holding gains or losses) and carry these cumulative changes as accumulated comprehensive income or loss within shareholders’ equity until realized.

Securities, at amortized cost, decreased by $62.4 million, or 16 percent, from $381.6 million at December 31, 2012 to $319.2 million at March 31, 2013.

Net unrealized holding losses were $1.0 million at March 31, 2013 and net unrealized holding losses were $0.6 million at December 31, 2012. As a percentage of securities, at amortized cost, unrealized holding gains were 0.30 percent and net unrealized holding losses were 0.15 percent at the end of each respective period. Securities are comprised largely of U.S. government agency notes, mortgage-backed securities and collateralized mortgage obligations, or CMOs. On a quarterly basis, we evaluate our individual available-for-sale securities in an unrealized loss position for other-than-temporary impairment. As part of this evaluation, we consider whether we intend to sell each security and whether it is more likely than not that we will be required to sell the security before the anticipated recovery of the security’s amortized cost basis. Should a security meet either of these conditions, we recognize an impairment charge to earnings equal to the entire difference between the security’s amortized cost basis and its fair value at the balance sheet date. For securities in an unrealized loss position that meet neither of these conditions, we consider whether we expect to recover the entire amortized cost basis of the security by comparing our best estimate, on a present value basis, of the expected future cash flows from the security with the amortized cost basis of the security. If our best estimate of expected future cash flows is less than the amortized cost basis of the security, we recognize an impairment charge to earnings for this estimated credit loss.

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The following table presents the gross unrealized losses and amortized cost of securities and the length of time that individual securities have been in a continuous unrealized loss position at March 31, 2013 and December 31, 2012.

	At March 31, 2013					
	Less Than 12 Months		Greater Than 12 Months		Total	
	Amortized Cost	Unrealized Losses	Amortized Cost	Unrealized Losses	Amortized Cost	Unrealized Losses
	(in thousands)					
U.S. government agency notes	$14,013	$(15)	$—	$—	$14,013	$(15)
U.S. government agency mortgage-backed securities	84,163	(447)	—	—	84,163	(447)
U.S. government agency collateralized mortgage obligations	34,968	(205)	—	—	34,968	(205)
Municipal securities	4,935	(144)	—	—	4,935	(144)
Other domestic debt securities	—	—	4,121	(1,401)	4,121	(1,401)
	$138,079	$(811)	$4,121	$(1,401)	$142,200	$(2,212)

	At December 31, 2012					
	Less Than 12 Months		Greater Than 12 Months		Total	
	Amortized Cost	Unrealized Losses	Amortized Cost	Unrealized Losses	Amortized Cost	Unrealized Losses
	(in thousands)					
U.S. government agency notes	$7,572	$(24)	$—	$—	$7,572	$(24)
U.S. government agency mortgage-backed securities	25,756	(124)	—	—	25,756	(124)
U.S. government agency collateralized mortgage obligations	67,055	(336)	5,820	(10)	72,875	(346)
Municipal securities	4,953	(81)	—	—	4,953	(81)
Other domestic debt securities	—	—	4,367	(1,640)	4,367	(1,640)
	$105,336	$(565)	$10,187	$(1,650)	$115,523	$(2,215)

We determined that, as of March 31, 2013, our U.S. government agency notes, mortgage-backed securities and CMOs were temporarily impaired because these securities were in a continuous loss position for less than 12 months. We believe the cause of the gross unrealized losses was movements in interest rates and not by the deterioration of the issuers' creditworthiness.

We own one pooled trust preferred security, rated triple-A at purchase, with an amortized cost basis of $4.1 million and an unrealized loss of $1.4 million at March 31, 2013. At December 31, 2012, the unrealized loss was $1.6 million. The gross unrealized loss is mainly due to extraordinarily high investor yield requirements resulting from an illiquid market, causing this security to be valued at a discount to its acquisition cost. Since 2009, this security had credit agency ratings of less than investment grade; however, in the 2012 third quarter, the security's rating increased to investment grade. The senior tranche owned by us has a collateral balance well in excess of the amortized cost basis of the tranche at March 31, 2013. Seventeen of the fifty-six issuers in the security have deferred or defaulted on their interest payments as of March 31, 2013. Our analysis determined that approximately half of the issuers would need to default on their interest payments before the senior tranche owned by us would be at risk of loss. As our estimated present value of expected cash flows to be collected was in excess of our amortized cost basis and we have the intent and ability to hold this security until the anticipated recovery of the remaining amortized cost basis, we concluded that the gross unrealized loss on this security was temporary.

Deposits

Deposits represent our primary source of funds for our lending activities. The following table presents the balance of each deposit category for the periods indicated:

(in thousands)	March 31, 2013	December 31, 2012
Core deposits:		
Non-interest bearing checking	$405,886	$546,638
Interest checking	113,970	124,765
Savings and money market accounts	448,652	478,052
Retail time deposits less than $100,000	55,223	59,311
Total core deposits	1,023,731	1,208,766
Noncore deposits:		
Prepaid debit cards	134,223	89,817
Retail time deposits $100,000 or more	149,246	157,767
Wholesale time deposits	1,368	1,482
State of California time deposits	50,000	50,000
Total noncore deposits	334,837	299,066
Total core and noncore deposits	$1,358,568	$1,507,832

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The 26 percent decline in non-interest checking deposits reflects principally the $131.1 million decline in EPS division deposits in this category.

Large balance certificates of deposit (that is, balances of $100,000 or more) were $200.6 million at March 31, 2013. Large balance certificates of deposit were $209.2 million at December 31, 2012. A portion of these large balance time deposits represent time deposits placed by the State Treasurer of California with the Bank. The time deposit program is one element of a pooled investment account managed by the State Treasurer for the benefit of the State of California and all participating local agencies. The pooled investment account has approximately $59 billion of investments, of which approximately $4.3 billion represent time deposits placed at various financial institutions. At March 31, 2013, and December 31, 2012, State of California time deposits placed with us, with original maturities of three months, were $50.0 million at each date. We believe that the State Treasurer will continue this program; we also believe that we have the ability to establish large balance certificates of deposit rates that will enable us to attract, replace, or retain those deposits accepted in our local market area if it becomes necessary under a modified funding strategy.

From time to time we use brokered time deposits, categorized as wholesale time deposits in the table above, to supplement our liquidity and achieve other asset-liability management objectives. Brokered time deposits are wholesale certificates of deposit accepted by us from brokers whose customers do not have any other significant relationship with us. As a result, we believe these funds are very sensitive to credit risk and interest rates, and pose greater liquidity risk to us. These customers may refuse to renew the certificates of deposits at maturity if higher rates are available elsewhere or if they perceive that our creditworthiness is deteriorating. At March 31, 2013 and December 31, 2012, we had no brokered time deposits.

We also use the Certificate of Deposit Account Registry System, or CDARS, for our deposit customers who wish to obtain FDIC insurance on their deposits beyond that available from a single institution. We place these deposits into the CDARS network and accept in return other customers' certificates of deposits in the same amount and at the same interest rate. We had $1.4 million of these reciprocal deposits, categorized as wholesale time deposits in the table above, at March 31, 2013 and $1.5 million at December 31, 2012.

Effective December 31, 2012, we reclassified our noninterest bearing checking deposits representing prepaid debit cardholder deposit balances as brokered or noncore deposits. At March 31, 2013, prepaid debit card deposits were $134.2 million, up from $89.8 million for the 2012 year-end due to seasonal fluctuation in these balances.

At March 31, 2013, the scheduled maturities of time certificates of deposit in denominations of $100,000 or more were as follows:

(Dollars in thousands)

Three months or less	$	73,073
Over three months to twelve months		46,634
Over twelve months		80,907
	$	200,614

Borrowings

Borrowings are comprised of federal funds purchased from other financial institutions, FHLB advances and securities sold under agreements to repurchase. At March 31, 2013, we had $107.0 million of borrowings outstanding, of which

$10.0 million was comprised of securities sold under agreements to repurchase and $97.0 million of FHLB advances. For our FHLB advances, the following table presents the amounts and weighted average interest rates outstanding.

	Three Months Ended March 31, 2013		Year Ended December 31, 2012	
(in thousands)	Federal Home Loan Bank Advances	Weighted average interest rate	Federal Home Loan Bank Advances	Weighted average Interest rate
Amount outstanding at end of period	$ 97,026	1.99%	$ 77,054	2.49%
Maximum amount outstanding at any month-end during the period	$ 97,035	1.99%	$ 102,700	2.76%
Average amount outstanding during the period	$ 90,200	2.06%	$ 93,082	2.60%

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The following table presents the maturities of FHLB term advances:

(dollars in thousands)	At March 31, 2013 Amount	Maturity Year	Weighted Average Interest Rate	At December 31, 2012 Amount	Maturity Year	Weighted Average Interest Rate
	$ 27,026	2013	0.80%	$ 7,054	2013	2.93%
	32,500	2014	2.95%	32,500	2014	2.95%
	15,000	2015	1.76%	15,000	2015	1.76%
	22,500	2017	2.20%	22,500	2017	2.20%
	$ 97,026			$ 77,054		

The following table presents maturities of securities sold under agreements to repurchase:

(dollars in thousands)	At March 31, 2013 Amount	Maturity Year	Weighted Average Interest Rate	At December 31, 2012 Amount	Maturity Year	Weighted Average Interest Rate
	$ —			$ 20,000	2013	3.60%
	10,000	2014	3.72%	10,000	2014	3.72%
	$ 10,000			$ 30,000		

Junior Subordinated Debentures

As of March 31, 2013 and December 31, 2012, we had $26.8 million of junior subordinated debentures outstanding from two issuances of trust preferred securities. First California Capital Trust I's capital securities have an outstanding balance of $16.5 million, mature on March 15, 2037, and are redeemable, at par, at the Company's option at any time on or after March 15, 2012. The securities have a variable annual rate, which resets quarterly, equal to the 3-month LIBOR rate plus 1.60% per annum. At March 31, 2013, the rate was 1.88%. FCB Statutory Trust I's capital securities have an outstanding balance of $10.3 million, mature on December 15, 2035, and are redeemable, at par, at the Company's option at any time on or after December 15, 2010. The securities have a variable annual rate, which resets quarterly, equal to the 3-month LIBOR rate plus 1.55% per annum. At March 31, 2013, the rate was 1.83%.

In December 2009, we purchased a $10.3 million notional forward-starting interest rate cap to limit the variable interest rate payments on our $10.3 million junior subordinated debentures. This interest rate cap became effective on December 15, 2010, has a rate cap of 4.00 percent and will expire on December 15, 2015. In September 2010, we purchased a $16.5 million notional forward-starting interest rate cap to limit the variable interest rate payments on our $16.5 million junior subordinated debentures. This interest rate cap became effective March 15, 2012, has a rate cap of 4.00 percent and will expire on March 15, 2017.

Capital resources

We have 1,000 issued shares of preferred stock series A, $0.01 par value, with a liquidation preference of $1,000 per share. Redemption of the preferred stock series A is at our option subject to certain restrictions imposed by our preferred stock series C. The redemption amount is computed at the per-share liquidation preference plus unpaid dividends at a rate of 8.5%. Each holder of preferred stock series A has the right, exercisable at the option of the holder, to convert all or some of such holder's series A shares into common stock, which such holders have agreed to do prior to the consummation of the PacWest Merger. The sum of each share's liquidation preference plus unpaid dividends divided by the conversion factor of $5.63 per share represents the number of common shares issuable upon the conversion of each share of preferred stock series A. As of March 31, 2013, we reserved 348,286 of common shares for the conversion of the preferred stock series A.

In July 2011, we participated in the U.S. Treasury Small Business Lending Fund, or the SBLF program, under which we received $25 million in exchange for issuing 25,000 preferred stock series C shares. The preferred stock series C shares are entitled to receive non-cumulative quarterly dividends and the initial dividend rate was 5 percent. The dividend rate can fluctuate between 1 and 5 percent during the next six quarters and is a function of the growth in qualified small business loans each quarter. On February 27, 2013, First California notified the Treasury that, subject to receipt of requisite regulatory approvals, First California intends to redeem all of its outstanding shares of Series C preferred stock simultaneously with the consummation of First California's pending merger with PacWest.

The Company is subject to various regulatory capital requirements administered by the federal and state banking agencies. Failure to meet minimum requirements can initiate certain mandatory - and possibly additional discretionary - actions by regulators that, if undertaken, could have a direct material effect on a company's financial statements. Under capital adequacy guidelines, bank holding companies must meet specific capital guidelines that involve quantitative measures of the company's assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. Capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

The following tables present the capital amounts and ratios of the Company with a comparison to the minimum ratios for the periods indicated:

	Actual			For Capital Adequacy Purposes		
		Amount	Ratio		Amount	Ratio
		(in thousands)				
March 31, 2013						
Total capital (to risk weighted assets)	$	208,437	18.95%	$	88,006	8.00%
Tier I capital (to risk weighted assets)	$	194,625	17.69%	$	44,003	4.00%
Tier I capital (to average assets)	$	194,625	11.08%	$	70,239	4.00%

	Actual			For Capital Adequacy Purposes		
		Amount	Ratio		Amount	Ratio
		(in thousands)				
December 31, 2012						
Total capital (to risk weighted assets)	$	209,164	18.19%	$	91,971	8.00%
Tier I capital (to risk weighted assets)	$	194,746	16.94%	$	45,986	4.00%
Tier I capital (to average assets)	$	194,746	10.20%	$	76,396	4.00%

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of Total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital to average assets (as defined). Management believes, as of March 31, 2013, that the Bank meets all capital adequacy requirements to which it is subject.

As of March 31, 2013, the Bank exceeded the minimum ratios to be well-capitalized under the prompt corrective action provisions. There are no conditions or events since March 31, 2013 that we believe would change the Bank's category.

The following tables present the capital amounts and ratios of the Bank with a comparison to the minimum ratios for the periods indicated:

	Actual		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provision	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(in thousands)			
March 31, 2013						
Total capital						
(to risk weighted assets)	$ 208,589	18.96%	$ 88,034	8.00%	$ 110,042	10.00%
Tier I capital						
(to risk weighted assets)	$ 194,777	17.70%	$ 44,017	4.00%	$ 66,025	6.00%
Tier I capital						
(to average assets)	$ 194,777	11.08%	$ 70,288	4.00%	$ 87,860	5.00%

	Actual		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provision	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(in thousands)			
December 31, 2012						
Total capital						
(to risk weighted assets)	$ 208,901	18.16%	$ 92,025	8.00%	$ 115,031	10.00%
Tier I capital						
(to risk weighted assets)	$ 194,474	16.91%	$ 46,013	4.00%	$ 68,019	6.00%
Tier I capital						
(to average assets)	$ 194,474	10.18%	$ 76,409	4.00%	$ 95,512	5.00%

We recognize that a strong capital position is vital to growth, continued profitability, and depositor and investor confidence. Our policy is to maintain sufficient capital at not less than the well-capitalized thresholds established by banking regulators.

Financial Instruments with Off-Balance Sheet Risk

In the normal course of business, we make commitments to extend credit or issue letters of credit to customers. We generally do not recognize these commitments in our balance sheet. These commitments involve, to varying degrees, elements of credit risk; however, we use the same credit policies and procedures as we do for on-balance sheet credit facilities.

The following summarizes our outstanding commitments at March 31, 2013 and December 31, 2012:

(in thousands)	March 31, 2013	December 31, 2012
Financial instruments whose contract amounts contain credit risk:		
Commitments to extend credit	$162,591	$161,395
Commercial and standby letters of credit	5,472	1,651
	$168,063	$163,046

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. Total commitment amounts do not necessarily represent future cash requirements because many expire without use. We may obtain collateral for the commitment based on our credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property and equipment, and income-producing properties.

Letters of credit written are conditional commitments issued by us to guarantee the performance of a customer to a third party. These guarantees support public and private borrowing arrangements, including commercial paper, bond financing, and similar transactions. Credit risk for letters of credit is essentially the same as that for loan facilities to customers. When we deem collateral necessary, we will hold cash, marketable securities, or real estate as collateral supporting those commitments.

The allowance for losses on undisbursed commitments was $86,000 at March 31, 2013, and December 31, 2012. The allowance for losses on undisbursed commitments is included in “accrued interest payable and other liabilities” on the consolidated balance sheets.

Interest Rate Risk

Interest rate risk is the risk to earnings or capital arising from movements in interest rates. Interest rate risk arises from differences between the timing of rate changes and the timing of cash flows (re-pricing risk), from changing rate relationships among different yield curves affecting bank activities (basis risk), from changing rate relationships across the spectrum of maturities (yield curve risk), and from interest-related options embedded in loans and products (options risk).

We manage interest rate risk through Board approved policies and procedures. The Directors review and approve these policies at least annually. Interest rate risk policies provide management with a framework for consistent evaluation of risk and establish risk tolerance parameters. Management’s Asset and Liability Committee meets regularly to evaluate interest rate risk, engages a third party to assist in the measurement and evaluation of risk and reports quarterly to the Directors’ Balance Sheet Management Committee on compliance with policies. The Directors’ Audit Committee also engages a third party to perform a review of management’s asset and liability practices to ensure compliance with policies.

We use simulation-modeling techniques that apply alternative interest rate scenarios to periodic forecasts of future business activity and assess the potential changes to net interest income. Our base scenario examines our balance sheet where we assume rate changes occur ratably over an initial 12-month horizon based upon a parallel shift in the yield curve and then is maintained at that level over the remainder of the simulation horizon. We also create alternative scenarios where we assume different types of yield curve movements. In our most recent base simulation, we estimated that net interest income would decrease approximately 0.48% within a 12-month time horizon for an assumed 100 basis point decrease in prevailing interest rates or increase approximately 1.19% for an assumed 100 basis point increase in prevailing interest rates. In addition, we estimated that net interest income would increase approximately 2.46% within a 12-month time horizon for an assumed 200 basis point increase in prevailing rates. These estimated changes were within the policy limits established by the Board. The table below illustrates the estimated percentage change in our net interest income in our base scenario over hypothetical 1, 3 and 5 year horizons.

	Time Horizon		
Percentage Change	1 Year	3 Years	5 Years
-100 bps	-0.48%	-1.82%	-3.61%
+100 bps	1.19%	1.77%	3.74%
+200 bps	2.46%	3.73%	10.73%
+400 bps	2.57%	11.77%	28.73%

All interest-earning assets, interest-bearing liabilities and related derivative contracts are included in the interest rate sensitivity analysis at March 31, 2013. At March 31, 2013, approximately 41 percent of our loans had a fixed rate of interest and approximately 59 percent had a variable interest rate. Of loans with a variable rate of interest, approximately 25 percent use an interest rate that floats with a specified interest rate such as the Wall Street Journal Prime Rate or 3-month LIBOR rate. Approximately 14 percent of our variable rate loans use an interest rate that adjusts periodically, such as monthly, quarterly or annually, with a specified index rate. Finally, approximately 61 percent of our variable interest rate loans have an interest rate that remains fixed for a period of time, such as 1, 2, 3 or 5 years, then adjusts periodically with a specified index rate.

In addition, approximately 87 percent of our variable interest rate loans have a minimum, or floor, rate of interest. Of these, 23 percent were at their minimum, or floor rate of interest. In a declining rate environment, the interest rate floors contribute to the favorable impact on our net interest income. However, in a rising rate environment, these interest rate floors serve to lessen the full benefit of higher interest rates. In our most recent base simulation, an assumed 200 basis point increase in prevailing interest rates would cause 76 percent of loans at their minimum rate of interest not to be at their floor rate of interest.

Our simulation model includes assumptions about anticipated prepayments on mortgage-related instruments, the estimated cash flow on loans and deposits, and our future business activity. These assumptions are inherently uncertain and, as a result, our modeling techniques cannot precisely estimate the effect of changes in net interest income. Actual results will differ from simulated results due to the timing, magnitude and frequency of interest rate changes, cash flow and business activity.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Please see the section above titled “Interest Rate Risk” in “Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations,” which provides an update to our quantitative and qualitative disclosure about market risk. Our analysis of market risk and market-sensitive financial information contains forward-looking statements and is subject to the disclosure above under “Forward Looking Statements” in Item 2 regarding such forward-looking information.

Item 4. Controls and Procedures

As of the end of the period covered by this report, an evaluation was carried out by management, with the participation of the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that these disclosure controls and procedures were effective.

There have not been any changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934) during our most recent fiscal quarter ending March 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

The information set forth in “Note 11 – Commitments and Contingencies” of the Company’s Notes to Consolidated Financial Statements included in this Quarterly Report on Form 10-Q is incorporated herein by reference.

The nature of our business causes us to be involved in routine legal proceedings from time to time. Except as disclosed in “Note 11 – Commitments and Contingencies” of the Company’s Notes to Consolidated Financial Statements included in this Quarterly Report on Form 10-Q, we are not aware of any pending or threatened legal proceedings expected to have a material adverse effect on our business, financial condition, results of operations or cash flow that arose during the fiscal quarter ended March 31, 2013 or any material developments in our legal proceedings previously reported in Item 3 to Part I of our Annual Report on Form 10-K for the fiscal year ended December 31, 2012.

Item 1A. Risk Factors

There have been no material changes from risk factors as previously disclosed in the “Risk Factors” section of our Annual Report on Form 10-K for the period ended December 31, 2012, filed with the SEC on March 18, 2013.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

The following Exhibits are filed as a part of this report:

Exhibit Number	Description
31.1	Certification of CEO Pursuant to Securities Exchange Act Rules 13a-14 and 15d-14 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of CFO Pursuant to Securities Exchange Act Rules 13a-14 and 15d-14 as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of CEO and CFO Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

SIGNATURES

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

First California Financial Group, Inc.

Date: May 10, 2013	By:	/s/Romolo Santarosa Romolo Santarosa (Principal Financial Officer and Duly Authorized Officer)