First California Financial Group, Inc.
Form 10-K
March 15, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

Form 10-K

þ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2011

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from __________________to __________________

Commission file number 000-52498

FIRST CALIFORNIA FINANCIAL GROUP, INC.
(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	38-3737811 (I.R.S. Employer Identification Number)
3027 Townsgate Road, Suite 300 Westlake Village, California (Address of Principal Executive Offices)	91361 (Zip Code)

Registrant's telephone number, including area code: (805) 322-9655

Securities registered pursuant to Section 12(b) of the Exchange Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, $0.01 par value	The Nasdaq Global Select Market

Securities registered pursuant to Section 12(g) of the Exchange Act: None

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

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. o Yes þ No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. þ Yes o No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

Large accelerated filer o	Accelerated filer þ	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

Aggregate market value of common stock held by non-affiliates as of June 30, 2011: $80,865,130

As of March 12, 2012, there were 29,249,104 shares of Common Stock, $0.01 par value, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

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PART I

Item 1. Business

Our Business

As used herein, the term “First California Financial Group,” “First California,” “FCAL,” “the Company,” “our,” “us,” “we” or expression includes First California Financial Group, Inc. and First California Bank unless the context indicates otherwise.

Business of First California Financial Group

First California is a bank holding company registered under the Bank Holding Company Act of 1956, as amended, or the BHCA. First California’s primary function is to coordinate the general policies and activities of its bank subsidiary, First California Bank, or the Bank, as well as to consider from time to time other legally available investment opportunities. SC Financial is an inactive subsidiary of First California.

First California incorporated under the laws of the State of Delaware on June 7, 2006. The Company formed as a wholly-owned subsidiary of National Mercantile Bancorp, a California corporation, or National Mercantile, for the purposes of facilitating the mergers of National Mercantile and FCB Bancorp, a California corporation, or FCB. On March 12, 2007, National Mercantile merged with and into First California. Immediately thereafter, the parties completed the previously announced merger of FCB with and into First California. In this document, we refer to the two-step merger of National Mercantile into First California and FCB into First California as the Mergers. As a result of the Mergers, the separate corporate existence of National Mercantile and FCB ceased, and First California succeeded, and assumed all the rights and obligations of, National Mercantile, whose principal assets were the capital stock of two bank subsidiaries, Mercantile National Bank, or Mercantile, and South Bay Bank, N.A., or South Bay, and the rights and obligations of FCB, whose principal assets was the capital stock of First California Bank. On June 18, 2007, First California integrated its bank subsidiaries into First California Bank. All references to the Bank on or before June 18, 2007 refer to the Bank, Mercantile and South Bay.

Business of First California Bank

The Bank is a full-service commercial bank headquartered in Westlake Village, California. The Bank is chartered under the laws of the State of California and is subject to supervision by the California Department of Financial Institutions, or the DFI. The Federal Deposit Insurance Corporation, or the FDIC, insures its deposits up to the maximum legal limit.

On November 5, 2010, the Bank assumed certain liabilities and acquired certain assets and substantially all of the operations of Western Commercial Bank, or WCB, located in Woodland Hills, California, from the FDIC. The Bank acquired, received and recognized certain assets with an estimated fair value of approximately $109 million, including $55 million of loans, $32 million of cash, $16.7 million of a FDIC shared-loss asset, $2 million of securities and $3 million of other assets. Liabilities with an estimated fair value of approximately $107 million were also assumed and recognized, including $105 million of deposits and $2 million of other liabilities. The Bank recorded a pre-tax bargain purchase gain of $2.3 million in connection with this transaction. The transaction increased the number of the Bank’s full-service branch locations to 18 and the Bank fully integrated the former WCB branch into its full-service branch network prior to December 31, 2010.

On February 18, 2011, the Bank assumed certain liabilities and acquired certain assets and substantially all of the operations of San Luis Trust Bank, or SLTB, located in San Luis Obispo, California, from the FDIC. The Bank acquired, received and recognized certain assets with an estimated fair value of approximately $367 million, including $139 million of loans, $99 million of cash and federal funds sold, $70 million of a FDIC shared-loss asset, $41 million of securities, $13 million of foreclosed property and $5 million of other assets. Liabilities with an estimated fair value of approximately $346 million were also assumed and recognized, including $266 million of deposits, $62 million of Federal Home Loan Bank advances, $15 million in a deferred tax liability, $2.6 million of a FDIC shared-loss liability and $0.4 million of other liabilities. The Bank recorded a pre-tax bargain purchase gain of $36.5 million in connection with this transaction. This transaction increased the number of the Bank’s full-service branch locations to 19 and the Bank fully integrated the former SLTB branch into its full-service branch network in June 2011.

On April 8, 2011, the Bank completed the acquisition of the Electronic Banking Solutions division of Palm Desert National Bank. The transaction included the division’s customer base, core deposits, and employees. The Electronic Payment Services Division, or the EPS division, its new name under the Bank, issues prepaid cards and sponsors merchant acquiring services for all national and regional networks, including Visa, MasterCard, and Discover throughout all 50 states and U.S. territories. The Bank acquired cash of $85.4 million, recognized intangible assets of $6.0 million, assumed $91 million of deposits and recognized a pre-tax bargain purchase gain of $0.5 million in connection with this transaction.

The Bank’s business strategy has been to attract individuals, professionals, and small- to mid-sized business borrowers in our primary service areas by offering a variety of loan products and a full range of banking services coupled with highly personalized service. The Bank’s operations are primarily located within the areas commonly known as the “101 corridor” stretching from the City of Ventura to Calabasas, California, the Moorpark-Simi Valley corridor, the western San Fernando Valley, the Tri-Cities area of Glendale-Burbank-Pasadena, the South Bay, the Inland Empire, north San Diego County, Century City and other parts of Los Angeles, Orange, San Luis Obispo and Ventura Counties in Southern California. Our lending products include revolving lines of credit, term loans, commercial real estate loans, construction loans and consumer and home equity loans, which often contain terms and conditions tailored to meet the specific demands of the market niche in which the borrower operates. Additionally, the Bank provides a wide array of deposit products serving the comprehensive banking needs of businesses and consumers in Los Angeles, Orange, Ventura, San Diego, Riverside, San Bernardino and San Luis Obispo counties through traditional business and consumer banking, construction finance, SBA lending, entertainment finance and commercial real estate lending via 19 full-service branch locations.

Business loans, represented by commercial mortgage loans, commercial loans and construction loans, comprise the largest portion of the Bank's loan portfolio. Commercial real estate loans rely upon the cash flow originating from the underlying real property. Commercial real estate is a cyclical industry that is affected not only by general economic conditions but also by local supply and demand. 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 and sell their goods or services for a profit. Construction loans provide developers or owners with funds to build or improve properties that will ultimately be sold or leased. Construction loans are generally considered to 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.

Consumer loans, a smaller component of the Bank's loan portfolio, are represented by home mortgages and home equity loans and lines of credit that are secured by first or second trust deeds on a borrower's real estate property, typically their principal residence. These loans are dependent 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.

The Bank's business strategy also stresses the importance of customer deposit relationships to support its lending activities. Checking deposits, savings deposits and certificates of deposit represent a significant low-cost and stable source of funds. Business customers are offered cash management products, including on-line banking and remote deposit capture, to meet their specific banking needs.

The Bank's goal is to offer its customers a consistently high level of individualized personal service. Accordingly, in order to meet the changing needs of our customers, the Bank is constantly evaluating a variety of options to broaden the services and products it provides. The Bank's strategy in attaining its goals has been to implement and maintain risk management and controls to achieve a safe and sound business policy, employing an aggressive marketing plan which emphasizes relationship banking and the "personal touch," offering competitive products and managing growth. The Bank provides convenience through 19 banking offices with ATM access, 24 hour telephone access to account information, on-line banking, courier service and remote deposit capture. The diversity of our delivery systems enables customers to choose the method of banking that is most convenient for them. The Bank trains its staff to recognize each customer, greet them, and be able to address them by name so that they feel as if they have a "private banker."

Financial and Statistical Disclosure

Certain of our financial and statistical information is presented within "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations." This information should be read in conjunction with the consolidated financial statements contained in "Item 8. Financial Statements and Supplementary Data."

Competition

The banking business in California, generally, and in the Bank's service areas, specifically, is highly competitive with respect to both loans and deposits and is dominated by a number of major banks that have many offices operating over wide geographic areas. The Bank competes for deposits and loans principally with these major banks and other financial institutions located in our market areas. Among the advantages that the major banks have over the Bank are their ability to finance extensive advertising campaigns and to allocate their investment assets to regions of highest yield and demand. Many of the major commercial banks operating in the Bank's service areas offer certain services (such as trust and international banking services) that are not offered directly by the Bank and, by virtue of their greater total capitalization, such banks have substantially higher lending limits. Moreover, all banks face increasing competition for loans and deposits from non-bank financial intermediaries such as mortgage companies, insurance companies, credit unions and securities firms.

In November 1999, the Gramm-Leach-Bliley Act, or the GLBA, was signed into law. The GLBA significantly changed the regulatory structure and oversight of the financial services industry. The GLBA revised the BHCA and repealed the affiliation prohibitions of the Glass-Steagall Act of 1933. Consequently, a qualifying holding company, called a financial holding company, can engage in a full range of financial activities, including banking, insurance, and securities activities, as well as merchant banking and additional activities that are “financial in nature” or “incidental” to those financial activities. Expanded financial affiliation opportunities for existing bank holding companies are now permitted. Moreover, various non-bank financial services providers can acquire banks while also offering services like securities underwriting and underwriting and brokering insurance products. The GLBA also expanded passive investment activities by financial holding companies, permitting investments in any type of company, financial or non-financial, through acquisitions of merchant banking firms and insurance companies.

Given that the traditional distinctions between banks and other providers of financial services have been effectively eliminated, the Bank has faced and will continue to face additional competition from thrift institutions, credit unions, insurance companies and securities firms. Additionally, the Bank's ability to cross-market banking products to existing customers or the customers of affiliated companies may make it more difficult to compete.

In order to compete, the Bank uses to the fullest extent possible the familiarity of its directors and officers with the market area and its residents and businesses and the flexibility that the Bank's independent status will permit. This includes an emphasis on specialized services, local promotional activity, and personal contacts by directors, officers and other employees. The Bank uses advertising, including newspaper ads and direct mail pieces, to inform the community of the services it offers. The Bank also utilizes emerging marketing techniques, such as the Internet, to reach target markets. The Bank also has an active calling program where officers, including commissioned business development officers, contact targeted prospects to solicit both deposit and loan business.

The Bank has developed programs that specifically address the needs of consumers, professionals and small-to medium-sized businesses. In the event there are customers whose loan demands exceed the Bank's lending limits, it arranges for such loans on a participation basis with other financial institutions and intermediaries. The Bank also assists those customers requiring other services not offered by the Bank to obtain those services from correspondent banks. In addition, the Bank offers ATM services, a night depository, remote deposit capture, courier services, bank-by-mail services, merchant windows, lockbox and direct deposit services.

The Bank's management believes that the Bank's reputation in the communities served and personal service philosophy enhance the ability to compete favorably in attracting and retaining individual, professional and business clients. The Bank also believes that it has an advantage over the larger national and "super regional" institutions because it is managed by locally-known, well-respected and experienced bankers. Moreover, our larger competitors may not offer adequate personalized banking services, since their emphasis is on large volume and standardized retail products.

The Bank also faces growing competition from other community banks. These institutions have similar marketing strategies, have also been successful and offer strong evidence regarding the potential success of the community banking sector.

No assurance can be given that ongoing efforts to compete will continue to be successful.

Dependence on One or a Few Major Customers; Business Concentrations

No individual or single group of related accounts is considered material in relation to our total assets or to the assets or deposits of the Bank, or in relation to our overall business. However, approximately 82% of our loan portfolio at December 31, 2011 consisted of real estate-secured loans, including commercial real estate loans, construction loans, home mortgage loans, home equity loans and lines of credit. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations — Financial Position — December 31, 2011 compared with December 31, 2010" in Part II of this Annual Report on Form 10-K. Moreover, our business activities are currently focused primarily in Southern California, with the majority of our business concentrated in Ventura, Orange and Los Angeles Counties. Consequently, our results of operations and financial condition are dependent upon the general trends in the Southern California economies and, in particular, the residential and commercial real estate markets. In addition, the concentration of our operations in Southern California exposes us to greater risk than other banking companies with a wider geographic base in the event of catastrophes, such as earthquakes, fires and floods in this region.

Internet Banking Services

The Bank maintains an internet website, which serves as an additional means of providing customer access to a variety of banking services, including 24/7 online banking. The Bank's website address is www.fcbank.com. No information contained on the website is incorporated herein by reference.

Employees

At December 31, 2011, the Bank had 304 full-time equivalent employees. The Bank's employees are not represented by any union or other collective bargaining agreement and the Bank considers its relations with employees to be excellent.

Supervision and Regulation

Recent Developments

On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act, or Dodd-Frank, was signed into law. Dodd-Frank will have a broad impact on the financial services industry and will impose significant new regulatory and compliance requirements, including the designation of certain financial companies as systemically significant, the imposition of increased capital, leverage and liquidity requirements, and numerous other provisions designed to improve supervision and oversight of, and strengthen safety and soundness within, the financial services sector. Additionally, Dodd-Frank establishes a new framework of authority to conduct systemic risk oversight within the financial system to be distributed among new and existing regulatory agencies, including the Financial Stability Oversight Council, or Council, the Board of Governors of the Federal Reserve System, or FRB, the Office of the Comptroller of the Currency, or OCC, and the FDIC. The rules and regulations promulgated under Dodd-Frank are likely to impact our operations and cost. Dodd-Frank includes, among other things, the following:

(i) the creation of a Financial Stability Oversight Counsel to identify emerging systemic risks and improve interagency cooperation;

(ii) requirement by statute that bank holding companies serve as a source of financial strength for their depository institution subsidiaries;

(iii) the elimination and phase-out of trust preferred securities from Tier 1 capital with certain exceptions;

(iv) the elimination of remaining barriers to de novo interstate branching by banks;

(v) expanded FDIC resolution authority to conduct the orderly liquidation of certain systemically significant non-bank financial companies in addition to depository institutions;

(vi) enhanced regulation of financial markets, including the derivative and securitizations markets, and the elimination of certain proprietary trading activities by banks;

(vii) the establishment of strengthened capital and liquidity requirements for banks and bank holding companies, including minimum leverage and risk-based capital requirements no less than the strictest requirements in effect for depository institutions as of the date of enactment;

(viii) a permanent increase of the previously implemented temporary increase of FDIC deposit insurance to $250,000 and an extension of federal deposit coverage until January 1, 2013 for the full net amount held by depositors in non-interest bearing transaction accounts;

(ix) authorization for financial institutions to pay interest on business checking accounts;

(x) changes in the calculation of FDIC deposit insurance assessments, such that the assessment base will no longer be the institution’s deposit base, but instead, will be its average consolidated total assets less its average tangible equity and increase the minimum reserve ratio for the Deposit Insurance Fund, or DIF, from 1.15 percent to 1.35 percent;

(xi) the transfer of oversight of savings and loan holding companies to the FRB, federally chartered thrift institutions to the Office of the Comptroller of the Currency and state-chartered savings banks to the FDIC, and the elimination of the Office of Thrift Supervision;

(xii) the creation of a Consumer Financial Protection Bureau, or CFPB, which is authorized to promulgate and enforce consumer protection regulations relating to bank and non-bank financial products and examine and enforce these regulations on banks with more than $10 billion in assets;

(xiii) expanded restrictions on transactions with affiliates and insiders under Sections 23A and 23B of the Federal Reserve Act and lending limits for derivative transactions, repurchase agreements and securities lending and borrowing transactions; and

(xiv) provisions that affect corporate governance and executive compensation at most United States publicly traded companies, including (1) stockholder advisory votes on executive compensation, (2) executive compensation "clawback" requirements for companies listed on national securities exchanges in the event of materially inaccurate statements of earnings, revenues, gains or other criteria similar to the requirements of the American Recovery and Reinvestment Act of 2009 for the Troubled Assets Relief Program Capital Purchase Program for the SEC recipients, (3) enhances independence requirements for compensation committee members, and (4) authority for the SEC to adopt proxy access rules which would permit stockholders of publicly traded companies to nominate candidates for election as a director and have those nominees included in a company's proxy statement.

We cannot predict the extent to which the interpretations and implementation of this wide-ranging federal legislation may affect us. Many of the requirements of Dodd-Frank will be implemented over time and most will be subject to regulations implemented over the course of several years. There can be no assurance that these or future reforms (such as possible new standards for commercial real estate lending or new stress testing guidance for all banks) arising out of studies and reports required by Dodd-Frank will not significantly increase our compliance or other operating costs and earnings or otherwise have a significant impact on our business, financial condition and results of operations. Dodd-Frank is likely to impose upon us more stringent capital, liquidity and leverage requirements or otherwise adversely affect our business. As a result of the changes required by Dodd-Frank, the profitability of our business activities may be impacted and we may be required to make changes to certain of our business practices. These changes may also require us to invest significant management attention and resources to evaluate and make any changes necessary to comply with new statutory and regulatory requirements.

In response to the financial crisis affecting the banking system and financial markets and going concern threats to investment banks and other financial institutions, on October 3, 2008, the Emergency Economic Stabilization Act of 2008, or the EESA, became law. Through its authority under the EESA, the Treasury announced in October 2008 the Troubled Asset Relief Program—Capital Purchase Program, or the CPP, a program designed to bolster healthy institutions, like First California, by making $250 billion of capital available to U.S. financial institutions in the form of preferred stock.

We participated in the CPP in December 2008 so that we could continue to lend and support our current and prospective clients, especially during this unstable economic environment. Under the terms of our participation, we received $25 million in exchange for the issuance of preferred stock and a warrant to purchase common stock, and became subject to various requirements, including certain restrictions on paying dividends on our common stock and repurchasing our equity securities, unless the Treasury has consented. The common stock warrant entitled the Treasury to purchase 599,042 shares of our common stock at an exercise price of $6.26 for a term of ten years. On July 14, 2011, we redeemed all 25,000 preferred stock series B shares and exited the CPP program. On August 24, 2011, we purchased the 10-year warrant from the Treasury for $599,042. In connection with the redemption of the preferred stock series B shares, the Company accelerated the amortization of the remaining difference between the par amount and the initially recorded fair value of the preferred stock series B shares. This $1.1 million deemed dividend reduced the amount of net income available to common shareholders in 2011.

We redeemed the $25 million of preferred stock series B shares with the $25 million of proceeds received in exchange for issuing 25,000 preferred stock series C shares to the Treasury as a participant in the Small Business Lending Fund program, or the SBLF. The preferred stock series C shares will receive non-cumulative quarterly dividends and the initial dividend rate was 5 percent. The dividend rate can fluctuate between 1 percent and 5 percent during the next eight quarters and is a function of the growth in qualified small business loans each quarter.

The EESA also temporarily increased FDIC deposit insurance on most accounts from $100,000 to $250,000. Dodd-Frank made the $250,000 deposit insurance limit permanent. In addition, the FDIC has implemented two temporary programs under the Temporary Liquidity Guaranty Program, or the TLGP, to provide deposit insurance for the full amount of most non-interest bearing transaction accounts through June 30, 2010 (for depository institutions that did not opt out prior to November 2, 2009) and to guarantee certain unsecured debt of financial institutions and their holding companies through June 2012. The Bank did not participate in these TLGP programs. Dodd-Frank extended until January 1, 2013 deposit insurance for the full net amount of non-interest bearing transaction accounts. The FDIC charges “systemic risk special assessments” to depository institutions that participate in the TLGP. The FDIC has recently proposed that Congress give the FDIC expanded authority to charge fees to the holding companies which benefit directly and indirectly from the FDIC guarantees. See “FDIC Deposit Insurance” below.

Dodd-Frank adopts the so-called “Volcker Rule” which, subject to a transition period and certain exceptions, will become effective on July 21, 2012 and prohibits a banking entity from engaging in “proprietary trading,” which is defined as engaging as principal for the “trading account” of the banking entity in securities or other instruments, as determined by federal regulators. After the conformance period commencing July 21, 2012, the Volcker Rule prohibitions and restrictions will apply to banking entities, including the Company, the Bank and their affiliates, unless an exception applies. Certain forms of proprietary trading may qualify as “permitted activities,” and thus not be subject to the ban on proprietary trading, such as “market-making-related activities”, “risk-mitigating hedging activities”, and trading in U.S. government or agency obligations, certain other U.S., state or municipal obligations, and the obligations of Fannie Mae, Freddie Mac or Ginnie Mae. Additionally, subject to a transition period and certain exceptions, the rule restricts a banking entity from sponsoring or investing in certain private funds. A banking entity that sponsors or invests in certain private funds is also restricted from providing credit or other support to the fund or permitting the fund to use the name of the bank. In October 2011, the OCC, FRB, FDIC, and SEC, in consultation with the Commodity Futures Trading Commission, jointly released a notice of proposed rulemaking implementing the

Volcker Rule limitations of Dodd-Frank. In light of the complexity of the proposed regulation and the likelihood that a substantial number of comments will be submitted, the Company cannot fully assess the impact of the Volcker Rule on its business until final rules and regulations are adopted.

General

Banking is a complex, highly regulated industry. The primary goals of the regulatory scheme are to maintain a safe and sound banking system, protect depositors and the FDIC insurance fund, and facilitate the conduct of sound monetary policy. This regulatory scheme is not designed for the benefit of stockholders of the Company or its successors. In furtherance of these goals, Congress and the states have created several largely autonomous regulatory agencies and enacted numerous laws that govern banks, bank holding companies and the financial services industry. Consequently, the growth and earnings performance of the Company or its successors and the Bank can be affected not only by management decisions and general economic conditions, but also by the requirements of applicable state and federal statues, regulations and the policies of various governmental regulatory authorities, including the FRB, the FDIC, the DFI, and the United States Department of the Treasury, or the Treasury.

The commercial banking business is also influenced by the monetary and fiscal policies of the federal government and the policies of the FRB. The FRB implements national monetary policies (with objectives such as curbing inflation and combating recession) by its open-market operations in United States Government securities, by adjusting the required level of reserves for financial intermediaries subject to its reserve requirements and by varying the discount rates applicable to borrowings by depository institutions. The actions of the FRB in these areas influence the growth of bank loans, investments and deposits and also affect interest rates charged on loans and paid on deposits. Indirectly, such actions may also impact the ability of non-bank financial institutions to compete with the Bank. The nature and impact of any future changes in monetary policies cannot be predicted.

The system of supervision and regulation applicable to financial services businesses governs most aspects of the business of the Company and the Bank, including: (i) the scope of permissible business; (ii) investments; (iii) reserves that must be maintained against deposits; (iv) capital levels that must be maintained; (v) the nature and amount of collateral that may be taken to secure loans; (vi) the establishment of new branches; (vii) mergers and consolidations with other financial institutions; and (viii) the payment of dividends.

From time to time laws or regulations are enacted which have the effect of increasing the cost of doing business, limiting or expanding the scope of permissible activities, or changing the competitive balance between banks and other financial and non-financial institutions. Proposals to change the laws and regulations governing the operations of banks and bank holding companies are frequently made in Congress, in the California legislature and by various bank and other regulatory agencies. For example, as noted above, Dodd-Frank, among other things, creates CFPB which has broad powers to regulate consumer financial services and products, creates the Financial Stability Oversight Council with regulatory authority over certain financial companies and activities, and would give shareholders a "say on pay" regarding executive compensation. The FRB has also issued proposed guidance on incentive compensation to ensure that banking organizations' incentive compensation policies do not undermine the safety and soundness of their organizations. Future changes in the laws, regulations or polices that impact the Company or its successors and the Bank cannot necessarily be predicted, but they may have a material effect on the business and earnings of the Company and the Bank.

Set forth below is a summary description of certain of the material laws and regulations that relate to our operations and those of the Bank. The description does not purport to be a complete description of these laws and regulations and is qualified in its entirety by reference to the applicable laws and regulations.

Regulation of First California

As a registered bank holding company, First California and its subsidiaries are subject to the FRB's supervision, regulation and examination under the BHCA. Under the BHCA, we are subject to periodic examination by the FRB. We are also required to file with the FRB periodic reports of our operations and such additional information regarding the Company and its subsidiaries as the FRB may require.

Under FRB regulations, a bank holding company is required to serve as a source of financial and managerial strength to its subsidiary banks and may not conduct its operations in an unsafe or unsound manner. In addition, it is the FRB's policy that in serving as a source of strength to its subsidiary banks, a bank holding company should stand ready to use available resources to provide adequate capital funds to its subsidiary banks during periods of financial stress or adversity and should maintain the financial flexibility and capital-raising capacity to obtain additional resources for assisting its subsidiary banks. A bank holding company's failure to meet its obligations to serve as a source of strength to its subsidiary banks will generally be considered by the FRB to be an unsafe and unsound banking practice or a violation of the FRB's regulations or both.

Dodd-Frank amends the Federal Deposit Insurance Act, or FDIA, to obligate the FRB to require bank holding companies to serve as a source of financial strength for any subsidiary depository institution. The appropriate federal banking agency for such a depository institution may require reports from companies that own the insured depository institution to assess their ability to serve as a source of strength and to enforce compliance with the source-of-strength requirements. The term “source of financial strength” is defined as the ability of a company to provide financial assistance to its insured depository institution subsidiaries in the event of financial distress at such subsidiaries. Under this requirement, First California in the future could be required to provide financial assistance to the Bank should it experience financial distress.

First California is required to obtain the FRB’s prior approval before acquiring ownership or control of more than 5% of the outstanding shares of any class of voting securities, or substantially all the assets, of any company, including a bank or bank holding company. Further, we are allowed to engage, directly or indirectly, only in banking and other activities that the FRB deems to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. Pursuant to the GLBA, in order to elect and retain financial holding company status, a bank holding company and all depository institution subsidiaries must be well capitalized, well managed, and, except in limited circumstances, be in satisfactory compliance with the Community Reinvestment Act, or the CRA.

First California’s securities are registered with the Securities and Exchange Commission, or the SEC, under the Securities Exchange Act of 1934, as amended, or the Exchange Act, and listed on the NASDAQ Global Select Market. As such, First California is subject to the information, proxy solicitation, insider trading, corporate governance, and other requirements and restrictions of the Exchange Act, as well as the Marketplace Rules and other requirements promulgated by the NASDAQ Stock Market, Inc.

First California is subject to the accounting oversight and corporate governance requirements of the Sarbanes-Oxley Act of 2002, including, among other things, required executive certification of financial reports, increased requirements for board audit committees and their members, and enhanced disclosure of controls and procedures and internal controls over financial reporting.

First California's earnings and activities are affected by legislation, by regulations and by local legislative and administrative bodies and decisions of courts in the jurisdictions in which First California and the Bank conduct business. For example, these include limitations on the ability of the Bank to pay dividends to us and our ability to pay dividends to our stockholders. It is the policy of the FRB that bank holding companies should pay cash dividends on common stock only out of income available over the past year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividends that undermines the bank holding company's ability to serve as a source of strength to its banking subsidiaries. Various federal and state statutory provisions limit the amount of dividends that subsidiary banks can pay to their holding companies without regulatory approval. In addition to these explicit limitations, the federal regulatory agencies have general authority to prohibit a banking subsidiary or bank holding company from engaging in an unsafe or unsound banking practice. Depending upon the circumstances, the agencies could take the position that paying a dividend would constitute an unsafe or unsound banking practice. In addition, as discussed below under "Regulation of the Bank", a bank holding company such as the Company is required to maintain minimum ratios of Tier 1 capital and total capital to total risk-weighted assets, as well as a minimum ratio of Tier 1 capital to total adjusted quarterly average assets as defined in such regulations.

Under the terms of the SBLF, for so long as any preferred stock issued under the SBLF remains outstanding, First California is permitted to make dividend payments to, or effectuate share repurchases from, other shareholders, provided that after the payment or repurchase, the institution's Tier 1 capital would be at least 90 percent of the amount existing at the time immediately after the SBLF closing date, excluding any subsequent net charge-offs and partial repayments of the SBLF funding.

Regulation of the Bank

The Bank is extensively regulated under both federal and state law. The Bank, as a California state chartered bank which is not a member of the Federal Reserve System, is subject to regulation, supervision, and regular examination by the DFI and the FDIC. The Bank's deposits are insured by the FDIC up to the maximum extent provided by law. The regulations of these agencies govern most aspects of the Bank's business. California law exempts all banks from usury limitations on interest rates. Various consumer laws and regulations also affect the Bank's operations, such as the CRA, the Equal Credit Opportunity Act, the Truth in Lending Act, the Fair Housing Act, the Home Mortgage Disclosure Act, and the Real Estate Settlement Procedures Act. These laws primarily protect depositors and other customers of the Bank, rather than First California or its stockholders. The creation of the CFPB by Dodd-Frank is also likely to lead to enhanced and strengthened enforcement of consumer financial protection laws. On July 21, 2011, the CFPB assumed its authority to supervise and enforce existing consumer financial protection rules. On January 4, 2012, President Obama named Richard Cordray as the Director of the CFPB via recess appointment. The validity of this recess appointment may be subject to challenge, creating uncertainty because the full authority to approve new consumer financial protection rules is vested in the director of the CFPB. Additionally, Dodd-Frank does not allow the CFPB to promulgate regulations until it has a director that has been confirmed by the Senate. At this time it is still unclear as to whether the recess appointment is sufficient to meet this statutory requirement. Accordingly, at this time the Company cannot fully assess the impact of the CFPB on its business.

Various requirements and restrictions under the laws of the State of California and the United States affect the operations of the Bank. State and federal statutes and regulations relate to many aspects of the Bank's operations, including standards for safety and soundness, reserves against deposits, interest rates payable on deposits and loans, investments, mergers and acquisitions, borrowings, dividends, locations of branch offices, fair lending requirements, CRA activities and loans to affiliates. Further, the Bank is required to maintain certain levels of capital.

Dividends and Capital Distributions

Dividends and capital distributions from the Bank constitute the principal source of cash to First California. As a result, First California's ability to pay dividends on its capital stock will depend primarily on the ability of the Bank to pay dividends to First California in amounts sufficient to service its obligations. The Bank is subject to various federal or state statutory and regulatory limitations on its ability to pay dividends and capital distributions to its shareholder, generally based on capital levels and current or retained earnings. The ability of the Bank to pay dividends is also subject to regulatory restrictions if paying dividends would impair its profitability, financial condition or other cash flow requirements.

The FRB has issued a policy statement with regard to the payment of cash dividends by bank holding companies. The policy statement provides that, as a matter of prudent banking, a bank holding company should not maintain a rate of cash dividends unless its net income available to common stockholders has been sufficient to fully fund the dividends, and the prospective rate of earnings retention appears to be consistent with the holding company's capital needs, asset quality and overall financial condition. Accordingly, a bank holding company should not pay cash dividends that exceed its net income or can only be funded in ways that weaken the bank holding company's financial health, such as by borrowing.

Under California law, banks may declare a cash dividend out of their net profits up to the lesser of retained earnings or the net income for the last three fiscal years (less any distributions made to shareholders during such period), or with the prior written approval of the DFI, in an amount not exceeding the greatest of (i) the retained earnings of the Bank, (ii) the net income of the Bank for its last fiscal year or (iii) the net income of the Bank for its current fiscal year. In addition, under federal law, banks are prohibited from paying any dividends if after making such payment they would fail to meet any of the minimum regulatory capital requirements. The federal regulators also have the authority to prohibit state banks from engaging in any business practices which are considered to be unsafe or unsound, and in some circumstances the regulators might prohibit the payment of dividends on that basis even though such payments would otherwise be permissible.

The Bank may from time to time be permitted to make additional capital distributions to its shareholder with the consent of the DFI. It is not anticipated that such consent could be obtained unless the distributing bank were to remain "well-capitalized" following such distribution.

Regulatory Capital Guidelines. Both the Company and the Bank are required to maintain certain levels of capital. The FRB and the FDIC have substantially similar risk-based capital ratio and leverage ratio guidelines for banking organizations. The current risk-based capital guidelines that apply to First California and the Bank, commonly referred to as Basel I, are based upon the 1988 capital accord of the International Basel Committee on Banking Supervision, or the Basel Committee, a committee of central banks and bank supervisors. The guidelines are intended to ensure that banking organizations have adequate capital given the risk levels of assets and off-balance sheet financial instruments.

Under the existing Basel I-based guidelines, the minimum ratio of total capital to risk-weighted assets (which are primarily the credit risk equivalents of balance sheet assets and certain off-balance sheet items such as standby letters of credit, but also include a nominal market risk equivalent balance related to foreign exchange and debt/equity trading activities) is eight percent, of which at least four percent must be composed of tier 1 capital. The FRB also has adopted a minimum leverage ratio for most bank holding companies, requiring tier 1 capital of at least four percent of average quarterly total consolidated assets, net of loan loss reserve, goodwill and certain other intangible assets. The federal banking regulators have also established risk-based and leverage capital guidelines that insured banks are required to meet. These regulations are generally similar to those established by the FRB for bank holding companies.

For purposes of calculating the ratios, a banking organization's assets and some of its specified off-balance sheet commitments and obligations are assigned to various risk categories. A depository institution's or holding company's capital, in turn, is classified in one of three tiers, depending on type:

- Core Capital (Tier 1): Tier 1 capital includes common equity, retained earnings, qualifying non-cumulative perpetual preferred stock, a limited amount of qualifying cumulative perpetual stock at the holding company level, minority interests in equity accounts of consolidated subsidiaries, and qualifying trust preferred securities less goodwill, most intangible assets and certain other assets.

- Supplementary Capital (Tier 2): Tier 2 capital includes, among other things, perpetual preferred stock and trust preferred securities not meeting the Tier 1 definition, qualifying mandatory convertible debt securities, qualifying subordinated debt, and allowances for possible loan and lease losses, subject to limitations.

- Market Risk Capital (Tier 3): Tier 3 capital includes qualifying unsecured subordinated debt.

The following table sets forth the regulatory capital guidelines and the actual capitalization levels for the Bank and the Company as of December 31, 2011 and 2010:

	Actual			For Capital Adequacy Purposes		To be Well-Capitalized Under Prompt Corrective Action Provision	
	Amount	Ratio		Amount (in thousands)	Ratio	Amount	Ratio
December 31, 2011							
Total capital (to risk weighted assets)							
First California Financial Group, Inc.	$ 194,694	17.32	%	$ 89,924	≥ 8.00 %		
First California Bank	$ 192,227	17.10	%	$ 89,944	≥ 8.00 %	$ 112,430	≥ 10.00 %
Tier I capital (to risk weighted assets)							
First California Financial Group, Inc.	$ 180,597	16.07	%	$ 44,962	≥ 4.00 %		
First California Bank	$ 178,126	15.84	%	$ 44,972	≥ 4.00 %	$ 67,458	≥ 6.00 %
Tier I capital (to average assets)							
First California Financial Group, Inc.	$ 180,597	10.33	%	$ 69,906	≥ 4.00 %		
First California Bank	$ 178,126	10.18	%	$ 69,968	≥ 4.00 %	$ 87,460	≥ 5.00 %

	Actual			For Capital Adequacy Purposes		To be Well-Capitalized Under Prompt Corrective Action Provision	
	Amount	Ratio		Amount (in thousands)	Ratio	Amount	Ratio
December 31, 2010							
Total capital (to risk weighted assets)							
First California Financial Group, Inc.	$ 172,599	16.79	%	$ 82,242	≥ 8.00 %		
First California Bank	$ 167,395	16.31	%	$ 82,090	≥ 8.00 %	$ 102,613	≥ 10.00 %
Tier I capital (to risk weighted assets)							
First California Financial Group, Inc.	$ 159,695	15.53	%	$ 41,121	≥ 4.00 %		
First California Bank	$ 154,515	15.06	%	$ 41,045	≥ 4.00 %	$ 61,658	≥ 6.00 %
Tier I capital (to average assets)							
First California Financial Group, Inc.	$ 159,695	11.00	%	$ 58,052	≥ 4.00 %		
First California Bank	$ 154,515	10.63	%	$ 58,134	≥ 4.00 %	$ 72,668	≥ 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.

The Basel Accords. The current risk-based capital guidelines which apply to First California and the Bank are based upon the 1988 capital accord of the Basel Committee. A new international accord, referred to as Basel II, became mandatory for large, internationally active banking organizations, known as “core” banking organizations, in 2008 (total assets of $250 billion or more or consolidated foreign exposures of $10 billion or more). Basel II emphasizes internal assessment of credit, market and operational risk, as well as supervisory assessment and market discipline in determining minimum capital requirements. It is optional for other banks, and if adopted, must first be complied with in a “parallel run” for two years along with the existing Basel I standards. In January 2009, the Basel Committee proposed to reconsider regulatory-capital standards, supervisory and risk-management requirements and additional disclosures to further strengthen the Basel II framework in response to recent worldwide developments. First California is not required to comply with Basel II and elected not to apply the Basel II requirements when they became effective.

On September 12, 2010, the Group of Governors and Heads of Supervision, the oversight body of the Basel Committee, announced agreement on the calibration and phase-in arrangements for a strengthened set of capital requirements, known as Basel III. Under these standards, when fully phased-in on January 1, 2019, banking institutions will be required to satisfy three risk-based capital ratios:

- A tier 1 common equity ratio of at least 7.0%, inclusive of 4.5% minimum tier 1 common equity ratio, net of regulatory deductions, and the new 2.5% “capital conservation buffer” of common equity to risk-weighted assets;

- A tier 1 capital ratio of at least 8.5%, inclusive of the 2.5% capital conservation buffer; and

- A total capital ratio of at least 10.5%, inclusive of the 2.5% capital conservation buffer.

The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a tier 1 common equity ratio above the minimum but below the conservation buffer may face constraints on dividends, equity repurchases and compensation based on the amount of such shortfall. The Basel Committee also announced a “countercyclical buffer” of 0% to 2.5% of common equity or other loss-absorbing capital “will be implemented according to national circumstances” as an “extension” of the conservation buffer during periods of excess credit growth.

Basel III introduces a non-risk adjusted tier 1 leverage ratio of 3%, based on a measure of total exposure rather than total assets and new liquidity standards. The phase-in of the new rules is to commence on January 1, 2013, with the phase-in of the capital conservation buffer commencing on January 1, 2015 and the rules to be fully phased-in by January 1, 2019.

In November 2010, Basel III was endorsed by the Seoul G20 Leaders Summit and will be subject to individual adoption by member nations, including the United States. On December 16, 2010, the Basel Committee issued text of the Basel III rules, which presents the details of global regulatory standards on bank capital adequacy and liquidity agreed to by the Basel Committee and endorsed by the Seoul G20 Leaders Summit. The federal banking agencies will likely implement changes to the current capital adequacy standards applicable to First California and the Bank in light of Basel III. If adopted by federal banking agencies, Basel III could lead to significantly higher capital requirements and more restrictive leverage and liquidity ratios. First California cannot determine the ultimate effect that potential legislation, or subsequent regulations, if enacted, would have upon First California's earnings or financial position. In addition, significant questions remain as to how the capital and liquidity mandates of Dodd-Frank will be integrated with the requirements of Basel III.

Note that Dodd-Frank also requires the establishment of more stringent prudential standards by requiring the federal banking agencies to adopt capital and liquidity requirements which address the risks that the activities of an institution pose to the institution and the public and private stakeholders, including risks arising from certain enumerated activities. In particular, Dodd-Frank excludes trust preferred securities issued on or after May 19, 2010 from tier 1 capital. For depository institution holding companies with total consolidated assets of more than $15 billion at December 31, 2009, trust preferred securities issued before May 19, 2010 will be phased-out of tier 1 capital over a three-year period.

Prompt Corrective Action and Other General Enforcement Authority. The Federal Deposit Insurance Corporation Improvement Act, or FDICIA, requires each federal banking agency to take prompt corrective action to resolve the problems of insured depository institutions, including undercapitalization. Each federal banking agency has issued regulations defining five capital categories: "well- capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized," and "critically undercapitalized." Under the regulations, a bank shall be deemed to be:

- "well-capitalized" if it has a total risk-based capital ratio of 10.0% or more, has a Tier 1 risk-based capital ratio of 6.0% or more, has a leverage capital ratio of 5.0% or more, and is not subject to specified requirements to meet and maintain a specific capital level for any capital measure;

- "adequately capitalized" if it has a total risk-based capital ratio of 8.0% or more, a Tier 1 risk-based capital ratio of 4.0% or more, and a leverage capital ratio of 4.0% or more (3.0% under certain circumstances) and does not meet the definition of "well capitalized";

- "undercapitalized" if it has a total risk-based capital ratio that is less than 8.0%, a Tier 1 risk-based capital ratio that is less than 4.0%, or a leverage capital ratio that is less than 4.0% (3.0% under certain circumstances);

- "significantly undercapitalized" if it has a total risk-based capital ratio that is less than 6.0%, a Tier 1 risk-based capital ratio that is less than 3.0% or a leverage capital ratio that is less than 3.0%; and

- "critically undercapitalized" if it has a ratio of tangible equity to total assets that is equal to or less than 2.0%.

Banks are prohibited from paying dividends or management fees to controlling persons or entities if, after making the payment, the bank would be “undercapitalized,” that is, the bank fails to meet the required minimum level for any relevant capital measure. Asset growth and branching restrictions apply to “undercapitalized” banks. Banks classified as “undercapitalized” are required to submit acceptable capital plans guaranteed by their holding companies, if any. Broad regulatory authority was granted with respect to “significantly undercapitalized” banks, including forced mergers, growth restrictions, ordering new elections for directors, forcing divestiture by its holding company, if any, requiring management changes, and prohibiting the payment of bonuses to senior management. Even more severe restrictions are applicable to “critically undercapitalized” banks, those with capital at or less than 2%. Restrictions for these banks include the appointment of a receiver or conservator. All of the federal banking agencies have promulgated substantially similar regulations to implement this system of prompt corrective action.

A bank, based upon its capital levels, that is classified as “well capitalized,” “adequately capitalized” or “undercapitalized” may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for a hearing, determines that an unsafe or unsound condition, or an unsafe or unsound practice, warrants such treatment. At each successive lower capital category, an insured bank is subject to more restrictions. The federal banking agencies, however, may not treat an institution as “critically undercapitalized” unless its capital ratios actually warrant such treatment.

In addition to measures taken under the prompt corrective action provisions, insured banks may be subject to potential enforcement actions by the federal banking agencies for unsafe or unsound practices in conducting their businesses or for violations of any law, rule, regulation or any condition imposed in writing by the agency or any written agreement with the agency. Enforcement actions may include the imposition of a conservator or receiver, the issuance of a cease-and-desist order that can be judicially enforced, the termination of insurance of deposits (in the case of a depository institution), the imposition of civil money penalties, the issuance of directives to increase capital, the issuance of formal and informal agreements, the issuance of removal and prohibition orders against institution-affiliated parties. The enforcement of such actions through injunctions or restraining orders may be based upon a judicial determination that the agency would be harmed if such equitable relief was not granted.

The DFI, as the primary regulator for California state-chartered banks, also has a broad range of enforcement measures, from cease and desist powers and the imposition of monetary penalties to the ability to take possession of a bank, including causing its liquidation.

Safety and Soundness Standards. The federal banking agencies have adopted guidelines designed to assist the federal banking agencies in identifying and addressing potential safety and soundness concerns before capital becomes impaired. The guidelines set forth operational and managerial standards relating to (i) internal controls, information systems and internal audit systems; (ii) loan documentation; (iii) credit underwriting; (iv) asset growth; (v) earnings; and (vi) compensation, fees and benefits.

In addition, the federal banking agencies have also adopted safety and soundness guidelines with respect to asset quality and for evaluating and monitoring earnings to ensure that earnings are sufficient for the maintenance of adequate capital and reserves. These guidelines provide six standards for establishing and maintaining a system to identify problem assets and prevent those assets from deteriorating. Under these standards, an insured depository institution should (i) conduct periodic asset quality reviews to identify problem assets; (ii) estimate the inherent losses in problem assets and establish reserves that are sufficient to absorb estimated losses; (iii) compare problem asset totals to capital; (iv) take appropriate corrective action to resolve problem assets; (v) consider the size and potential risks of material asset concentrations; and (vi) provide periodic asset quality reports with adequate information for management and the board of directors to assess the level of asset risk.

Transactions with Affiliates. Under Sections 23A and 23B of the Federal Reserve Act and the FRB's Regulation W, loans by the Bank to affiliates, investments by them in affiliates' stock, and taking affiliates' stock as collateral for loans to any borrower is limited to 10% of the Bank's capital, in the case of any one affiliate, and is limited to 20% of the Bank's capital, in the case of all affiliates. The Bank's holding company and any subsidiaries it may purchase or organize are generally deemed to be affiliates of the Bank within the meaning of Section 23A and 23B and Regulation W. In addition, transactions between the Bank and other affiliates must be on terms and conditions that are consistent with safe and sound banking practices; in particular, a bank and its subsidiaries generally may not purchase from an affiliate a low-quality asset, as defined in the Federal Reserve Act. These restrictions also prevent a bank holding company and its other affiliates from borrowing from a banking subsidiary of the bank holding company unless the loans are secured by marketable collateral of designated amounts. The Company or its successors and the Bank are also subject to certain restrictions with respect to engaging in the underwriting, public sale and distribution of securities.

Dodd-Frank generally enhances the restrictions on transactions with affiliates under Section 23A and 23B, including an expansion of the definition of "covered transactions" to include credit exposures related to derivatives, repurchase agreements and securities lending arrangements, and an increase in the amount of time for which collateral requirements regarding covered credit transactions must be satisfied. The definition of "affiliate" was expanded to include any investment fund to which First California or an affiliate serves as an investment adviser. The ability of the FRB to grant exemptions from these restrictions was also narrowed, including by requiring coordination with other bank regulators.

Loans to Insiders. Extensions of credit by the Bank to insiders of both the Bank and First California are subject to prohibitions and other restrictions imposed by federal regulations. For purposes of these limits, "insiders" include directors, executive officers and principal shareholders of the Bank or First California and their related interests. The term "related interest" means a company controlled by a director, executive officer or principal shareholder of the Bank or First California. The Bank may not extend credit to an insider of the Bank or First California unless the loan is made on substantially the same terms as, and subject to credit underwriting procedures that are no less stringent than, those prevailing at the time for comparable transactions with non-insiders. Under federal banking regulations, the Bank may not extend a loan to insiders in an amount greater than $500,000 without prior board approval (with any interested person abstaining from participating directly or indirectly in the voting). The federal regulations place additional restrictions on loans to executive officers, and generally prohibit loans to executive officers other than for certain specified purposes. The Bank is required to maintain records regarding insiders and extensions of credit to them.

Federal Deposit Insurance. The FDIC insures our customer deposits through the Deposit Insurance Fund, or the DIF, up to prescribed limits for each depositor. Pursuant to the EESA, the basic limit on federal deposit insurance coverage was temporarily raised from $100,000 to $250,000 per depositor. Dodd-Frank made the $250,000 deposit insurance limit permanent. The federal banking agencies also recently issued final rules implementing the Dodd-Frank repeal of the prohibition on paying interest on demand deposits. Further, as required under Section 343 of Dodd-Frank, the FDIC has adopted a final rule that provides temporary unlimited deposit insurance coverage for non-interest-bearing transaction accounts. As mandated by Dodd-Frank, the FDIC will fully insure the amounts in non-interest-bearing transaction accounts without limits from December 31, 2010 through December 31, 2012. The unlimited coverage would be separate from, and in addition to, the coverage provided to depositors with other accounts held at an institution. Beginning January 1, 2013, the unlimited coverage will cease and these accounts will be insured under the FDIC's general deposit insurance coverage rules.

Dodd-Frank changes the deposit insurance assessment framework, primarily by basing assessments on an institution's total assets less tangible equity (subject to risk-based adjustments that would further reduce the assessment base for custodial banks) rather than domestic deposits, which is expected to shift a greater portion of the aggregate assessments to large banks. Dodd-Frank also increases the minimum designated reserve ratio of the DIF from 1.15% to 1.35% of the estimated amount of total insured deposits by September 30, 2020, eliminates the upper limit for the reserve ratio designated by the FDIC each year, and eliminates the requirement that the FDIC pay dividends to depository institutions when the reserve ratio exceeds certain thresholds.

On December 14, 2010, the FDIC raised the minimum designated reserve ratio of the DIF to 2%. The ratio is higher than the minimum reserve ratio of 1.35% as set by Dodd-Frank.

On February 7, 2011, the FDIC approved a final rule on Assessments, Dividends, Assessment Base and Large Bank Pricing. The final rule, mandated by Dodd-Frank, changes the deposit insurance assessment system from one that is based on domestic deposits to one that is based on average consolidated total assets minus average tangible equity. Because the new assessment base under Dodd-Frank is larger than the current assessment base, the final rule's assessment rates are lower than the current rates, which achieves the FDIC's goal of not significantly altering the total amount of revenue collected from the industry. In addition, the final rule adopts a "scorecard" assessment scheme for larger banks and suspends dividend payments if the DIF reserve ratio exceeds 1.5 % but provides for decreasing assessment rates when the DIF reserve ratio reaches certain thresholds. The final rule further reduces the assessment base for custodial banks by the daily or weekly average of a certain amount of low-risk assets (i.e., assets with a Basel risk weighting of 0%, regardless of maturity, plus 50% of assets with a Basel risk weighting of 20%, again regardless of maturity) subject to the limitation that the daily or weekly average value of these assets cannot exceed the daily or weekly average value of those deposits classified as transaction accounts and identified by the institution as being directly linked to a fiduciary or custodial and safekeeping account. The final rule identifies custodial banks as insured depository institutions with previous calendar year-end trust assets (i.e., fiduciary and custody and safekeeping assets) of at least $50 billion or those insured depository institutions that derived more than 50% of their revenue (interest income plus non-interest income) from trust activity over the previous calendar year. The final rule took effect for the quarter beginning April 1, 2011, and was reflected in the invoices for assessments due September 30, 2011.

Continued action by the FDIC to replenish the DIF, as well as the changes in Dodd-Frank, are likely to result in higher assessment rates, which would reduce the profitability of the Bank.

In addition to its insurance assessment, each insured bank was subject in 2011 to quarterly debt service assessments in connection with bonds issued by a government corporation that financed the federal savings and loan bailout. The first quarter 2011 debt service assessment was .0102%.

Money Laundering, Currency Controls and Economic Sanctions. Various federal statutory and regulatory provisions are designed to enhance record-keeping and reporting of currency and foreign transactions. Pursuant to the Bank Secrecy Act, financial institutions must report high levels of currency transactions or face the imposition of civil monetary penalties for reporting violations. The Money Laundering Control Act imposes sanctions, including revocation of federal deposit insurance, for institutions convicted of money laundering.

The International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001, or the IMLAFATA, a part of the USA Patriot Act, authorizes the Secretary of the Treasury, in consultation with the heads of other government agencies, to adopt special measures applicable to banks and other financial institutions to enhance record-keeping and reporting requirements for certain financial transactions that are of primary money laundering concern. Among its other provisions, IMLAFATA requires each financial institution to: (i) establish an anti-money laundering program; (ii) establish due diligence policies, procedures and controls with respect to its private banking accounts and correspondent banking accounts involving individuals and certain foreign banks; and (iii) avoid establishing, maintaining, administering, or managing correspondent accounts in the United States for, or on behalf of, a foreign bank that does not have a physical presence in any country. In addition, IMLAFATA contains a provision encouraging cooperation among financial institutions, regulatory authorities and law enforcement authorities with respect to individuals, entities and organizations engaged in, or reasonably suspected of engaging in, terrorist acts or money laundering activities.

The Treasury's regulations implementing IMLAFATA mandate that federally-insured banks and other financial institutions establish customer identification programs designed to verify the identity of persons opening new accounts, maintain the records used for verification, and determine whether the person appears on any list of known or suspected terrorists or terrorist organizations.

The U.S. Department of the Treasury's Office of Foreign Assets Control, or OFAC, is responsible for requiring that U.S. entities do not engage in transactions with certain prohibited parties, as defined by various Executive Orders and Acts of Congress. OFAC publishes lists of persons, organizations and countries suspected of aiding, harboring or engaging in terrorist acts, known as Specially Designated Nationals and Blocked Persons. If First California and the Bank finds a name on any transaction, account or wire transfer that is on an OFAC list, First California or the Bank must freeze or block such account or transaction, file a report of blocked or rejected transaction and notify OFAC.

Patriot Act. On October 26, 2001, the President signed into law comprehensive anti-terrorism legislation, the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, known as the Patriot Act. The Patriot Act was designed to deny terrorists and others the ability to obtain access to the United States financial system, and has significant implications for depository institutions and other businesses involved in the transfer of money. The Patriot Act, as implemented by various federal regulatory agencies, required financial institutions, including the Bank, to implement policies and procedures or amend existing policies and procedures with respect to, among other matters, anti-money laundering, compliance, suspicious activity and currency transaction reporting and due diligence on customers. The Patriot Act and its underlying regulations also permit information sharing for counter-terrorist purposes between federal law enforcement agencies and financial institutions, as well as among financial institutions, subject to certain conditions, and require the FRB and other federal banking agencies to evaluate the effectiveness of an applicant in combating money laundering activities when considering applications filed under Section 3 of the BHCA or the Bank Merger Act. The Bank has adopted comprehensive policies and procedures to address the requirements of the Patriot Act. The Bank believes that the ongoing cost of compliance with the Patriot Act is not likely to be material to the Bank.

Community Reinvestment Act. The Bank is subject to the CRA. The CRA is intended to encourage insured depository institutions, while operating safely and soundly, to help meet the credit needs of their communities. The CRA specifically directs the federal bank regulatory agencies, in examining insured depository institutions, to assess their record of helping to meet the credit needs of their entire community, including low-and moderate-income neighborhoods, consistent with safe and sound banking practices. The CRA further requires the agencies to take a financial institution’s record of meeting its community credit needs into account when evaluating applications for, among other things, domestic branches, consummating mergers or acquisitions, or holding company formations. The Bank’s compliance with the CRA is reviewed and evaluated by the FDIC, which assigns the Bank a publicly available CRA rating at the conclusion of the examination.

The federal banking agencies have adopted regulations which measure a bank’s compliance with its CRA obligations on a performance-based evaluation system. This system bases CRA ratings on an institution’s actual lending service and investment performance rather than the extent to which the institution conducts needs assessments, documents community outreach or complies with other procedural requirements. In connection with its assessment of CRA performance, the FDIC assigns a rating of “outstanding”, “satisfactory”, “needs to improve” or “substantial noncompliance” Failure of an institution to receive at least a “Satisfactory” rating could inhibit such institution or its holding company from undertaking certain activities, including acquisitions.

The Bank had a CRA rating of “Satisfactory” as of its most recent regulatory examination.

Interstate Banking and Branching. Federal law permits an adequately capitalized and adequately managed bank holding company, with FRB approval, to acquire banking institutions located in states other than the bank holding company’s home state without regard to whether the transaction is prohibited under state law. In addition, national banks and state banks with different home states are permitted to merge across state lines, with the approval of the appropriate federal banking agency, unless the home state of a participating banking institution passed legislation prior to June 1, 1997 that expressly prohibits interstate mergers. Dodd-Frank permits a national bank or a state bank, with the approval of its regulator, to open a branch in any state if the law of the state in which the branch is to be located would permit the establishment of the branch if the bank were a bank chartered in that state.

Sarbanes-Oxley Act. On July 30, 2002, the President signed into law the Sarbanes-Oxley Act of 2002. The Sarbanes-Oxley Act aims to restore the credibility lost as a result of high profile corporate scandals by addressing, among other issues, corporate governance, auditing and accounting, executive compensation and enhanced and timely disclosure of corporate information. The NASDAQ Stock Market has adopted corporate governance rules intended to allow shareholders to more easily and effectively monitor the performance of companies and directors. The principal provisions of the Sarbanes-Oxley Act, many of which have been interpreted through regulations released in 2003, provide for and include, among other things: (i) the creation of the Public Company Accounting Oversight Board; (ii) auditor independence provisions that restrict non-audit services that accountants may provide to their audit clients; (iii) additional corporate governance and responsibility measures, including the requirement that the chief executive officer and chief financial officer of a public company certify financial statements; (iv) the forfeiture of bonuses or other incentive-based compensation and profits from the sale of an issuer's securities by directors and senior officers in the twelve month period following initial publication of any financial statements that later require restatement; (v) an increase in the oversight of, and enhancement of certain requirements relating to, audit committees of public companies and how they interact with that company's independent auditors; (vi) requirements that audit committee members must be independent and are barred from accepting consulting, advisory or other compensatory fees from the issuer; (vii) requirements that companies disclose whether at least one member of the audit committee is a "financial expert' (as such term is defined by the Securities and Exchange Commission, (or "SEC") and if not disclosed, why the audit committee does not have a financial expert; (viii) expanded disclosure requirements for corporate insiders, including accelerated reporting of stock transactions by insiders and a prohibition on insider trading during pension blackout periods; (ix) a prohibition on personal loans to directors and officers, except certain loans made by insured financial institutions on non-preferential terms and in compliance with other bank regulatory requirements; (x) disclosure of a code of ethics and filing a Form 8-K for a change or waiver of such code; (xi) a range of enhanced penalties for fraud and other violations; and (xii) expanded disclosure and certification relating to an issuer's disclosure controls and procedures and internal controls over financial reporting.

As a result of the Sarbanes-Oxley Act, and its implementing regulations, we have incurred substantial costs to interpret and ensure compliance with the law and its regulations. Future changes in the laws, regulation, or policies that impact us cannot necessarily be predicted and may have a material effect on our business and earnings.

Environmental Regulation. Federal, state and local laws and regulations regarding the discharge of harmful materials into the environment may have an impact on the Bank. Since the Bank is not involved in any business that manufactures, uses or transports chemicals, waste, pollutants or toxins that might have a material adverse effect on the environment, the Bank's primary exposure to environmental laws is through its lending activities and through properties or businesses the Bank may own, lease or acquire. Based on a general survey of the Bank's loan portfolio, conversations with local appraisers and the type of lending currently and historically done by the Bank, management is not aware of any potential liability for hazardous waste contamination that would be reasonably likely to have a material adverse effect on the Company or its successors as of the date of this report.

Safeguarding of Customer Information and Privacy. In 1970, the Federal Fair Credit Reporting Act, or the FCRA, was enacted to insure the confidentiality, accuracy, relevancy and proper utilization of consumer credit report information. The FCRA affirmatively preempts state law in a number of areas, including the ability of entities affiliated by common ownership to share and exchange information freely, and the requirements on credit bureaus to reinvestigate the contents of reports in response to consumer complaints, among others.

The Fair and Accurate Credit Transaction Act, or the FACT Act, became law in 2003, effectively extending and amending provisions of the FCRA. The FACT Act created many new responsibilities for consumer reporting agencies and users of consumer reports. It contains many new consumer disclosure requirements as well as provisions to address identity theft.

The FRB and other bank regulatory agencies have adopted guidelines for safeguarding confidential, personal customer information. These guidelines require financial institutions to create, implement and maintain a comprehensive written information security program designed to ensure the security and confidentiality of customer information, protect against any anticipated threats or hazard to the security or integrity of such information and protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer. The Bank has adopted a customer information security program to comply with such requirements.

Federal banking rules also limit the ability of banks and other financial institutions to disclose non-public information about consumers. Pursuant to these rules, financial institutions must provide: (i) initial notices to customers about their privacy policies, describing the conditions under which they may disclose nonpublic personal information to nonaffiliated third parties and affiliates; (ii) annual notices of their privacy policies to current customers; and (iii) a reasonable method for customers to "opt out" of disclosures to nonaffiliated third parties. These privacy provisions affect how consumer information is transmitted through diversified financial companies and conveyed to outside vendors. We have implemented our privacy policies in accordance with the law.

In recent years, a number of states have implemented their own versions of privacy laws. For example, in 2003, California adopted standards that are more restrictive than federal law, allowing bank customers the opportunity to bar financial companies from sharing information with their affiliates. More specifically, the California Financial Information Privacy Act requires a financial institution to provide specific information to a consumer related to the sharing of that consumer's nonpublic personal information. The Act allows a consumer to direct the financial institution not to share his or her nonpublic personal information with affiliated or nonaffiliated companies with which a financial institution has contracted to provide financial products and services, and requires that permission from each such consumer be acquired by a financial institution prior to sharing such information.

Other Aspects of Banking Law. The Bank is also subject to federal statutory and regulatory provisions covering, among other things, security procedures, insider and affiliated party transactions, management interlocks, electronic funds transfers, funds availability, and truth-in-savings. There are also a variety of federal statutes which regulate acquisitions of control and the formation of bank holding companies.

Impact of Monetary Policies

Banking is a business that depends on rate differentials. In general, the difference between the interest rate paid by a bank on its deposits and its other borrowings and the interest rate earned on its loans, securities and other interest-earning assets comprises the major source of a Bank's earnings. These rates are highly sensitive to many factors which are beyond the Bank's control and, accordingly, the earnings and growth of the Bank are subject to the influence of economic conditions generally, both domestic and foreign, including inflation, recession, and unemployment; and also to the influence of monetary and fiscal policies of the United States and its agencies, particularly the FRB. The FRB implements national monetary policy, such as seeking to curb inflation and combat recession, by:

- Open-market dealings in United States government securities;
- Adjusting the required level of reserves for financial institutions subject to reserve requirements; and
- Adjusting the discount rate applicable to borrowings by banks which are members of the Federal Reserve System.

The actions of the FRB in these areas influence the growth of bank loans, investments, and deposits and also affect interest rates. The nature and timing of any future changes in the FRB's policies and their impact on the Company and its successors and the Bank cannot be predicted; however, depending on the degree to which our interest-earning assets and interest-bearing liabilities are rate sensitive, increases in rates would have a temporary effect of increasing our net interest margin, while decreases in interest rates would have the opposite effect. In addition, adverse economic conditions could make a higher provision for loan losses a prudent course and could cause higher loan charge-offs, thus adversely affecting our net income or other operating costs.

Available Information

We maintain an Internet website at www.fcalgroup.com, and a website for First California Bank at www.fcbank.com. At www.fcalgroup.com and via the "Investor Relations" link at the Bank's website, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to such reports filed or furnished pursuant to Section 13 or 15(d) of the Exchange Act are available, free of charge, as soon as reasonably practicable after such forms are electronically filed with, or furnished to, the SEC. The public may read and copy any materials we file with the SEC at the SEC's Public Reference Room, located at 100 F Street, NE, Washington, D.C. 20549 on official business days during the hours of 10:00 a.m. to 3:00 p.m. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC also maintains an Internet site at www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. You may obtain copies of the Company's filings on the SEC site. These documents may also be obtained in print upon request by our shareholders to our Investor Relations Department.

You may contact our Investor Relations Department at First California Financial Group, Inc., 3027 Townsgate Road, Suite 300, Westlake Village, California 91361, telephone number (805) 322-9655.

(All website addresses given in this document are for information only and are not intended to be an active link or to incorporate any website information into this document.)

We have adopted a written code of ethics that applies to all directors, officers and employees of the Company, including our principal executive officer and senior financial officers, in accordance with Section 406 of the Sarbanes-Oxley Act of 2002 and the rules of the Securities and Exchange Commission promulgated thereunder. The code of ethics is available on our website at www.fcalgroup.com and also upon request, at no charge. Requests for copies should be directed to: Investor Relations Department, 3027 Townsgate Road, Suite 300, Westlake Village, California 91361, telephone number (805) 322-9655. In the Corporate Governance section of our corporate website we have also posted the charters for our Audit Committee, Compensation Committee and Governance and Nominating Committee.

Item 1A. Risk Factors

Ownership of our common stock involves risks. You should carefully consider the risks described below in addition to the other information set forth herein. Events or circumstances arising from one or more of these risks could adversely affect our business, financial condition, operating results, cash flows and prospects, and the value and market price of our securities could decline. The risks identified below are not intended to be a comprehensive list of all risks we face and additional risks that we may currently view as not material may also impair our business operations and results. Unless otherwise specified, references to "we," "our" and "us" in this subsection mean First California and its subsidiaries.

Risks Related to Our Business

Our business has been and may continue to be adversely affected by current conditions in the financial markets and economic conditions generally.

The global, U.S. and California economies are experiencing significantly reduced business activity and consumer spending as a result of, among other factors, disruptions in the capital and credit markets. Dramatic declines in the housing market during the past several years, with falling home prices and increasing foreclosures and unemployment, have resulted in significant write-downs of asset values by financial institutions, including government-sponsored entities and major commercial and investment banks. A sustained weakness or weakening in business and economic conditions generally or specifically in the principal markets in which we do business could have one or more of the following adverse effects on our business:

- a decrease in the demand for loans or other products and services offered by us;
- a decrease in the value of our loans or other assets secured by consumer or commercial real estate;
- a decrease to deposit balances due to overall reductions in the accounts of customers;
- an impairment of certain intangible assets or investment securities;
- a decreased ability to raise additional capital on terms acceptable to us or at all; or
- an increase in the number of borrowers who become delinquent, file for protection under bankruptcy laws or default on their loans or other obligations to us. An increase in the number of delinquencies, bankruptcies or defaults could result in a higher level of nonperforming assets, net charge-offs and provision for credit losses, which would reduce our earnings

Until conditions improve, we expect our business, financial condition and results of operations to be adversely affected.

Recent and future legislation and regulatory initiatives to address current market and economic conditions may not achieve their intended objectives, including stabilizing the U.S. banking system or reviving the overall economy.

Recent and future legislative and regulatory initiatives to address current market and economic conditions, such as Dodd-Frank, EESA or the ARRA, may not achieve their intended objectives, including stabilizing the U.S. banking system or reviving the overall economy. EESA was enacted in October 2008 to restore confidence and stabilize the volatility in the U.S. banking system and to encourage financial institutions to increase their lending to customers and to each other. Treasury and banking regulators have implemented, and likely will continue to implement, various other programs under this legislation to address capital and liquidity issues in the banking system, including the Troubled Asset Relief Program, or TARP, the CPP, President Obama's Financial Stability Plan announced in February 2009, the ARRA and the FDIC's TLGP. There can be no assurance as to the actual impact that any of the recent, or future, legislative and regulatory initiatives will have on the financial markets and the overall economy. Any failure of these initiatives to help stabilize or improve the financial markets and the economy, and a continuation or worsening of current financial market and economic conditions could materially and adversely affect our business, financial condition, results of operations, access to credit or the trading price of our common stock. In addition, many aspects of Dodd-Frank are subject to rulemaking and will take effect over several years, making it difficult to anticipate the overall financial impact on us and the financial services industry more generally.

Current levels of market volatility are unprecedented.

The capital and credit markets have been experiencing volatility and disruption for several years. The volatility and disruption has reached unprecedented levels. In some cases, the markets have produced downward pressure on stock prices and credit availability for certain issuers without regard to those issuers' underlying financial strength. If current levels of market disruption and volatility continue or worsen, there can be no assurance that we will not experience an adverse effect, which may be material, on our ability to access capital and on our business, financial condition and results of operations.

Additional requirements under our regulatory framework, especially those imposed under Dodd-Frank, ARRA, EESA or other legislation intended to strengthen the U.S. financial system, could adversely affect us.

Recent government efforts to strengthen the U.S. financial system, including the implementation of Dodd-Frank, ARRA, EESA, the TLGP and special assessments imposed by the FDIC, subject participants to additional regulatory fees and requirements, including heightened compliance requirements, corporate governance requirements, executive compensation restrictions, restrictions on declaring or paying dividends, restrictions on share repurchases, limits on executive compensation tax deductions and prohibitions against golden parachute payments. These requirements, and any other requirements that may be subsequently imposed, may have a material and adverse effect on our business, financial condition, and results of operations.

Our growth presents certain risks, including a possible decline in credit quality or capital adequacy.

The asset growth experienced by National Mercantile and FCB in the years prior to the Mergers and by us after the Mergers presents certain risks. While we believe we have maintained good credit quality notwithstanding such growth, rapid growth is frequently associated with a decline in credit quality. Accordingly, continued asset growth could lead to a decline in credit quality in the future. In addition, continued asset growth could cause a decline in capital adequacy for regulatory purposes, which could in turn cause us to have to raise additional capital in the future to maintain or regain "well capitalized" status as defined under applicable banking regulations.

We may be subject to more stringent capital requirements.

Dodd-Frank requires federal banking agencies to establish minimum leverage and risk-based capital requirements that will apply to both insured banks and their holding companies. The federal banking agencies are in the process of developing regulations to implement these requirements. Implementation of these standards, or any other new regulations, including Basel III, may adversely affect our ability to pay dividends, or require us to reduce business levels or raise capital, including in ways that may adversely affect our results of operations of financial condition.

Our performance and growth are dependent on maintaining a high quality of service for our customers, and will be impaired by a decline in our quality of service.

Our growth will be dependent on maintaining a high quality of service for our customers. As a result of the Mergers and the corresponding growth, it may become increasingly difficult to maintain high service quality for our customers. This could cause a decline in our performance and growth with respect to net income, deposits, assets and other benchmarks.

The fair value of our investment securities can fluctuate due to market conditions out of our control.

Our investment securities portfolio is comprised mainly of U.S. treasury notes/bills, U.S. government agency notes, U.S. government agency mortgage-backed securities and U.S. government agency collateralized mortgage obligations. At December 31, 2011, gross unrealized losses on our investment portfolio were $5.6 million. The majority of unrealized losses at December 31, 2011 were related to a type of mortgage-backed security also known as private-label collateralized mortgage obligations. As of December 31, 2011, the amortized cost of these securities, rated triple-A at purchase, was $15.9 million and the gross unrealized loss was $2.8 million and these securities represented 3 percent of our securities portfolio. We also own one pooled trust preferred security, rated triple-A at purchase, with an amortized cost basis of $4.7 million and an unrealized loss of $2.1 million at December 31, 2011. This unrealized loss is primarily caused by a severe disruption in the market for these securities.

Factors beyond our control can significantly influence the fair value of securities in our portfolio and can cause potential adverse changes to the fair value of these securities. These factors include but are not limited to rating agency downgrades of the securities, defaults by the issuer or with respect to the underlying securities, changes in market interest rates and continued instability in the credit markets. Any of these mentioned factors could cause an other-than-temporary impairment in future periods and result in a realized loss.

If borrowers and guarantors fail to perform as required by the terms of their loans, we will sustain losses.

A significant source of risk arises from the possibility that losses will be sustained if our borrowers and guarantors fail to perform in accordance with the terms of their loans and guaranties. This risk increases when the economy is weak. We have adopted underwriting and credit monitoring procedures and credit policies, including the establishment and review of the allowance for loan losses, that we believe are appropriate to minimize this risk by assessing the likelihood of nonperformance, tracking loan performance and diversifying our credit portfolio. These policies and procedures, however, may not prevent unexpected losses that could materially adversely affect our results of operations.

Our allowance for loan losses may not be adequate to cover actual losses.

In accordance with accounting principles generally accepted in the United States, we maintain an allowance for loan losses to provide for probable loan and lease losses. Our allowance for loan losses may not be adequate to cover actual loan and lease losses, and future provisions for credit losses could materially and adversely affect our operating results. Our allowance for loan losses is based on prior experience, as well as an evaluation of the risks in the current portfolio. The amount of future losses is susceptible to changes in economic, operating and other conditions, including changes in interest rates that may be beyond our control, and these losses may exceed current estimates. Federal and state regulatory agencies, as an integral part of their examination process, review our loans and allowance for loan losses. While we believe that our allowance for loan losses is adequate to cover probable losses, it is possible that we will further increase the allowance for loan losses or that regulators will require increases. Either of these occurrences could materially and negatively affect our earnings.

The banking business is subject to interest rate risk and variations in interest rates may negatively affect our financial performance.

Changes in the interest rate environment may reduce our profits. It is expected that we will continue to realize income from the differential between the interest earned on loans, securities and other interest-earning assets, and interest paid on deposits, borrowings and other interest-bearing liabilities. Net interest margin is affected by the difference between the maturities and repricing characteristics of interest-earning assets and interest-bearing liabilities. In addition, loan volume and yields are affected by market interest rates on loans, and rising interest rates generally are associated with a lower volume of loan originations. We may not be able to minimize our interest rate risk. In addition, while an increase in the general level of interest rates may increase our net interest margin and loan yield, it may adversely affect the ability of certain borrowers with variable rate loans to pay the interest on and principal of their obligations. Accordingly, changes in levels of market interest rates could materially and adversely affect our net interest margin, asset quality, loan origination volume and overall profitability.

We face strong competition from financial services companies and other companies that offer banking services which could negatively affect our business.

We conduct our banking operations in Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Luis Obispo and Ventura counties, California. Increased competition in these markets may result in reduced loans and deposits. Ultimately, we may not be able to compete successfully against current and future competitors. Many competitors offer the same banking services that we offer in our service areas. These competitors include national banks, regional banks and other community banks. We also face competition from many other types of financial institutions, including without limitation, savings and loan institutions, finance companies, brokerage firms, insurance companies, credit unions, mortgage banks and other financial intermediaries. In particular, competitors include several major financial companies whose greater resources may afford them a marketplace advantage by enabling them to maintain numerous banking locations and ATMs and conduct extensive promotional and advertising campaigns.

Additionally, banks and other financial institutions with larger capitalizations and financial intermediaries not subject to bank regulatory restrictions have larger lending limits than we have and are thereby able to serve the credit needs of larger customers. Areas of competition include interest rates for loans and deposits, efforts to obtain deposits, and range and quality of products and services provided, including new technology-driven products and services. Technological innovation continues to contribute to greater competition in domestic and international financial services markets as technological advances enable more companies to provide financial services. We also face competition from out-of-state financial intermediaries that have opened low-end production offices or that solicit deposits in our market areas. If we are unable to attract and retain banking customers, we may be unable to continue to grow our loan and deposit portfolios and our results of operations and financial condition may otherwise be adversely affected.

Changes in economic conditions, in particular an economic slowdown in Southern California, could materially and negatively affect our business.

Our business is directly impacted by factors such as economic, political and market conditions, broad trends in industry and finance, legislative and regulatory changes, changes in government monetary and fiscal policies and inflation, all of which are beyond our control. Any further deterioration in economic conditions, whether caused by national or local concerns, in particular any further economic slowdown in Southern California, could result in the following consequences, any of which could hurt our business materially: loan delinquencies may increase; problem assets and foreclosures may increase; demand for our products and services may decrease; low cost or noninterest bearing deposits may decrease; and collateral for loans made by us, especially real estate, may decline in value, in turn reducing customers' borrowing power, and reducing the value of assets and collateral associated with our existing loans. The State of California and certain local governments in our market area continue to face fiscal challenges upon which the long-term impact on the State's or the local economy cannot be predicted.

A portion of our loan portfolio consists of construction and land development loans in Southern California, which have greater risks than loans secured by completed real properties.

At December 31, 2011, we had outstanding construction and land development loans in Southern California in the amount of $58.0 million, representing 5% of our loan portfolio. These types of loans generally have greater risks than loans on completed homes, multifamily properties and commercial properties. A construction loan generally does not cover the full amount of the construction costs, so the borrower must have adequate funds to pay for the balance of the project. Price increases, delays and unanticipated difficulties can materially increase these costs. Further, even if completed, there is no assurance that the borrower will be able to sell the project on a timely or profitable basis, as these are closely related to real estate market conditions, which can fluctuate substantially between the start and completion of the project. If the borrower defaults prior to completion of the project, the value of the project will likely be less than the outstanding loan, and we could be required to complete construction with our own funds to minimize losses on the project.

Further disruptions in the real estate market could materially and negatively affect our business.

There has been a slow-down in the real estate market due to negative economic trends and credit market disruption, the impacts of which are not yet completely known or quantified. At December 31, 2011, approximately 82% of our loans are secured by real estate. Any further downturn in the real estate market could materially and adversely affect our business because a significant portion of our loans is secured by real estate. Our ability to recover on defaulted loans by selling the real estate collateral would then be diminished and we would be more likely to suffer losses on defaulted loans. An increase in losses on defaulted loans may have a material impact on our financial condition and results of operations, by reducing income, increasing expenses, and leaving less cash available for lending and other activities.

Substantially all of our real property loan collateral is located in Southern California. Real estate values have declined recently, particularly in California. If real estate sales and appreciation continue to weaken, especially in Southern California, the collateral for our loans would provide less security. Real estate values have been and could be affected by, among other things, an economic recession or slowdown, an increase in interest rates, earthquakes, brush fires, flooding and other natural disasters particular to California.

We are subject to extensive regulation which could adversely affect our business.

Our operations are subject to extensive regulation by federal, state and local governmental authorities and are subject to various laws and judicial and administrative decisions imposing requirements and restrictions on part or all of our operations. Because our business is highly regulated, the laws, rules and regulations applicable to us are subject to regular modification and change. There are currently proposed laws, rules and regulations that, if adopted, would impact our operations. For example, Dodd-Frank will have a broad impact on the financial services industry, including imposing significant regulatory and compliance changes, such as: (1) enhanced resolution authority of troubled and failing banks and their holding companies; (2) enhanced lending limits strengthening the existing limits on a depository institution's credit exposure to one borrower; (3) increased capital and liquidity requirements; (4) increased regulatory examination fees; (5) changes to assessments to be paid to the FDIC for federal deposit insurance; (6) prohibiting bank holding companies, such as us, from including in regulatory Tier 1 capital future issuances of trust preferred securities or other hybrid debt and equity securities; and (7) numerous other provisions designed to improve supervision and oversight of, and strengthening safety and soundness for, the financial services sector. Additionally, Dodd-Frank establishes a new framework for systemic risk oversight within the financial system to be distributed among new and existing federal regulatory agencies, including the Financial Stability Oversight Council, the FRB, the OCC and the FDIC. Further, Dodd-Frank addresses many corporate governance and executive compensation matters that will affect most U.S. publicly traded companies, including us. Many of the requirements called for in Dodd-Frank will be implemented over time and most will be subject to implementing regulations over the course of several years. Given the uncertainty associated with the manner in which the provisions of Dodd-Frank will be implemented by the various regulatory agencies and through regulations, the full extent of the impact such requirements will have on our operations is unclear. The changes resulting from Dodd-Frank may impact the profitability of our business activities, require changes to certain of our business practices, impose upon us more stringent capital, liquidity and leverage ratio requirements or otherwise adversely affect our business. In particular, the potential impact of Dodd-Frank on our operations and activities, both currently and prospectively, include, among others:

- a reduction in our ability to generate or originate revenue-producing assets as a result of compliance with heightened capital standards;
- increased cost of operations due to greater regulatory oversight, supervision and examination of banks and bank holding companies, and higher deposit insurance premiums;
- the limitation on our ability to raise capital through the use of trust preferred securities as these securities will no longer be included in Tier 1 capital going forward; and
- the limitation on our ability to expand consumer product and service offerings due to anticipated stricter consumer protection laws and regulations

Further, we may be required to invest significant management attention and resources to evaluate and make necessary changes in order to comply with new statutory and regulatory requirements. Failure to comply with the new requirements may negatively impact our results of operations and financial condition. While we cannot predict what effect any presently contemplated or future changes in the laws or regulations or their interpretations would have on us, these changes could be materially adverse to our investors.

In addition, there are other currently proposed laws, rules and regulations that, if adopted, would impact our operations. For example, federal bank regulators have enacted regulations that would (1) require banking organizations to report the structures of all incentive-based compensation arrangements and (2) prohibit incentive-based payment arrangements that encourage inappropriate risks by providing employees, directors, or principal shareholders with excessive compensation or that could lead to material financial loss to the organization.

Additionally, in order to conduct certain activities and transactions, including acquisitions, we are required to obtain regulatory approval. There can be no assurance that any required approvals can be obtained, or obtained without conditions or on a timeframe acceptable to us. For more information, please see the section entitled “Item 1. Business-Supervision and Regulation” above.

We are exposed to risk of environmental liabilities with respect to properties to which we take title.

In the course of our business, we may own or foreclose and take title to real estate, and could be subject to environmental liabilities with respect to these properties. We may be held liable to a governmental entity or to third parties for property damage, personal injury, investigation and clean-up costs incurred by these parties in connection with environmental contamination, or may be required to investigate or clean up hazardous or toxic substances, or chemical releases at a property. The costs associated with investigation or remediation activities could be substantial. In addition, as the owner or former owner of a contaminated site, we may be subject to common law claims by third parties based on damages and costs resulting from environmental contamination emanating from the property. If we ever become subject to significant environmental liabilities, our business, financial condition, liquidity and results of operations could be materially and adversely affected.

Our internal operations are subject to a number of risks.

We are subject to certain operational risks, including, but not limited to, data processing system failures and errors, customer or employee fraud, security breaches of our computer systems and catastrophic failures resulting from terrorist acts or natural disasters. We maintain a system of internal controls to mitigate against such occurrences and maintain insurance coverage for such risks that are insurable, but should such an event occur that is not prevented or detected by our internal controls and uninsured or in excess of applicable insurance limits, it could have a significant adverse impact on our business, financial condition or results of operations.

We face reputation and business risks due to our interactions with business partners, service providers and other third parties.

We rely on third parties in a variety of ways, including to provide key components of our business infrastructure or to further our business objectives. These third parties may provide services to us and our clients or serve as partners in business activities. We rely on these third parties to fulfill their obligations to us, to accurately inform us of relevant information and to conduct their activities professionally and in a manner that reflects positively on us. Any failure of our business partners, service providers or other third parties to meet their commitments to us or to perform in accordance with our expectations could harm our business and operations, financial performance, strategic growth or reputation.

We face risks in connection with our strategic undertakings.

If appropriate opportunities present themselves, we may engage in strategic activities, which may include acquisitions, investments, asset purchases or other business growth initiatives or undertakings. There can be no assurance that we will successfully identify appropriate opportunities, that we will be able to negotiate or finance such activities or that such activities, if undertaken, will be successful.

In order to finance future strategic undertakings, we might obtain additional equity or debt financing. Such financing might not be available on terms favorable to us, or at all. If obtained, equity financing could be dilutive and the incurrence of debt and contingent liabilities could have a material adverse effect on our business, results of operations and financial condition.

Our ability to execute strategic activities successfully will depend on a variety of factors. These factors likely will vary based on the nature of the activity but may include our success in integrating the operations, services, products, personnel and systems of an acquired company into our business, operating effectively with any partner with whom we elect to do business, retaining key employees, achieving anticipated synergies, meeting management’s expectations and otherwise realizing the undertaking’s anticipated benefits. Our ability to address these matters successfully cannot be assured. In addition, our strategic efforts may divert resources or management’s attention from ongoing business operations and may subject us to additional regulatory scrutiny. If we do not successfully execute a strategic undertaking, it could adversely affect our business, financial condition, results of operations, reputation and growth prospects. In addition, if we were to conclude that the value of an acquired business had decreased and that the related goodwill had been impaired, that conclusion would result in an impairment of goodwill charge to us, which would adversely affect our results of operations.

We are dependent on key personnel and the loss of one or more of those key personnel may materially and adversely affect our prospects.

We depend heavily on the services of our President and Chief Executive Officer, C. G. Kum, our Senior Executive Vice President and Chief Operating Officer/Chief Financial Officer, Romolo C. Santarosa and a number of other key management personnel. The loss of any of their services or that of other key personnel could materially and adversely affect our future results of operations and financial condition. Our success also depends in part on our ability to attract and retain additional qualified management personnel. Competition for such personnel is strong in the banking industry and we may not be successful in attracting or retaining the personnel we require.

We may incur impairments to goodwill.

We assess goodwill for impairment on an annual basis or at interim periods if an event occurs or circumstances change which may indicate a change in the implied fair value of the goodwill. Impairment exists when the carrying amount of goodwill exceeds its implied fair value. It is our practice to perform the annual impairment assessment at the end of our fiscal year and to use independent data to assist us in determining the fair value of the Company and in determining appropriate market factors to be used in the fair value calculations. At December 31, 2011 the annual assessment resulted in the conclusion that goodwill was not impaired. A significant decline in our stock price, a significant decline in our expected future cash flows, a significant change in the fair values of our assets and liabilities, a significant adverse change in the business climate or slower growth rates could result in impairment of our goodwill. If we were to conclude that a future write-down of our goodwill is necessary, then we would record the appropriate non-cash charge, which could have an adverse effect on our operating results and financial position.

We are a holding company and depend on our banking subsidiary for dividends, distributions and other payments.

We are a holding company that conducts substantially all our operations through our banking subsidiary, First California Bank. As a result, our ability to make dividend payments on our common and preferred stock and debt service payments depends upon the ability of the Bank to make payments, distributions and loans to us. The ability of the Bank to make payments, distributions and loans to us is limited by, among other things, its earnings, its obligation to maintain sufficient capital, and by applicable regulatory restrictions. For example, if, in the opinion of an applicable regulatory authority, the Bank is engaged in or is about to engage in an unsafe or unsound practice, which could include the payment of dividends under certain circumstances, such authority may take actions requiring that the Bank refrain from the practice. Additionally, under applicable California law, the Bank generally cannot make any distribution (including a cash dividend) to its stockholder, us, in an amount which exceeds the lesser of: (1) the retained earnings of the Bank and (2) the net income of the Bank for its last three fiscal years, less the amount of any distributions made by the Bank to its stockholder during such period. If the Bank is not able to make payments, distributions and loans to us, we may not be unable to pay dividends on our common and preferred stock or make debt service payments.

If we are unable to increase our small business loans within 2 years, the cost of the Series C Preferred Stock will increase to us.

If we are unable to redeem the series C non-cumulative perpetual preferred stock prior to December 31, 2013, and we have not increased the amount of qualified small business loans above our baseline amount, the cost of this capital to us will increase substantially on that date, from a maximum of 5.0% per annum (approximately $1.25 million annually) to 7.0% per annum (approximately $1.75 million annually). Depending on our financial condition at the time, this increase in the annual dividend rate on the series C non-cumulative perpetual preferred stock could have a material negative effect on our liquidity and our earnings available to common stockholders.

We may experience difficulty in managing the loan portfolios acquired through FDIC-assisted acquisitions, which are within the limits of the shared-loss protection provided by the FDIC.

The Bank entered into shared-loss agreements with the FDIC that covered most of SLTB's and all of WCB's loans and foreclosed property. The Bank shares in the losses, beginning with the first dollar of loss incurred, on the loans and foreclosed property covered under the shared-loss agreements, or covered assets. Pursuant to the terms of the shared-loss agreements, the FDIC is obligated to reimburse the Bank 80 percent of eligible losses with respect to the covered assets. The Bank has 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 loans are in effect for 5 years and 10 years, respectively, from the acquisition date and the loss recovery provisions are in effect for 8 years and 10 years, respectively, from the acquisition date. Ten years after the acquisition date, the Bank is required to pay the FDIC 50 percent of the excess, if any, of specific amounts stated in the original agreements for each respective acquisition. Although we have expertise in asset resolution, we cannot guarantee that we will be able to adequately manage the loan portfolio within the limits of the shared-loss protection provided by the FDIC. Failure to comply with the requirements of the shared-loss agreements could result in loss of indemnification by the FDIC. Additionally, the Bank is subject to audits by the FDIC, through its designated agent, under the terms of the shared-loss agreements. The requirements of the shared-loss agreements are extensive and failure to comply with any of the guidelines could potentially result in a specific asset or group of assets losing shared-loss coverage.

Risks Related to Our Common Stock

Certain preferences and rights of preferred stockholders of First California may negatively affect the rights of holders of First California common stock.

First California's certificate of incorporation authorizes its Board of Directors to issue up to 2,500,000 shares of preferred stock and to determine the rights, preferences, powers and restrictions granted or imposed upon any series of preferred stock without prior stockholder approval. The preferred stock that may be authorized could have preference over holders of First California common stock with respect to dividends and other distributions upon the liquidation or dissolution of First California. If First California's Board of Directors authorizes the issuance of additional series of preferred shares having a voting preference over common stock, such issuances may inhibit or delay the approval of measures supported by holders of common stock that require stockholder approval and consequently may make it difficult and expensive for a third party to pursue a tender offer, change in control or takeover attempt that is opposed by our management and Board of Directors. Accordingly, such issuance could substantially impede the ability of public stockholders to benefit from a change in control or change of our management and Board of Directors and, as a result, may adversely affect the market price of our common stock and the stockholders' ability to realize any potential change of control premium.

Currently, in the event of a voluntary or involuntary liquidation or dissolution, holders of series A convertible perpetual preferred stock of First California are entitled to receive a liquidation preference of $1,000 plus an amount equal to 8.5% per annum of the $1,000, which is deemed to have commenced accrual on December 10, 2001. Also, holders of series C non-cumulative perpetual preferred stock of First California are entitled to receive a liquidation preference of $1,000 plus an accrued amount equal to the per-share amount of any unpaid dividends for the then-current period, if any. These amounts are payable out of the assets of First California before any distribution to holders of common stock. If the number of preferred shares having a similar liquidation preference increases, the chance that holders of common stock may receive a smaller distribution upon liquidation or dissolution may be higher.

Certain regulations and restrictions will affect our ability to declare or pay dividends and repurchase our shares.

As a result of our participation in the SBLF, our ability to declare or pay dividends on any of our common stock has been limited. Specifically, we are not able to repurchase shares or declare dividend payments on our common, junior preferred or pari passu preferred stock if we are in arrears on the dividends on our series C non-cumulative perpetual preferred stock. Furthermore, First California is permitted to make dividend payments to, or effectuate share repurchases from, other shareholders, provided that after the payment or repurchase, the institution's Tier 1 capital would be at least 90 percent of the amount existing at the time immediately after the SBLF closing date, excluding any subsequent net charge-offs and partial repayments of the SBLF funding.

Our ability to pay dividends to holders of our common stock may be restricted by Delaware law and under the terms of indentures governing the trust preferred securities we have issued.

Our ability to pay dividends to our stockholders is restricted in specified circumstances under indentures governing the trust preferred securities we have issued, and we may issue additional securities with similar restrictions in the future. In addition, our ability to pay any dividends to our stockholders is subject to the restrictions set forth under Delaware law. We cannot assure you that we will meet the criteria specified under these agreements or under Delaware law in the future, in which case we may not be able to pay dividends on our common stock even if we were to choose to do so.

The price of our common stock may fluctuate significantly, and this may make it difficult for you to resell our common stock when you want to or at prices you find attractive.

We cannot predict how our common stock will trade in the future. The market value of our common stock will likely continue to fluctuate in response to a number of factors including the following, most of which are beyond our control, as well as the other factors described in this "RISK FACTORS" section:

- actual or anticipated quarterly fluctuations in our operating and financial results;
- developments related to investigations, proceedings or litigation that involve us;
- changes in financial estimates and recommendations by financial analysts;
- dispositions, acquisitions and financings;
- actions of our current stockholders, including sales of our Common Stock by existing stockholders and our directors and executive officers;
- fluctuations in the stock price and operating results of our competitors;
- regulatory developments; and
- developments related to the financial services industry.

Only a limited trading market exists for our common stock, which could lead to significant price volatility.

Our common stock was designated for listing on the NASDAQ Global Market in March 2007 under the trading symbol "FCAL" and trading volumes since that time have been modest. The limited trading market for our common stock may cause fluctuations in the market value of our common stock to be exaggerated, leading to price volatility in excess of that which would occur in a more active trading market of our common stock. In addition, even if a more active market in our common stock develops, we cannot assure you that such a market will continue or that stockholders will be able to sell their shares.

A holder with as little as a 5% interest in First California could, under certain circumstances, be subject to regulation as a "Bank Holding Company."

Any entity (including a "group" composed of natural persons) owning 25% or more of the outstanding First California common stock, or 5% or more if such holder otherwise exercises a "controlling influence" over First California, may be subject to regulation as a "bank holding company" in accordance with the BHCA. In addition, (i) any bank holding company or foreign bank with a U.S. presence may be required to obtain the approval of the FRB under the BHCA to acquire or retain 5% or more of the outstanding First California common stock and (ii) any person other than a bank holding company may be required to obtain the approval of the FRB under the Change in Bank Control Act to acquire or retain 10% or more of the outstanding First California common stock. Becoming a bank holding company imposes certain statutory and regulatory restrictions and burdens, and might require the holder to divest all or a portion of the holder's investment in First California. In addition, because a bank holding company is required to provide managerial and financial strength for its bank subsidiary, such a holder may be required to divest investments that may be deemed incompatible with bank holding company status, such as a material investment in a company unrelated to banking.

Concentrated ownership of our common stock creates risks for our stockholders, including a risk of sudden changes in our share price.

As of January 31, 2012, directors, executive officers and other affiliates of First California owned approximately 22% of First California's outstanding common stock (not including vested option shares). As a result, if all of these stockholders were to take a common position, they would be able to significantly affect the election of directors, with respect to which stockholders are authorized to use cumulative voting, as well as the outcome of most corporate actions requiring stockholder approval, such as the approval of mergers or other business combinations. Such concentration may also have the effect of delaying or preventing a change in control of First California. In some situations, the interests of First California's directors and executive officers may be different from other stockholders.

Investors who purchase our common stock may be subject to certain risks due to the concentrated ownership of our common stock. The sale by any of our large stockholders of a significant portion of that stockholder's holdings could have a material adverse effect on the market price of our common stock. Furthermore, a group of our large stockholders can also demand that we register their shares under certain circumstances. Any such increase in the number of our publicly registered shares may cause the market price of our common stock to decline or fluctuate significantly.

We do not expect to pay dividends on our common stock in the foreseeable future.

We have never paid a cash dividend on our common stock and we do not expect to pay a cash dividend in the foreseeable future. We presently intend to retain earnings and increase capital in furtherance of our overall business objectives. We will periodically review our dividend policy in view of the operating performance of the company, and may declare dividends in the future if such payments are deemed appropriate.

There may be future sales of additional common stock or preferred stock or other dilution of our equity, which may adversely affect the market price of our common stock.

We are not restricted from issuing additional common stock or preferred stock, including any securities that are convertible into or exchangeable for, or that represent the right to receive, common stock or preferred stock or any substantially similar securities. On March 3, 2010, a proposal was approved by our stockholders to amend our Amended and Restated Certificate of Incorporation to increase the number of authorized shares of our common stock from 25,000,000 shares to 100,000,000 shares. This increase in the number of our authorized shares of common stock provides us with the flexibility to consider and respond to future business opportunities and needs as they arise, including equity offerings, acquisitions, stock dividends, issuances under stock incentive plans and other corporate purposes. The market value of our common stock could decline as a result of sales by us of a large number of shares of common stock or preferred stock or similar securities in the market or the perception that such sales could occur.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The Bank leases approximately 21,900 square feet of space at Westlake Park Place, 3027 Townsgate Road, Westlake Village, California for its administrative headquarters. The lease term will expire in February 2019.

The Bank also leases approximately 13,900 square feet of space for administrative functions located at 1880 Century Park East, Los Angeles, California. The lease term will expire in May 2014. The Bank has sublet approximately half of this space through March 2014.

The Bank owns its Camarillo Branch Office located at 1150 Paseo Camarillo, Camarillo, California. The building has approximately 9,000 square feet of space.

The Bank leases approximately 4,000 square feet of space for its Westlake Village Branch Office located at 32111 Agoura Road, Westlake Village, California. The lease term will expire in December 2014.

The Bank leases approximately 2,200 square feet of space for its Ventura Branch Office located at 1794 S. Victoria Avenue, Suite B, Ventura, California. The lease term will expire in May 2012.

The Bank leases approximately 1,700 square feet of space for its Oxnard Branch Office located at 300 Esplanade Drive, Suite 102, Oxnard, California. The lease term will expire in January 2016.

The Bank leases approximately 3,850 square feet of space for its Thousand Oaks Branch Office located at 11 E. Hillcrest Drive, Suite A, Thousand Oaks, California. The lease term will expire in October 2013 with two 5-year renewal options.

The Bank leases approximately 27,000 square feet of land for its Simi Valley Branch Office located at Simi Valley Towne Center, Simi Valley, California. The Bank owns the building which has approximately 5,000 square feet of space. The land lease term commenced in January 2006 and expires in 20 years.

The Bank leases approximately 1,900 square feet of space for its Century City Branch Office located at 1880 Century Park East, Los Angeles, California. The lease term will expire in June 2014.

The Bank leases approximately 1,650 square feet of space for its Encino Branch Office located at 16661 Ventura Boulevard, Encino, California. The lease term will expire in May 2012.

The Bank owns its Torrance Branch Office located at 2200 Sepulveda Blvd., Torrance, California. The building has approximately 15,966 square feet of space.

The Bank owns its Irvine Branch Office located at 19752 MacArthur Blvd., Irvine, California 92612. The building has approximately 21,000 square feet of space. The Bank has sublet a portion of this space through July 2013.

The Bank leases approximately 6,000 square feet of space for its Woodland Hills Branch Office located at 21550 Oxnard Street, Suite 100, Woodland Hills, California. The lease term will expire in March 2016.

The Bank leases approximately 3,500 square feet of space for its Glendale Branch Office located at 505 North Brand Boulevard, Glendale, California. The lease has an initial term of five years and will expire in November 2013.

The Bank leases approximately 8,500 square feet of space for its Redlands Branch Office located at 218 East State Street, Redlands, California. The lease term will expire in July 2014.

The Bank leases approximately 5,100 square feet of space for its Brea Branch Office located at 10 Pointe Drive, Suite 130, Brea, California. The lease term will expire in May 2014.

The Bank leases approximately 3,700 square feet of space for its Escondido Office located at 320 West Mission Avenue, Escondido, California. The lease term will expire in February 2021.

The Bank leases approximately 4,500 square feet of space for its Palm Desert Branch Office located at 78-000 Fred Waring Drive, suite 100, Palm Desert, California. The lease term will expire in May 2014.

The Bank leases approximately 4,600 square feet of space for its Irwindale Branch Office located at 15622 Arrow Highway, Irwindale, California. The lease term will expire in May 2014.

The Bank leases approximately 5,000 square feet of space for its Temecula Branch Office located at 27645 Jefferson Avenue, Temecula, California. The lease term will expire in June 2012.

The Bank lease approximately 5,120 square feet of space for its San Luis Obispo Office located at 1001 Marsh Street, San Luis Obispo, California. The lease term will expire in August 2016.

The Bank leases approximately 1,220 square feet of space for its temporary Palm Springs Office located at 333 S. Indian Canyon Drive, suite E, Palm Springs, California. The lease term will expire in November 2012.

The Bank leases approximately 8,800 square feet of space for its Electronic Payment Services Division located at 70115 Highway 111, Rancho Mirage, California. The lease term will expire in December 2018.

The Bank believes that its premises will be adequate for present and anticipated needs. The Bank also believes that it has adequate insurance to cover its owned and leased premises.

Item 3. Legal Proceedings

The information set forth in "Note 22-Commitments and Contingencies" of the Company's Notes to Consolidated Financial Statements included in this Annual Report on Form 10-K is incorporated herein by reference.

Item 4. Mine Safety Disclosures

Not Applicable.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The common stock of First California began trading on the NASDAQ Global Select Market under the symbol "FCAL" on March 13, 2007. Prior to that time, the common stock of National Mercantile, First California's predecessor, traded on the NASDAQ Capital Market under the symbol "MBLA". The information in the following table indicates the high and low sales prices for First California's common stock from January 1, 2010 to December 31, 2011, as reported by NASDAQ. Because of the limited market for First California's common stock, these prices may not be indicative of the fair market value of the common stock. The information does not include transactions for which no public records are available. The trading prices in such transactions may be higher or lower than the prices reported below.

	Common Stock	
	High	Low
2010		
First Quarter	$3.38	$2.54
Second Quarter	3.50	2.61
Third Quarter	2.91	2.36
Fourth Quarter	2.90	2.26
2011		
First Quarter	$4.09	$2.80
Second Quarter	4.00	3.40
Third Quarter	3.95	2.77
Fourth Quarter	3.72	2.79

At March 12, 2012, First California had 386 stockholders of record for its common stock. The number of beneficial owners for the common stock is higher, as many people hold their shares in "street" name.

Dividends

From its inception and until the completion of the Mergers in March 2007, First California was a "business combination shell company," conducting no operations or owning or leasing any real estate or other property. Accordingly, First California did not pay any dividends to its sole stockholder, National Mercantile, prior to the Mergers, nor has First California paid any dividends to its common stockholders since the completion of the Mergers. Our common stockholders are entitled to receive dividends when and as declared by our Board of Directors, out of funds legally available therefore, subject to the restrictions set forth in the Delaware General Corporation Law, or the DGCL. The DGCL provides that a corporation may declare and pay dividends out of any surplus, and, if it has no surplus, out of any net profits for the fiscal year in which the dividend was declared or for the preceding fiscal year (provided that the payment will not reduce capital to an amount less than the aggregate amount of the capital represented by the issued and outstanding stock of all classes having a preference upon the distribution of assets). In addition, First California may not pay dividends on its capital stock if it is in default or has elected to defer payments of interest under its junior subordinated debentures. The Company cannot declare or pay a dividend on its common stock if we are in arrears on the dividends on our series C non-cumulative perpetual preferred stock.

We do not currently expect to pay a cash dividend to our common stockholders in the foreseeable future. We presently intend to retain earnings and increase capital in furtherance of our overall business objectives. We will periodically review our dividend policy in view of the operating performance of the company, and may declare dividends in the future if such payments are deemed appropriate.

Securities Authorized for Issuance Under Equity Compensation Plans

The following table sets forth as of December 31, 2011 information regarding outstanding options and the number of shares available for future option grants under all of our equity compensation plans. All equity plans of FCB Bancorp, in addition to those of National Mercantile Bancorp and all outstanding option awards were assumed by First California in connection with the Mergers.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by shareholders (1)	590,008	$ 7.86	1,501,910
Equity compensation plans not approved by shareholders	N/A	N/A	N/A
Total	590,008	$ 7.86	1,501,910

(1) Includes the First California 2007 Omnibus Equity Incentive Plan (as amended May 26, 2011), FCFG FCB 2005 Stock Option Plan, FCFG 2005 NMB Stock Incentive Plan, FCFG Amended 1996 NMB Stock Incentive Plan, FCFG 1994 NMB Stock Option Plan.

Recent Sales of Unregistered Securities

None

Issuer Purchases of Equity Securities

There were no shares repurchased by the Company during the year ended December 31, 2011.

Item 6. Selected Financial Data

Not applicable.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

This discussion contains certain forward-looking information about us; we intend such 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:

- 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;
- 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;
- the costs and effects of legal, accounting and regulatory developments;
- recent volatility in the credit or equity markets and its effect on the general economy;
- 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 of this 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 Annual Report on Form 10-K. We make these forward-looking 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 individuals 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 and services through 19 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 December 31, 2011, we had consolidated total assets of $1.8 billion, total loans of $1.1 billion, total deposits of $1.4 billion and shareholders’ equity of $223.1 million. A year ago, at December 31, 2010, we had consolidated total assets of $1.5 billion, total loans of $1.0 billion, total deposits of $1.2 billion and shareholders’ equity of $198.0 million. The increase in loans and deposits was due in part to the FDIC-assisted San Luis Trust Bank transaction and the acquisition of the EPS division during 2011.

On November 5, 2010, the Bank assumed all of the deposits and substantially all of the assets of Western Commercial Bank, located in Woodland Hills, California, from the FDIC. The Bank acquired approximately $109 million of total assets, including $55 million in loans related to the transaction. The Bank assumed approximately $105 million of deposits related to the transaction. We accounted for the FDIC-assisted Western Commercial Bank transaction using the acquisition method of accounting; accordingly, our balance sheet includes the estimates of the fair value of the assets acquired and liabilities assumed. Our results of operations for the twelve months ended December 31, 2010 include the effects of the FDIC-assisted Western Commercial Bank transaction from the date of the transaction. As part of the Purchase and Assumption Agreement, the Bank and the FDIC entered into shared-loss agreements, whereby the FDIC will cover a substantial portion of any future losses on loans (and related unfunded loan commitments), foreclosed property and accrued interest on loans for up to 90 days. Under the terms of the shared-loss agreements, the FDIC will absorb 80 percent of losses and share in 80 percent of loss recoveries. The shared-loss agreements for commercial mortgage loans are in effect for 5 years from the November 5, 2010 acquisition date and the loss recovery provisions are in effect for 8 years from the acquisition date. The Bank continues to operate the one former WCB branch location as part of the Bank’s 19 branch locations.

On February 18, 2011, the Bank assumed certain liabilities and acquired certain assets and substantially all of the operations of San Luis Trust Bank, or SLTB, located in San Luis Obispo, California, from the FDIC. The Bank acquired, received and recognized certain assets with an estimated fair value of approximately $367 million, including $139 million of loans, $99 million of cash and federal funds sold, $70 million of a FDIC shared-loss asset, $41 million of securities, $13 million of foreclosed property and $5 million of other assets. The Bank also assumed and recognized liabilities with an estimated fair value of approximately $346 million, including $266 million of deposits, $62 million of Federal Home Loan Bank advances, $15 million in a deferred tax liability, $2.6 million of a FDIC shared-loss liability and $0.4 million of other liabilities. The Bank recorded a pre-tax bargain purchase gain of $36.5 million in connection with this transaction. As part of the Purchase and Assumption Agreement, the Bank and the FDIC entered into shared-loss agreements, whereby the FDIC will cover a substantial portion of any future losses on loans (and related unfunded loan commitments), foreclosed property and accrued interest on loans for up to 90 days. Under the terms of the shared-loss agreements, the FDIC will absorb 80 percent of losses and share in 80 percent of loss recoveries. The shared-loss agreements for commercial and residential mortgage loans are in effect for 5 years and 10 years, respectively, from the February 18, 2011 acquisition date and the loss recovery provisions are in effect for 8 years and 10 years, respectively, from the acquisition date. Our results of operations for the twelve months ended December 31, 2011 include the effects of the FDIC-assisted San Luis Trust bank transaction from the date of the transaction. The Bank continues to operate the one former SLTB branch location as part of the Bank’s 19 branch locations.

On April 8, 2011, the Bank completed the acquisition of the Electronic Banking Solutions division of Palm Desert National Bank. The transaction included the division’s customer base, core deposits, and employees. The Electronic Payment Services Division, or the EPS division, its new name under the Bank, issues prepaid cards and sponsors merchant acquiring services for all national and regional networks, including Visa, MasterCard, and Discover throughout all 50 states and U.S. territories. The Bank acquired cash of $85.4 million, recognized intangible assets of $6.0 million, assumed $91 million of deposits and recognized a pre-tax bargain purchase gain of $0.5 million in connection with this transaction. Our results of operations for the twelve months ended December 31, 2011 include the effects of the EPS acquisition from the date of the transaction.

For the year ended December 31, 2011, we had net income of $23.4 million compared to net income of $1.4 million for the year ended December 31, 2010. After dividend payments of $2.6 million on our Series B and Series C preferred shares, including a $1.1 million deemed dividend related to the full redemption of our Series B preferred shares in the third quarter of 2011, we had net income per diluted common share of $0.71 for the year ended December 31, 2011. After dividend payments of $1.3 million on our Series B preferred shares, we had net income per diluted common share of $0.01 for the year ended December 31, 2010. The significant increase in net income in 2011 was due largely to the bargain purchase gains on the SLTB and EPS acquisitions.

For the year ended December 31, 2010, we had net income of $1.4 million compared to a net loss of $4.7 million for the year ended December 31, 2009. After dividend payments of $1.3 million on our Series B preferred shares, we had net income per diluted common share of $0.01 for the year ended December 31, 2010. After dividend payments of $1.1 million on our Series B preferred shares, we incurred a loss per diluted common share of $0.50 for the year ended December 31, 2009. The net loss for 2009 was largely due to the $16.6 million provision for loan losses. The provision for loan losses was $8.3 million for 2010.

Critical Accounting Policies

We base our discussion and analysis of our consolidated results of operations and financial condition on 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 loans against the allowance when we believe that the collectability of the loan is unlikely. We perform periodic and systematic detailed reviews of the loan portfolio to identify trends and to assess the overall collectability of the loan portfolio. 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. We believe the accounting estimate related to the allowance for loan losses is a "critical accounting estimate" because: changes in it can materially affect the provision for loan losses and net income, it requires management to predict borrowers' likelihood or capacity to repay, and it requires management to distinguish between losses incurred as of a balance sheet date and losses expected to be incurred in the future. Accordingly, this is a highly subjective process and requires significant judgment since it is often difficult to determine when specific loss events may actually occur. 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 $17.7 million at December 31, 2011 and $17.0 million at December 31, 2010.

Non-covered foreclosed property

We acquire, through foreclosure or through full or partial satisfaction of a non-covered loan, real or personal property. At the time of foreclosure, we obtain an appraisal of the property and record 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 non-covered foreclosed property received; we credit earnings for the fair value amount of the non-covered foreclosed property in excess of the non-covered loan due. Subsequent to foreclosure, we periodically assess our disposition efforts and the estimated fair value less costs to sell of the non-covered foreclosed property. We establish a valuation allowance through a charge to earnings for estimated declines in fair value subsequent to foreclosure. Operating income and operating expense related to non-covered foreclosed property is included in earnings as are any ultimate gains or losses on the sale of the non-covered foreclosed property. Our recognition of gain is, however, dependent on the buyer's initial investment in the purchase of the non-covered foreclosed property meeting certain criteria. The estimated fair value of non-covered foreclosed property was $20.3 million at December 31, 2011 and $26.0 million at December 31, 2010.

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. Covered foreclosed property is reported exclusive of expected reimbursement cash flows from the FDIC. Foreclosed covered loan collateral is transferred into covered foreclosed property at the collateral's net realizable value, less estimated selling costs.

Covered foreclosed property was initially recorded at its estimated fair value on the acquisition date based on similar market comparable valuations less estimated selling costs. Any subsequent valuation adjustments due to declines in fair value will be charged to non-interest expense, and will be mostly offset by non-interest income representing the corresponding increase to the FDIC shared-loss asset for the offsetting loss reimbursement amount. Any recoveries of previous valuation adjustments will be credited to non-interest expense with a corresponding charge to non-interest income for the portion of the recovery that is due to the FDIC. The estimated fair value of covered foreclosed property was $14.6 million at December 31, 2011 and $1.0 million at December 31, 2010.

Deferred income taxes

We recognize deferred tax assets subject to our judgment that realization of the assets are more-likely-than-not. We establish a valuation allowance when we determine that realization of income tax benefits may not occur in future years. There were net deferred tax liabilities of $7.4 million at December 31, 2011 and net deferred tax assets of $4.6 million at December 31, 2010. There were no valuation allowances at either year-end.

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 non-interest 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. 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 $68.1 million at December 31, 2011 and $16.7 million at December 31, 2010.

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 $3.8 million and $1.0 million at December 31, 2011 and December 31, 2010.

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 designated hedged transactions on a quarterly basis. The Company recognizes the unrealized gains or losses of derivative instruments directly in current period earnings to the extent these instruments are not effective. At December 31, 2011, the Company had $37.1 million notional interest rate caps to limit the variable interest rate payments on our $26.8 million junior subordinated debentures. Our quarterly effectiveness assessments throughout 2011 indicated that these instruments were effective.

At December 31, 2011, the Bank had $120 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. At December 31, 2011, the estimated fair value of these interest rate caps was $291,000 and this amount is recorded within “accrued interest receivable and other assets” on the consolidated balance sheets.

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 that may indicate impairment may potentially exist. 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.

At December 31, 2011, we had goodwill of $60.7 million. We recognized goodwill of $50.1 million in connection with the Merger in 2007 and $10.6 million in connection with the FDIC-assisted 1st Centennial Bank transaction in 2009. We consolidated all operations under First California Bank at the time of each transaction; accordingly, we performed our goodwill impairment analysis on a consolidated or single unit basis.

The first step of our analysis compared the fair value of the Company to the carrying amount of the Company, including goodwill. At December 31, 2011, the measurement date, the carrying amount of the Company was $223.1 million. We used various approaches to estimate the fair value of the Company as described below:

Market Approach—Publicly Traded Companies—This approach considers the fair value of the Company based on observed, traded values of similar companies. We identified 15 publicly traded financial institutions to serve as guideline companies based on size, geography and performance metrics. We made an adjustment for a control premium, or the price at which a willing buyer and seller would complete a transaction. We assigned a weighting of 20 percent to this methodology.

Market Approach—Recent Transactions—This approach considers the fair value of the Company based on observed, key pricing multiples arising from similar control transactions using recent transactions. We assigned a weighting of 20 percent to this methodology.

Market Price Analysis—This approach considers the trading price of the Company as of the valuation date and adjusts for a control premium. We listed our common stock on the NASDAQ Global Market under the trading symbol “FCAL” and our trading volumes have been modest since the Merger. The limited trading for our common stock, we believe, causes exaggerated fluctuations in the market value of our common stock, leading to price volatility in excess of that which would occur in a more active trading market of our common stock. We used this method as a benchmark to the valuation performed in the Income approach below and was not a direct component of the valuation.

Income Approach—Discounted Cash Flow Method—This approach considers the present value of the Company's expected future cash flows. We believe this approach is the most theoretically correct method of valuation since it explicitly considers the future benefits associated with owning the business. We estimated our five-year future free cash flow and then discounted these to a present value at a rate of return that considers the relative risk of achieving the projected cash flows and the time value of money. We also estimated the residual or terminal free cash flow at the end of the projection period and discounted this to a present value. We assigned a weighting of 60 percent to this methodology.

Based on this first step of the impairment analysis, we determined that the carrying value of goodwill exceeded its fair value and therefore indicated a potential impairment. If this first step indicates a potential impairment, we next determine or estimate the implied fair value of the goodwill. That is, we estimated the fair value of the Company's individual assets and liabilities and then compared these to the fair value determined above. The excess of the fair value of the Company over the fair value of its tangible and intangible assets and liabilities is the implied fair value of goodwill as of the measurement date.

The following provides a summary of the valuation methodology we used in determining the fair values of major tangible assets, intangible assets and liabilities. We believe these methodologies are consistent with industry practices:

Securities —valued in the same manner as presented on our balance sheet.

Non-covered and covered loans —We divided loans into three 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, and (3) impaired loans. We estimated the fair value of impaired loans and loans that mature or re-price within three months at their carrying value. We used a 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 and other factors. We projected monthly principal and interest cash flows based on the contractual terms of the loan, adjusted for assumed prepayments, 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.

Deposits and borrowings with maturities—We used a discounted cash flow methodology to estimate the fair value of our certificates of deposits, securities sold under agreements to repurchase, Federal Home Loan Bank advances and junior subordinated debentures. The discount rate for certificates of deposits considered published retail and brokered rates as of the measurement date. The discount rate for securities sold under agreements to repurchase and Federal Home Loan Bank advances considered published rates as of the measurement date. The discount rate for our junior subordinated debentures considered comparable rates from recent and comparable issuances.

Core deposit intangibles—Core deposits are comprised of checking, savings and money market deposits. The value ascribed to the core deposit base is equal to the present value of the difference in cash flows between maintaining the existing core deposit base and obtaining alternative funds over the life of the deposit base. The cost of maintaining the existing core deposit base includes both the interest cost associated with the deposit and net maintenance costs (i.e., FDIC insurance, opportunity cost of reserve requirements, less service charge income and other deposit related revenue). We assumed the cost of alternative funding to be equivalent to brokered CD rates for deposit equivalent durations as of the measurement date. The discount rate considered the relative risk of achieving the projected cash flows and the time value of money.

Based on the results of this second step of the impairment analysis, we concluded that the implied fair value of goodwill was greater than our carrying value and that no goodwill impairment existed at December 31, 2011.

A significant decline in our stock price, a significant decline in our expected future cash flows, a significant change in the fair values of our assets and liabilities, a significant adverse change in the business climate or slow growth rates could result in impairment of our goodwill. If we were to conclude that a future write-down of our goodwill is necessary, we would record the appropriate non-cash charge, which could have a material adverse effect on our operating results and financial position; however, such non-cash charge would have no effect on our cash balances, liquidity or regulatory risk-based capital ratios.

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 debt security has been in a continuous unrealized loss position, the severity of the decline in value, the rating of the debt security, and the long-term financial outlook of the issuer. In addition, we consider the expected future cash flows of the debt security and our ability and intent on holding the debt security until the fair values recover.

For 2011, other-than-temporary impairment related to the credit loss on debt securities and recognized in earnings was $1.4 million.

For 2010, other-than-temporary impairment related to the credit loss on debt securities and recognized in earnings was $0.7 million. In addition, we recognized impairment of $41,000 on a $1.0 million community development-related equity investment.

For 2009, other-than-temporary impairment related to the credit loss on debt securities and recognized in earnings was $1.1 million. In addition, we recognized impairment of $392,000 on a $1.0 million community development-related equity investment.

Results of Operations—for the two years ended December 31, 2011

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 2011 was $59.5 million, up 33 percent from $44.7 million last year. The increase in our net interest income principally reflects the increase in interest-earning assets from the SLTB acquisition combined with a lower cost of interest-bearing liabilities.

Our net interest margin (on a taxable equivalent basis) was 3.92 percent for 2011 compared with 3.46 percent for 2010. The increase in our net interest margin was primarily due to a 39 basis point reduction in the cost of our interest-bearing liabilities. The rate paid on interest-bearing liabilities for 2011 was 1.16 percent compared with 1.55 percent for 2010. The improvement in the yield on interest-earning assets also contributed to the increase in the net interest margin. The yield on interest-earning assets for 2011 increased 20 basis points to 4.79 percent from 4.59 percent for 2010.

The following table presents the average balances, the amount of interest earned or incurred and the applicable taxable equivalent yields for interest-earning assets and the costs of interest-bearing liabilities that generate net interest income:

Average Balance Sheet and Analysis of Net Interest Income

	Year Ended December 31, 2011			Year Ended December 31, 2010		
	Average Amount	Interest Income/ Expense	Weighted Average Yield/ Rate	Average Amount	Interest Income/ Expense	Weighted Average Yield/ Rate
Loans (1)	$ 1,065,350	$ 65,945	6.19 %	$ 931,271	$ 53,240	5.72 %
Securities	325,850	6,303	1.97 %	300,162	5,914	2.00 %
Federal funds sold and deposits with banks	127,470	350	0.27 %	63,042	196	0.31 %
Total earning assets	1,518,670	72,598	4.79 %	1,294,475	59,350	4.59 %
Non-earning assets	267,839			165,642		
Total average assets	$ 1,786,509			$ 1,460,117		
Interest-bearing checking	$ 99,900	340	0.34 %	$ 81,016	277	0.34 %
Savings and money market	469,468	3,922	0.84 %	367,371	3,611	0.98 %
Certificates of deposit	401,859	3,750	0.93 %	334,914	4,085	1.22 %

Total interest-bearing deposits	971,227	8,012	0.82 %	783,301	7,973	1.02 %
Borrowings	128,947	3,750	2.91 %	133,995	4,945	3.69 %
Junior subordinated debentures	26,805	1,342	5.01 %	26,779	1,736	6.48 %
Total borrowed funds	155,752	5,092	3.26 %	160,774	6,681	4.14 %
Total interest-bearing liabilities	1,126,979	13,104	1.16 %	944,075	14,654	1.55 %
Noninterest checking	422,933			317,533		
Other liabilities	22,807			9,543		
Shareholders’ equity	213,790			188,966		
Total liabilities and shareholders’ equity	$ 1,786,509			$ 1,460,117		
Net interest income		$ 59,494			$ 44,696	
Net interest margin (tax equivalent) (2)			3.92 %			3.46 %

(1) Yields and amounts earned on loans include loan fees and discount/premium accretion of $2.9 million and ($0.5) million for the years ended December 31, 2011 and 2010, respectively. The average loan balance includes nonaccrual loans; however, there is no interest income related to nonaccrual loans in the amount earned on loans.

(2) Includes tax equivalent adjustments 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 changes in our interest income and interest expense:

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

	2011 vs. 2010 Increase (Decrease) due to: Volume	Rate	Net Increase (Decrease)
Interest Income:			
Interest on loans (2)	$7,665	$5,040	$12,705
Interest on securities	513	(124)	389
Interest on Federal funds sold and deposits with banks	200	(46)	154
Total interest income	8,378	4,870	13,248
Interest Expense:			
Interest on deposits	1,913	(1,874)	39
Interest on borrowings	(186)	(1,009)	(1,195)
Interest on junior subordinated debentures	2	(396)	(394)
Total interest expense	1,729	(3,279)	(1,550)
Net interest income	$6,649	$8,149	$14,798

(1) The change in interest income or interest expense that is attributable to both changes in average balance and average rate has been allocated 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.

Provision for loan losses

The provision for loan losses was $5.3 million for the year ended December 31, 2011 compared with $8.3 million for the year ended December 31, 2010. The decrease in the provision for loan losses in 2011 compared to 2010 reflects a decline in non-covered loan balances. We revised downward in the fourth quarter of 2011 our estimated loss factors for the qualitative considerations used in the determination of the adequacy of our allowance for loan losses. We revised upward in the first three quarters of 2011 and revised downward in the final quarter of 2011, our estimated loss factors for the quantitative considerations used in the determination of the adequacy of our allowance for loan losses. The change in our estimated loss factors for the 2011 period was less than the change for the 2010 period; however, the changes resulted in a higher ratio of the allowance for loan losses to non-covered loans. At December 31, 2011, the ratio of the allowance for loan losses to non-covered loans was 1.90 percent compared with 1.80 percent at December 31, 2010.

Noninterest income

Noninterest income was $44.6 million for 2011 compared with $8.8 million for 2010. The increase is primarily due to gain on acquisitions.

Service charges on deposit accounts were $3.4 million for 2011, up 7 percent from $3.2 million for 2010. The increase reflects the related growth in our deposit balances from $1.2 billion at December 31, 2010 to $1.4 billion at December 31, 2011.

In 2011, we did not sell any loans. During 2010 we sold one loan for a gain of $8,000. We did not receive commissions on brokered commercial and multifamily mortgages in 2011 compared with $47,000 in 2010.

For all of 2011 we sold $39.0 million of securities and net gains from the sales of these securities were $1.0 million. For all of 2010 we sold $236.0 million of securities and net gains from the sales of these securities were $2.0 million.

In 2011, we recognized other-than-temporary impairment losses on private-label collateralized mortgage obligations of $1.4 million. In 2010, we recognized other-than-temporary impairment losses on private-label collateralized mortgage obligations of $0.7 million. In addition, we recognized an impairment loss of $41,000 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 impairment losses in future periods.

In the 2011 fourth quarter we completed the foreclosures on a $1.4 million office building and a $0.9 million multifamily property. We obtained current appraisals and determined the fair values of these properties were $0.4 million higher than the loan balances. Accordingly, we recognized a $0.4 million market gain on foreclosed assets in the 2011 fourth quarter. In the 2010 second quarter we completed the foreclosure on a $21.0 million completed office construction project. This project consisted of 20 completed units ranging from approximately 1,650 square feet to 14,600 square feet in size. We obtained a current appraisal, evaluated the estimated retail sales prices as well as the estimated costs to sell and determined the fair value of this project to be $21.7 million. Accordingly, in the 2010 second quarter, we recognized a market value gain on foreclosed assets of $0.7 million.

On February 18, 2011, the Bank assumed all of the deposits and substantially all of the assets of San Luis Trust Bank, located in San Luis Obispo, California, from the FDIC. We recognized a pre-tax bargain purchase gain of $36.5 million in connection with this transaction. On April 8, 2011, the Bank acquired the Electronic Banking Solutions division of Palm Desert National Bank. We recognized a pre-tax bargain purchase gain of $0.5 million in connection with this transaction. On November 5, 2010, the Bank assumed all of the deposits and substantially all of the assets of Western Commercial Bank, located in Woodland Hills, California, from the FDIC. We recognized a pre-tax bargain purchase gain of $2.3 million in connection with this transaction.

Other income was $3.7 million for 2011, up 363 percent from $0.8 million in 2010. The significant increase was due to the acquisition of the EPS division in April 2011 that generates fee income from the issuance of prepaid cards and sponsoring merchant acquiring services for all national and regional credit card networks.

The following table presents a summary of noninterest income:

	For the years ended December 31,	
	2011	2010
	(in thousands)	

Service charges on deposit accounts	$	3,447	$	3,225
Earnings on cash surrender value of life insurance		438		441
Loan sales and commissions		—		55
Net gain on sale of securities		1,022		2,014
Impairment losses on securities		(1,387)		(749)
Market gain on foreclosed assets		429		691
Gain on acquisition		36,922		2,312
Other income		3,738		807
Total noninterest income	$	44,609	$	8,796

Noninterest expense

Our noninterest expense for 2011 was $58.5 million, up 37 percent from $42.8 million for 2010. The increase in noninterest expense was largely in salaries and benefits expense, professional expense and loss on and expense of foreclosed properties. Salaries and benefits expense reflects the workforce increases from the acquisitions of Western Commercial Bank in November 2010, San Luis Trust Bank in February 2011 and the EPS division in April 2011. Full-time equivalent employees were 304 at December 31, 2011 as compared with 248 at December 31, 2010. Professional expense increased to $5.6 million in 2011 from $2.0 million in 2010. The increase was due to litigation expense related to ongoing legal cases and a high level of legal loan collection expense. Loss on and expense of foreclosed properties increased to $5.2 million in 2011 from $3.0 million in 2010. The increase was mainly due to valuation allowances recorded on our two largest foreclosed properties.

The following table presents a summary of noninterest expense:

	For the years ended December 31,	
	2011	2010
	(in thousands)	
Salaries and employee benefits	$26,510	$19,014
Premises and equipment	6,298	6,268
Data processing	3,500	2,564
Legal, audit, and other professional services	5,570	2,033
Printing, stationary, and supplies	366	258
Telephone	800	841
Directors' fees	460	428
Advertising and marketing	1,637	918
Postage	222	212
Insurance and regulatory assessments	2,199	2,944
Loss on and expense of foreclosed property, net	5,178	2,954
Amortization of intangible assets	2,289	1,666
Other expenses	3,435	2,705
Total noninterest expense	$58,464	$42,805

Our efficiency ratio was 75 percent for both 2011 and 2010. The efficiency ratio is the percentage relationship of noninterest expense, excluding amortization of intangibles, loss on and expense of foreclosed property and integration/conversion expenses related to acquisitions, to the sum of net interest income and noninterest income, excluding gains or losses on security sales, other-than-temporary impairment losses and gain on acquisitions.

Income taxes

The income tax provision was $16.9 million for 2011 compared with $0.9 million for 2010. The effective tax rate was 42.0 percent for 2011 compared with 40.0 percent for 2010.

The combined federal and state statutory rate for 2011 and 2010 was 42.05 percent. The effective tax rates for 2011 and 2010 approximated the combined federal and state statutory tax rate because the additions to and exclusions from taxable income were not material.

Results of Operations—for the two years ended December 31, 2010

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 2010 was $44.7 million, down 1 percent from $45.1 million last year. The decrease in our net interest income principally reflects the decline in interest income derived from securities.

Our net interest margin (on a taxable equivalent basis) was 3.46% for 2010 compared with 3.53% for 2009. The decrease in our net interest margin was primarily due to lower yields on our securities and reflects the shift in the composition of our securities to lower yielding, shorter-term securities. The yield on interest-earning assets for 2010 was 4.59 percent, down 49 basis points from 5.08 percent for 2009. The reduction in the cost of our interest-bearing liabilities, which equaled 1.55 percent for 2010, down 47 basis points from 2.02 percent for 2009, partially offset the effects of lower yields on interest-earning assets.

The following table presents the average balances, the amount of interest earned or incurred and the applicable taxable equivalent yields for interest-earning assets and the costs of interest-bearing liabilities that generate net interest income:

Average Balance Sheet and Analysis of Net Interest Income

	Year Ended December 31, 2010			Year Ended December 31, 2009		
	Average Amount	Interest Income/ Expense	Weighted Average Yield/ Rate	Average Amount	Interest Income/ Expense	Weighted Average Yield/ Rate
Loans (1)	$ 931,271	$ 53,240	5.72 %	$ 920,272	$ 52,439	5.70 %
Securities	300,162	5,914	2.00 %	281,960	12,086	4.52 %
Federal funds sold and deposits with banks	63,042	196	0.31 %	86,415	416	0.48 %
Total earning assets	1,294,475	59,350	4.59 %	1,288,647	64,941	5.08 %
Non-earning assets	165,642			154,231		
Total average assets	$ 1,460,117			$ 1,442,878		
Interest-bearing checking	$ 81,016	277	0.34 %	$ 78,581	235	0.30 %
Savings and money market	367,371	3,611	0.98 %	276,097	3,007	1.10 %
Certificates of deposit	334,914	4,085	1.22 %	445,293	8,889	2.00 %
Total interest-bearing deposits	783,301	7,973	1.02 %	799,971	12,131	1.52 %
Borrowings	133,995	4,945	3.69 %	155,252	5,924	3.82 %
Junior subordinated debentures	26,779	1,736	6.48 %	26,727	1,832	6.85 %
Total borrowed funds	160,774	6,681	4.14 %	181,979	7,756	4.25 %
Total interest-bearing liabilities	944,075	14,654	1.55 %	981,950	19,887	2.02 %
Noninterest checking	317,533			288,893		
Other liabilities	9,543			11,711		
Shareholders' equity	188,966			160,324		
Total liabilities and shareholders' equity	$ 1,460,117			$ 1,442,878		
Net interest income		$ 44,696			$ 45,054	
Net interest margin (tax equivalent) (2)			3.46 %			3.53 %

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(1) Yields and amounts earned on loans include loan fees of ($0.5) million and ($0.1) million for the years ended December 31, 2010 and 2009, respectively. The average loan balance includes loans held-for-sale and nonaccrual loans; however, there is no interest income related to nonaccrual loans in the amount earned on loans.
(2) Includes tax equivalent adjustments 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 changes in our interest income and interest expense:

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

	2010 vs 2009 Increase (Decrease) due to:		Net Increase (Decrease)
	Volume	Rate	
Interest Income:			
Interest on loans (2)	$627	$174	$801
Interest on securities	780	(6,952)	(6,172)
Interest on Federal funds sold and deposits with banks	(112)	(108)	(220)
Total interest income	1,295	(6,886)	(5,591)
Interest Expense:			
Interest on deposits	(253)	(3,905)	(4,158)
Interest on borrowings	(811)	(168)	(979)
Interest on junior subordinated debentures	4	(100)	(96)
Total interest expense	(1,060)	(4,173)	(5,233)
Net interest income	$2,355	$(2,713)	$(358)

(1) The change in interest income or interest expense that is attributable to both changes in average balance and average rate has been allocated 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.

Provision for loan losses

The provision for loan losses was $8.3 million for the year ended December 31, 2010 compared with $16.6 million for the year ended December 31, 2009. The decrease in the provision for loan losses in 2010 compared to 2009 was the result of lower nonaccrual loans, past due loans and classified loans in 2010 as compared to 2009. We revised upward in the second quarter and fourth quarter of 2010 and in the first quarter of 2009, our estimated loss factors for the qualitative considerations used in the determination of the adequacy of our allowance for loan losses. The change in our estimated loss factors for the 2010 periods was less than the change for the 2009 period; however, the changes resulted in a higher ratio of the allowance for loan losses to non-covered loans. At December 31, 2010, the ratio of the allowance for loan losses to non-covered loans was 1.80 percent compared with 1.76 percent at December 31, 2009.

Noninterest income

Noninterest income was $8.8 million for 2010 compared with $10.0 million for 2009.

Service charges on deposit accounts were $3.2 million for 2010, down 8 percent from $3.5 million for 2009. The decrease reflects a lower incidence of customers drawing checks against their deposit account when insufficient funds are on deposit.

During 2010 we sold one loan for a gain of $8,000. In 2009, we did not sell any loans. Commissions received on brokered commercial and multifamily mortgages were $47,000 in 2010 compared with $70,000 in 2009.

For all of 2010, we sold $236.0 million of securities and net gains from the sale of these securities were $2.0 million. For all of 2009 we sold $244.1 million of securities and net gains from the sales of these securities were $6.5 million.

In 2010, we recognized other-than-temporary impairment losses on private-label collateralized mortgage obligations of $0.7 million. In addition, we recognized an impairment loss of $41,000 on a $1.0 million community development-related equity investment. In 2009, we recognized other-than-temporary impairment losses on private-label collateralized mortgage obligations of $1.1 million. In addition, we recognized an impairment loss of $392,000 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 impairment losses in future periods.

In the 2010 second quarter we completed the foreclosure on a $21.0 million completed office construction project. This project consisted of 20 completed units ranging from approximately 1,650 square feet to 14,600 square feet in size. We obtained a current appraisal, evaluated the estimated retail sales prices as well as the estimated costs to sell and determined the fair value of this project to be $21.7 million. Accordingly, in the 2010 second quarter, we recognized a market value gain of $0.7 million. Subsequent to foreclosure, we sold one unit of approximately 4,100 square feet resulting in net proceeds of approximately $1.0 million. In the 2010 fourth quarter, a $2.1 million valuation reserve was established on this property as the time to sell the units will more likely than not be longer than that estimated in the June 2010 appraisal.

On November 5, 2010, the Bank assumed all of the deposits and substantially all of the assets of Western Commercial Bank, located in Woodland Hills, California, from the FDIC. The Bank recorded a pre-tax bargain purchase gain of $2.3 million in connection with this transaction.

The following table presents a summary of noninterest income:

	For the years ended December 31,	
	2010	2009
	(in thousands)	
Service charges on deposit accounts	$3,225	$3,516
Earnings on cash surrender value of life insurance	441	437
Loan sales and commissions	55	70
Net gain on sale of securities	2,014	6,469
Impairment losses on securities	(749)	(1,507)
Market gain on foreclosed assets	691	—
Gain on acquisition	2,312	—
Other income	807	1,049
Total noninterest income	$8,796	$10,034

Noninterest expense

Our noninterest expense for 2010 was $42.8 million down 9 percent from $46.9 million for 2009. The decrease in noninterest expense reflects the workforce reductions effected in the 2009 and 2010 third quarters. Noninterest expense for 2010 included integration and conversion expenses related to the FDIC-assisted Western Commercial Bank transaction of approximately $430,000. Noninterest expense for 2009 included integration and conversion expenses related to the FDIC-assisted 1st Centennial Bank transaction of approximately $774,000.

The following table presents a summary of noninterest expense:

	For the years ended December 31,	
	2010	2009
	(in thousands)	
Salaries and employee benefits	$19,014	$20,867
Premises and equipment	6,268	6,538
Data processing	2,564	2,403
Legal, audit, and other professional services	2,033	2,719
Printing, stationary, and supplies	258	757

Telephone	841	986
Directors’ fees	428	521
Advertising and marketing	918	1,380
Postage	212	245
Insurance and regulatory assessments	2,944	3,376
Loss on and expense of foreclosed property	2,954	1,563
Market value loss on loans held-for-sale	—	709
Amortization of intangible assets	1,666	1,626
Other expenses	2,705	3,166
Total noninterest expense	$42,805	$46,856

Salaries and benefits fell 9 percent to $19.0 million for 2010 from $20.9 million for 2009. The decline reflects the 2009 and 2010 third quarter workforce reductions of approximately 10 percent. In addition, stock-based compensation expense decreased by approximately $0.5 million in 2010 compared to 2009.

The FDIC charged all institutions a special insurance assessment in 2009. Our special assessment was $668,000. The insurance and regulatory assessments expense shown above for 2009 includes the FDIC special assessment. The FDIC also implemented a rule requiring insured depository institutions to prepay their quarterly risk-based assessments for the fourth quarter of 2009, and all of 2010, 2011, and 2012 on December 30, 2009. Our prepaid assessment was $9.4 million. Our regular FDIC insurance expense was $2.2 million for both 2010 and 2009. We do not anticipate any further special assessments or prepaid assessments; however, we cannot assure you that the FDIC will not increase assessment rates in future periods.

We determined in the second quarter of 2009 not to pursue the sale of $31.2 million of loans previously classified as held-for-sale and returned these performing, multifamily mortgage loans to our regular portfolio. We recognized a market loss of $709,000 in noninterest expense to reduce our carrying value to the lower of cost or market value.

The cost of foreclosed real estate and the loss on sale of foreclosed real estate was $3.0 million for 2010 compared with $1.6 million for 2009. The increase was primarily due to the recognition of a $2.1 million loss in the fourth quarter of 2010 to reduce the carrying value of a $21.0 million office complex to its estimated fair value less estimated costs of disposal. It was determined that the time to sell the units would likely be longer than the estimated timeframe in the most current appraisal, thus, resulting in a further discounting of the expected cash flows. In the fourth quarter of 2009, we recognized a loss of $1.1 million to reduce the carrying value of one property to its then-appraised fair value less estimated costs of disposal.

Our efficiency ratio was 80 percent for 2010 compared with 91 percent for 2009. The efficiency ratio is the percentage relationship of noninterest expense, excluding amortization of intangibles, to the sum of net interest income and noninterest income, excluding gains or losses on security sales. The improvement in our efficiency ratio in 2010 reflects the decline in noninterest expense coupled with the benefit of the $2.3 million gain on the Western Commercial Bank transaction.

Income taxes

The income tax provision was $0.9 million for 2010 compared with a tax benefit of $3.8 million for 2009. The effective tax rate was 40.0 percent for 2010 compared with 44.6 percent for 2009.

The combined federal and state statutory rate for 2010 and 2009 was 42.05 percent. The effective tax rates for 2010 and 2009 approximated the combined federal and state statutory tax rate because the additions to and exclusions from taxable income were not material.

Financial Position

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 six 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, among other factors.

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 in a regular manner; 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, changes 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 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, monitor delinquencies and reports quarterly to the Directors' Credit Review Committee on compliance with policies. The Directors’ Credit Review 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 1 percent to $936.1 million at December 31, 2011 from $947.7 million at December 31, 2010. The decline in commercial loans and lines of credit in 2011 includes the $3.8 million payoff of four motion picture and video production shared national credit loans. The decline in the remainder of non-covered loans in 2011 was due to payoffs and paydowns outpacing new originations for the period.

The following table presents our portfolio of non-covered loans:

	For the years ended December 31, 2011	2010	2009	2008	2007
	(in thousands)				
Commercial mortgage	$ 393,376	$ 399,634	$ 381,334	$ 302,016	$ 295,496
Commercial loans and lines of credit	180,421	213,576	235,849	228,958	189,638
Multifamily mortgage	187,333	135,639	138,548	51,607	34,198
Home mortgage	106,350	108,076	51,036	45,202	46,193
Construction and land development	35,082	55,260	86,609	133,054	148,101
Home equity loans and lines of credit	28,645	29,828	40,122	22,568	22,519
Installment & credit card	4,896	5,724	5,748	5,016	10,034
Total non-covered loans	936,103	947,737	939,246	788,421	746,179
Allowance for loan losses	(17,747)	(17,033)	(16,505)	(8,048)	(7,828)
Non-covered loans, net	$ 918,356	$ 930,704	$ 922,741	$ 780,373	$ 738,351
Loans held-for-sale	$ —	$ —	$ —	$ 31,401	$ 11,454

The loan categories above are derived from bank regulatory reporting standards for loans secured by real estate; however, a portion of the commercial and home mortgage loans above are loans that we consider to be commercial loans 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 42 percent of non-covered loans at December 31, 2011, and 2010. We had approximately 371 commercial mortgage loans with an average balance of $1,062,000. Many different commercial property types collateralize our commercial mortgage loans. Our top three categories have been industrial, office, 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 county	At December 31, 2011	At December 31, 2010
	(in thousands)	
Southern California		
Los Angeles	$ 182,282	$ 199,102
Orange	27,151	29,788
Ventura	122,921	109,684
Riverside	22,041	19,835
San Bernardino	15,538	16,233
San Diego	14,170	15,859
Santa Barbara	225	230

Total Southern California		384,328		390,731
Northern California				
Alameda		343		344
Alpine		569		—
Contra Costa		354		383
Fresno		2,404		2,443
Imperial		335		352
Kern		672		920
Madera		521		536
Placer		603		613
Sacramento		333		348
San Mateo		2,363		2,401
Solano		265		272
Tulare		286		291
Total Northern California		9,048		8,903
Total non-coverd commercial mortgage loans	$	393,376	$	399,634

The following table shows the distribution of our non-covered commercial mortgage loans by property type at December 31, 2011 and 2010.

Non-covered commercial mortgage loans by property type	At December 31, 2011 (in thousands)	At December 31, 2010
Industrial/warehouse	$ 113,480	$ 108,860
Office	87,136	98,277
Retail	64,646	65,917
Hotel	23,746	24,429
Self storage	19,752	19,409
Medical	14,043	10,388
Mixed use	12,343	14,528
Restaurant	7,771	9,419
Assisted living	5,649	5,768
All other	44,810	42,639
Total non-covered commercial mortgage loans	$ 393,376	$ 399,634

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	2012	2013	2014	2015	2016 and Thereafter	Total
2005 and earlier	$ 1,964	$ 1,707	$ 12,363	$ 5,726	$ 74,350	$ 96,110
2006	152	6,235	—	110	36,437	42,934
2007	13,002	734	7,488	—	30,946	52,170
2008	13,021	1,905	229	126	45,130	60,411
2009	1,530	—	6,018	102	51,286	58,936
2010	104	379	—	2,918	28,045	31,446
2011	52	—	—	—	51,317	51,369
Total	$ 29,825	$ 10,960	$ 26,098	$ 8,982	$ 317,511	$ 393,376

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 ratio of our non-covered commercial mortgage portfolio was 58.6 percent and the weighted average debt-service-coverage ratio was 1.70 at December 31, 2011. At December 31, 2010, the weighted-average loan-to-value ratio was 59.4 percent and debt-service-coverage ratio was 1.62 for our non-covered commercial mortgage loan portfolio. We focus on cash flow; consequently, regardless 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 affect 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.

At December 31, 2011, commercial loans were 19 percent of non-covered loans, down from 23 percent at December 31, 2010. We had approximately 843 commercial loans with an average balance of $213,000. Unused commitments on commercial loans were $110.9 million at December 31, 2011 compared with $134.9 million at December 31, 2010. 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 U.S. Small Business Administration, or SBA, or other federal or state agencies. Broadly diversified business sectors with the largest sectors in real estate/construction, finance and insurance, information, manufacturing and trade comprise the commercial loan portfolio. We also participate in larger credit facilities known as shared national credits. At December 31, 2011, five loans under these facilities had outstanding balances of $19.2 million. These loans consist of four motion picture and video production loan participations and a $0.9 million healthcare facility loan participation. At December 31, 2011, we also have a commitment of $10.0 million for one other motion picture and video production facility with no outstanding balances. Below is a table of our non-covered loans by business sector.

Non-covered commercial loans by industry/sector	At December 31, 2011	At December 31, 2010
	(in thousands)	
Real estate	$ 47,439	$ 54,387
Services	47,219	53,549
Information	30,040	44,193
Trade	22,988	22,488
Manufacturing	16,196	18,722
Healthcare	14,712	16,593
Transportation and Warehouse	1,827	3,644
Total non-covered commercial loans	$ 180,421	$ 213,576

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 generally underwrite 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.

Non-covered construction and land development loans were 4 percent of non-covered loans at December 31, 2011 down from 6 percent at December 31, 2010. At December 31, 2011, we had 31 projects with an average commitment of $1,958,000. Construction loans represent single-family, multi-family and commercial building projects. The decline in construction and land loans since the end of 2009 reflects principally the successful completion and sale of projects as well as the general reduction in new business activity. At December 31, 2011, 18 percent of these loans or $6.3 million represent single-family residential construction projects and 35 percent, or $12.3 million were commercial projects. The remaining 47 percent or $16.5 million were land development projects. Construction loans are typically short term, with maturities ranging from 12 to 18 months. Beginning in the third quarter of 2009, we changed the maximum loan-to-value to 70 percent for both commercial and residential projects from 75 percent for commercial projects and 80 percent for residential projects. The weighted average loan-to-value ratio for our non-covered construction and land portfolio was 69.9 percent at December 31, 2011 and 61.7 percent at December 31, 2010. 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 economic trends 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	At December 31, 2011 Commitment (in thousands)	At December 31, 2011 Outstanding	At December 31, 2010 Commitment	At December 31, 2010 Outstanding
Los Angeles	$29,369	$11,603	$27,168	$21,786
Orange	5,857	2,909	15,019	14,239
Ventura	20,473	15,608	16,194	12,508
Riverside	3,772	3,726	3,983	3,906
Santa Barbara	1,239	1,236	2,840	2,823
Total non-covered construction	$60,710	$35,082	$65,204	$55,260

We are mindful of the economic disruption in our marketplace and supplemented our regular monitoring practices with updated project appraisals, re-evaluation of estimated project marketing time and re-evaluation of the sufficiency of the original loan commitment to absorb interest charges (i.e., interest reserves) when necessary. We also re-evaluate the project sponsor's ability, where applicable, to successfully complete other projects funded by other institutions. In circumstances where the interest reserve was not sufficient, we request the project sponsor to make payments to us from their general resources or request the project sponsor to place with us the proceeds from a portion of the project sales. While we believe that our monitoring practices are adequate, we cannot assure you that there will not be further delinquencies, lengthened project marketing time or declines in real estate values.

Multifamily residential mortgage loans were 20 percent of non-covered loans at December 31, 2011, up from 14 percent at December 31, 2010. We had approximately 184 multifamily loans with an average balance of $1,010,000. Apartments mostly located in our six-county market area serve as collateral for our multifamily loans. We underwrite multifamily mortgage loans in a fashion similar to commercial mortgage loans previously described. The weighted average loan-to-value ratio was 60.3 percent and the weighted average debt-service-coverage ratio was 1.44 for our non-covered multifamily portfolio at December 31, 2011. A year ago, the weighted average loan-to-value ratio was 60.3 percent and the weighted average debt-service-coverage ratio was 1.34 percent. Below is a table of our non-covered multifamily mortgage loans by county.

Non-covered multi-family mortgage loans by county	At December 31, 2011 (in thousands)	At December 31, 2010
Southern California		
Los Angeles	$ 107,580	$ 92,897
Orange	15,638	15,948
Ventura	6,942	7,495
Riverside	496	502
San Bernardino	3,989	3,979
San Diego	20,965	4,999
Santa Barbara	1,853	1,876
Total	157,463	127,696
Northern California		
Alameda	7,247	787
Calaveras	1,337	1,357
Contra Costa	613	—
Fresno	239	245

Kern		2,538		2,609
Merced		650		664
Monterey		373		379
Mono		224		228
San Francisco		4,228		1,329
Santa Clara		12,085		—
Santa Cruz		336		345
Total		29,870		7,943
Total non-covered multifamily mortgage loans	$	187,333	$	135,639

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 2012	2013	2014	2015	2016 and Thereafter	Total
2005 and earlier	$ 880	$ 1,088	$ —	$ —	$ 11,702	$ 13,670
2006	—	—	—	—	1,337	1,337
2007	—	—	—	—	9,574	9,574
2008	—	—	—	—	41,321	41,321
2009	237	—	—	—	40,890	41,127
2010	—	—	—	—	9,711	9,711
2011	—	—	—	—	70,593	70,593
Total	$ 1,117	$ 1,088	$ —	$ —	$ 185,128	$ 187,333

The table below illustrates the distribution of our non-covered loan portfolio by loan size at December 31, 2011. We distribute all non-covered loans by loan balance outstanding except construction and land loans, which we distribute by loan commitment. At year-end 2011, 34 percent of our loans were less than $1 million; 79 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.

	December 31, 2011 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 $12,600,000
Commercial mortgage	10 %	14 %	32 %	14 %	19 %	11 %
Commercial loans and lines of credit	29 %	12 %	32 %	13 %	14 %	0 %
Construction and land development	3 %	7 %	45 %	15 %	30 %	0 %
Multifamily mortgage	11 %	23 %	45 %	8 %	7 %	6 %
Home mortgage	39 %	23 %	21 %	3 %	14 %	0 %
Home equity loans and lines of credit	44 %	13 %	12 %	31 %	0 %	0 %

Installment & credit card	87	%	13	%	0	%	0	%	0	%	0	%
Totals	18	%	16	%	33	%	12	%	15	%	6	%

The following table presents the scheduled maturities of fixed and variable rate loans for our non-covered and covered loan portfolios.

	December 31, 2011			
	One year or less (in thousands)	After one year to five years	After five years	Total
Fixed rate loans				
Commercial mortgage	$16,344	$49,922	$101,369	$167,635
Commercial loans and lines	16,773	31,474	19,097	67,344
Multifamily mortgage	4,601	4,518	43,021	52,140
Home mortgage	5,257	19,109	101,738	126,104
Construction and land	12,791	5,717	11,121	29,629
Home equity loans	291	2,420	6,208	8,919
Installment & credit card	1,530	923	726	3,179
Total fixed rate loan maturities	57,587	114,083	283,280	454,950
Variable rate loans				
Commercial mortgage	15,985	11,563	235,997	263,545
Commercial loans and lines	88,120	25,730	10,433	124,283
Multifamily mortgage	236	41,349	109,552	151,137
Home mortgage	1	1,090	15,891	16,982
Construction and land	17,014	8,260	3,054	28,328
Home equity loans	6,776	9,871	13,920	30,567
Installment & credit card	474	680	569	1,723
Total adjustable rate loan maturities	128,606	98,543	389,416	616,565
Total maturities	$186,193	$212,626	$672,696	$1,071,515

Allowance for 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, multifamily 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 also charge-off consumer loans by the time they become 90 days delinquent unless the loan is 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 loan losses. We assess the allowance on a monthly basis and undertake a more critical evaluation quarterly. At the time of the quarterly 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 non-accruals, 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 loans to identify specific probable losses and assigns estimated loss factors to specific groups or types of 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 loans and concentrations of credit. We refer to these as qualitative considerations.

Our year-end 2011 evaluation of the adequacy of the allowance for loan losses considered, among other things, estimated loss factors assigned to specific types of loans, changes and trends in the level of delinquencies, nonaccrual loans and loan charge-offs, changes in the value of collateral, changes in the local and regional economic and business conditions, 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 revised downward, in the fourth quarter of 2011, our estimated loss factors for our qualitative considerations. We revised upward in each of the first three quarters of 2011 and then downward in the final quarter of 2011 our estimated loss factors for our quantitative considerations. Our reasons are as follows.

We considered the trend in the level of our loan credit quality indicators, delinquencies, nonaccrual loans and loan charge-offs. Loans rated Special mention, Substandard, Doubtful or Loss decreased to $68.6 million at December 31, 2011 from $75.1 million a December 31, 2010. Total non-covered past due loans and nonaccrual loans decreased to $17.3 million at December 31, 2011 from $29.9 million at December 31, 2010. Non-covered foreclosed property decreased to $20.3 million at December 31, 2011 from $26.0 million at December 31, 2010. Net non-covered loan charge-offs decreased to $4.6 million, or 0.51% of average non-covered loans for the year ended December 31, 2011 compared with $7.8 million, or 0.85% of average non-covered loans for the year ended December 31, 2010.

We considered the marketing time and sales prices for our completed construction loan portfolio. Our non-covered construction and land loan portfolio was 4 percent of non-covered loans at December 31, 2011 compared with 6 percent at December 31, 2010. While this loan portfolio declined principally from successful marketing and sales efforts, the continued disruption in the residential and commercial mortgage loan markets and the continued downward pressure on real estate values may adversely affect these loans.

Finally, we considered the weakness of the economic recovery and the impact it might have on our borrowers, especially our small business borrowers, 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.

As a result, the allowance for loan losses increased to $17.7 million at December 31, 2011 from $17.0 million at December 31, 2010. The provision for loan losses was $5.3 million for the year ended December 31, 2011, compared with $8.3 million for the year ended December 31, 2010. The ratio of the allowance for loan losses to non-covered loans was 1.90 percent at December 31, 2011 compared with 1.80 percent at December 31, 2010.

We believe that our allowance for loan losses was adequate at December 31, 2011 and 2010. The determination of the allowance for loan losses, however, 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 the future.

The following table presents activity in the allowance for loan losses.

	For the years ended December 31,				
	2011	2010	2009	2008	2007
	(in thousands)				
Beginning balance	$17,033	$16,505	$8,048	$7,828	$4,740
Balance acquired in purchase	—	—	—	—	3,554
Provision for loan losses	5,346	8,337	16,646	1,150	—
Loans charged-off	(5,177)	(8,535)	(8,580)	(1,075)	(567)
Transfer to undisbursed commitment	—	—	—	—	—

Recoveries on loans charged-off	545		726		391		145		101	
Ending balance	$17,747		$17,033		$16,505		$8,048		$7,828	
Allowance to non-covered loans	1.90	%	1.80	%	1.76	%	1.02	%	1.05	%
Net loans charged-off to average non-covered loans	0.51	%	0.85	%	0.89	%	0.12	%	0.07	%

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

(in thousands)	Twelve months ended December 31, 2011	2010	2009
Construction	$176	$382	$853
Home mortgage	475	447	1,210
Commercial loans & lines	3,480	5,256	4,537
Commercial mortgage	366	1,680	1,599
Home equity	39	—	—
Consumer	96	44	(10)
Total	$4,632	$7,809	$8,189

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

	For the years ended December 31, 2011		2010		2009		2008		2007	
	Allocation of the allowance by loan category (in thousands)	Percent of Loans in Category to Total Non-covered Loans	Allocation of the allowance by loan category	Percent of Loans in Category to Total Non-covered Loans	Allocation of the allowance by loan category	Percent of Loans in Category to Total Non-covered Loans	Allocation of the allowance by loan category	Percent of Loans in Category to Total Non-covered Loans	Allocation of the allowance by loan category	Percent of Loans in Category to Total Non-covered Loans
Commercial mortgage	$ 6,091	42 %	$ 6,134	42 %	$ 4,850	41 %	$ 2,504	38 %	$ 2,928	40 %
Multifamily mortgage	2,886	20 %	2,273	14 %	3,277	15 %	421	7 %	174	5 %
Commercial loans	6,221	19 %	4,934	23 %	4,796	25 %	2,463	29 %	1,991	25 %
Construction loans	814	4 %	1,698	6 %	2,460	9 %	2,069	17 %	1,836	20 %
Home equity loans	390	3 %	416	3 %	453	4 %	186	3 %	75	3 %
Home mortgage	1,274	11 %	1,496	11 %	605	5 %	362	6 %	471	6 %
Installment and credit card	71	1 %	82	1 %	64	1 %	43	— %	353	1 %
Total	$ 17,747	100 %	$ 17,033	100 %	$ 16,505	100 %	$ 8,048	100 %	$ 7,828	100 %

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

We had 16 non-covered restructured loans for $4.4 million at December 31, 2011; of these, six restructured loans for $0.9 million were current at December 31, 2011, one restructured loan for $0.7 million was included in the accruing loans past due 30 to 89 days category shown below and nine restructured loans for $2.8 million were included in the nonaccrual loan category shown below. We had twelve non-covered restructured loans for $4.2 million at December 31, 2010; of these, three restructured loans for $1.3 million were current at December 31, 2010, one restructured loan for $0.7 million was included in the accruing loans past due 30 to 89 days category shown below and eight restructured loans for $2.3 million were included in the $18.2 million nonaccrual loan category shown below.

The following table presents non-covered past due and nonaccrual loans.

	For the years ended December 31,									
	2011		2010		2009		2008		2007	
	(in thousands)									
Accruing non-covered loans past due 30 to 89 days	$3,449		$11,630		$14,592		$2,644		$4,746	
Accruing non-covered loans past due 90 days or more	$—		$—		$200		$429		$2,848	
Nonaccrual loans	$13,860		$18,241		$39,958		$8,475		$5,720	
Ratios:										
Accruing loans past due 90 days or more to average non-covered loans	—		—		0.02	%	0.05	%	0.42	%
Non-covered nonaccrual loans to non-covered loans	1.48	%	1.92	%	4.25	%	1.07	%	0.77	%
Interest foregone on non-covered nonaccrual loans	$841		$2,066		$2,134		$543		$339	

Accruing non-covered loans past due 30 to 89 days decreased to $3.4 million at December 31, 2011 from $11.6 million at December 31, 2010. This category of non-covered loans historically has had the most fluctuation from period to period.

Our largest nonaccrual loan was a revolving credit facility to purchase and develop a film library with a balance of $8.5 million at December 31, 2011. This amount is after charge-offs of $3.3 million. The charge-off represented the estimated 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 December 31, 2011 a specific loss allowance of $2.6 million for this loan.

Our next largest nonaccrual loan was a $1.2 million commercial business loan. This loan was performing in accordance with modified loan terms at December 31, 2011. We estimated a specific loss allowance of $306,000 for this loan at December 31, 2011.

Our third largest nonaccrual loan was a $1.1 million commercial restaurant loan. This loan was performing in accordance with modified loan terms at December 31, 2011. We estimated a specific loss allowance of $71,000 for this loan at December 31, 2011.

All other nonaccrual loans were individually under $1 million at December 31, 2011.

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

	Twelve months ended December 31,			
	2011		2010	
	# of Loans	$ Amount	# of Loans	$ Amount
	(dollars in thousands)			
Beginning balance	28	$18,241	21	$39,958
New loans added	37	8,385	44	27,650
Repurchase of SBA-guaranteed participation	—	—	—	317
Loans transferred to foreclosed property	(5)	(3,103)	(8)	(24,806)
Loans returned to accrual status	(12)	(2,955)	(9)	(4,380)
Payoffs on existing loans	(9)	(2,144)	(11)	(11,585)
Loans sold	—	—	(1)	(490)
Partial charge-offs on existing loans	—	(221)	—	(6,170)
Charge-offs on existing loans	(10)	(3,234)	(8)	(859)
Payments on existing loans	—	(1,109)	—	(1,394)
Ending balance	29	$13,860	28	$18,241

Non-covered foreclosed property at December 31, 2011 consists of a $14.0 million completed office complex project consisting of 16 buildings in Ventura County, a $2.8 million unimproved land property of 161 acres located in an unincorporated section of western Los Angeles County known as Liberty Canyon and a $1.8 million industrial building in Costa Mesa, California. The remainder consists of one multifamily property, repossessed equipment and two single-family residences.

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

	Twelve months ended December 31,			
	2011		2010	
	# of Properties	$ Amount	# of Properties	$ Amount
	(dollars in thousands)			
Beginning balance	8	$26,011	1	$4,893

New properties added	4	3,356	10	25,660
Valuation allowances	—	(5,784)	—	(2,305)
Sales of properties	(5)	(3,234)	(3)	(2,237)
Ending balance	7	$20,349	8	$26,011

The allowance for losses on undisbursed commitments was $101,000 at both December 31, 2011, and December 31, 2010. The allowance for losses on undisbursed commitments is included in “accrued interest payable and other liabilities” on the consolidated balance sheets.

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. We determine loan impairment through periodic evaluation on an individual loan basis. The average investment in impaired loans was $17.6 million for the year ended December 31, 2011 and $26.0 million for the year ended December 31, 2010. Impaired loans were $13.9 million at December 31, 2011 and $17.2 million at December 31, 2010. Allowances for losses for individually impaired loans are based on either the estimated collateral value less estimated selling costs (if the loan is a collateral-dependent loan), or the present value of expected future cash flows discounted at the loan’s effective interest rate. Of the $13.9 million of impaired loans at December 31, 2011, $11.1 million had specific allowances of $3.1 million. Of the $17.2 million of impaired loans at December 31, 2010, $12.5 million had specific allowances of $2.0 million.

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 covered under the shared-loss agreements. We refer to all other loans in our loan portfolio not acquired from WCB or SLTB and not covered by the shared-loss agreements 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 (loans and foreclosed property). 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 increased to $135.4 million at December 31, 2011 from $53.9 million at December 31, 2010 because of the FDIC-assisted SLTB acquisition in February 2011. The following table sets forth the composition of the covered loan portfolio by type.

Covered loans by property type (in thousands)	At December 31, 2011	At December 31, 2010
Commercial mortgage	$ 37,804	$ 26,046
Home mortgage	36,736	2,046
Construction and land loans	22,875	6,143
Multifamily	15,944	2,688
Commercial loans and lines of credit	11,206	16,820
Home equity loans and lines of credit	10,841	135
Installment and credit card	6	—
Total covered loans	$ 135,412	$ 53,878

The FDIC shared-loss asset represents the present value of the amounts we expect to receive from the FDIC under the shared-loss agreements. The FDIC shared-loss asset was $68.1 million at December 31, 2011 and $16.7 million at December 31, 2010. The increase was due to the initial FDIC shared-loss asset recorded in conjunction with the FDIC-assisted SLTB acquisition on February 18, 2011.

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.

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 twelve months ended December 31, 2011.

	Twelve months ended December 31, 2011		
(in thousands)	WCB	SLTB	Total

Balance, beginning of period	$ 16,725	$ —	$ 16,725
Acquisition	—	70,293	70,293
FDIC share of additional losses	740	2,189	2,929
Cash payments received from FDIC	(8,379)	(13,672)	(22,051)
Net accretion	73	114	187
Balance, end of period	$ 9,159	$ 58,924	$ 68,083

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 $3.8 million and $1.0 million at December 31, 2011 and December 31, 2010.

Covered foreclosed property

Covered foreclosed property at December 31, 2011 was $14.6 million and $1.0 million at December 31, 2010. We acquired these properties as part of the FDIC-assisted Western Commercial Bank and San Luis Trust Bank acquisitions. We recorded these properties at their estimated fair value, less estimated costs to sell, at the time of acquisition. Since year-end 2010, we sold $19.5 million of properties and acquired or added $33.6 million.

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

	Twelve months ended December 31,			
	2011		2010	
	# of Properties	$ Amount	# of Properties	$ Amount
	(dollars in thousands)			
Beginning balance	2	$ 977	—	$ —
New properties acquired	22	11,052	2	977
New properties added	57	22,587	—	—
Valuation allowances	—	(455)	—	—
Sales of properties	(32)	(19,545)	—	—
Ending balance	49	$ 14,616	2	$ 977

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 non-brokered certificates of deposit). At December 31, 2011, core deposits were $1.2 billion. At December 31, 2010, core deposits were $892.7 million. The increase is a result of the core deposits acquired in connection with the EPS division acquisition as well as deposit growth throughout our branch network. 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, federal funds purchased from other institutions, securities sold under agreements to repurchase and borrowings. Total alternative funds used at December 31, 2011 declined to $392.9 million from $395.1 million at December 31, 2010. The increase in core deposits allowed us to reduce these funds.

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 December 31, 2011 and 2010. We also have a $14.3 million secured borrowing facility with the Federal Reserve Bank of San Francisco, which had no balance outstanding at December 31, 2011 and 2010. In addition, we had approximately $271.9 million of available borrowing capacity on the Bank's secured FHLB borrowing facility at December 31, 2011.

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 equity and debt instruments. 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 dividends 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 California state banks. A California 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 January 1, 2012, there were $27.2 million of dividends available for payment under the method described. During the years ended December 31, 2011 and 2010, we received no dividends from the Bank. The Company had $3.2 million in cash on deposit with the Bank at December 31, 2011.

In order to meet our deposit, borrowings 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 December 31, 2011, we had non-interest earning cash balances at the Reserve Bank of $34.2 million compared with $19.9 million at December 31, 2010. Interest-bearing deposits with the Reserve Bank and other financial institutions decreased to $21.2 million at December 31, 2011 from $62.5 million at December 31, 2010. The $41.3 million decrease reflects the increase in securities. We believe that these sources of liquidity will be sufficient for the Company to meet its liquidity needs over the next twelve months. A number of factors may affect funds generated from these liquidity sources. See "Risk Factors" in Part I, Item 1A of this Annual Report on Form 10-K for a discussion of the factors that can negatively affect the amount of funds we could receive.

As disclosed in the Consolidated Statements of Cash Flows, net cash used in operating activities was $6.0 million during the twelve months ended December 31, 2011. The difference between cash used by operating activities and net income largely consisted of non-cash items including a $36.9 million gain on acquisitions.

Net cash of $185.9 million provided by investing activities consisted principally of $122.1 million of cash acquired in the SLTB and EPS division acquisitions and $53.8 million of proceeds from net covered and non-covered loan paydowns.

Net cash of $165.2 million used in financing activities reflects primarily the run-off and maturities of SLTB wholesale deposits and borrowings.

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.

The following table presents securities, at amortized cost, by expected maturity distribution and weighted average yield (tax equivalent). Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	At December 31, 2011 One year or less (in thousands)	After one year to five years	After five years to ten years	Over ten years	Total
Maturity distribution					
U.S. Treasury notes/bills	$ 45,151	$ —	$ —	$ —	$ 45,151
U.S. government agency notes	21,209	38,003	—	—	59,212
U.S. government agency mortgage-backed securities	—	78,692	29,603	23,846	132,141
U.S. government agency collateralized mortgage obligations	—	121,392	43,155	3,611	168,158
Private label collateralized mortgage obligations	—	3,216	12,637	—	15,853
Municipal securities	80	—	16,647	11,845	28,572
Other domestic debt securities	—	2,500	—	4,651	7,151
Total	$ 66,440	$ 243,803	$ 102,042	$ 43,953	$ 456,238

	At December 31, 2011									
	One year or les (in thousands)		After one year to five years		After five years to ten years		Over ten years		Total	
Weighted average yield										
U.S. Treasury notes/bills	0.16	%	—		—		—		0.16	%
U.S. government agency notes	0.33	%	1.06	%	—		—		0.80	%
U.S. government agency mortgage-backed securities	—		2.54	%	2.59	%	3.70	%	2.76	%
U.S. government agency collateralized mortgage obligations	—		2.41	%	2.38	%	2.74	%	2.41	%
Private label collateralized mortgage obligations	—		6.50	%	5.54	%	—		5.73	%
Municipal securities	7.42	%	—		4.01	%	4.50	%	4.22	%
Other domestic debt securities	—		1.20	%	—		1.48	%	1.38	%
Total	0.22	%	2.28	%	3.10	%	3.60	%	2.29	%

Securities, at amortized cost, increased by $177.2 million, or 64 percent, from $279.0 million at December 31, 2010 to $456.2 million at December 31, 2011 primarily from the deployment of excess liquidity.

Net unrealized holding losses were $2.5 million at December 31, 2011 and $6.5 million at December 31, 2010. As a percentage of securities, at amortized cost, net unrealized holding losses were 0.55 percent and 2.35 percent at the end of each respective period. Securities are comprised largely of U.S. Treasury bills and notes, and U.S. government agency notes, mortgage-backed securities and collateralized mortgage obligations. 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.

We determined that, as of December 31, 2011, our U.S. Treasury notes and bills, and U.S. government agency notes, mortgage-backed securities and collateralized mortgage obligations 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 from 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 $4.7 million and an unrealized loss of $2.1 million at December 31, 2011. The gross unrealized loss was 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. One credit rating agency has now rated the security triple-C while another has rated the security Baa3. The senior tranche owned by us has a collateral balance well in excess of the amortized cost basis of the tranche at December 31, 2011. Eighteen of the fifty-six issuers in the security have deferred or defaulted on their interest payments as of December 31, 2011. 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, we concluded that the gross unrealized loss on this security was temporary.

The majority of gross unrealized losses at December 31, 2011, relate to a type of mortgage-backed security also known as private-label collateralized mortgage obligations, or CMOs. As of December 31, 2011, the current par value of these securities was $18.1 million and the amortized cost basis, net of other-than-temporary impairment charges, was $15.9 million. At year-end 2011, the fair value of these securities was $13.0 million, representing 3 percent of our securities portfolio. Gross unrealized losses for these private-label CMO’s were $2.8 million, or 18 percent of the amortized cost basis of these securities at December 31, 2011.

The gross unrealized losses on these securities were primarily due to extraordinarily high investor yield requirements resulting from an illiquid market, significant uncertainty about the future condition of the mortgage market and the economy, and continued deterioration in the credit performance of loan collateral underlying these securities, causing these securities to be valued at significant discounts to their acquisition cost. Our three private-label CMO’s had credit agency ratings of less than investment grade at December 31, 2011. We performed a discounted cash flow analysis for the these three securities using the current month, last three month and last twelve month historical prepayment speed, the cumulative default rate and the loss severity rate to determine if there was other-than-temporary impairment at year-end. Based upon this analysis, we determined that the three private-label CMO’s were other-than-temporarily impaired as of December 31, 2011 (that is, securities for which we determined that it was more likely than not that the entire amortized cost basis would not be recovered), and we recognized a credit loss of $321,000 in the fourth quarter of 2011. We had previously recognized a $1,066,000 credit loss on these three securities in the first quarter of 2011. For the year ended December 31, 2011, impairment losses charged to earnings were $1,387,000. For the year ended December 31, 2010, impairment losses charged to earnings were $749,000. This included a $41,000 impairment recognized on a $1.0 million community development-related equity investment. We do not intend to sell these securities and we do not believe it likely that we will be required to sell these securities before the anticipated recovery of the remaining amortized cost basis. If current conditions in the mortgage markets and general business and economic conditions continue to deteriorate further, the fair value of our private-label CMOs may decline further and we may experience further impairment losses. We cannot predict whether we will be required to record additional impairment charges on our securities in the future.

Deposits

The following tables present the balance of each deposit category at the periods indicated:

	At December 31, 2011 Balance	At December 31, 2010 Balance	At December 31, 2009 Balance
Core deposits			
Noninterest bearing checking	$ 482,156	$ 331,648	$ 317,610
Interest checking	107,077	88,638	82,806
Savings and money market accounts	486,000	388,289	339,750
Retail time deposits less than $100,000	74,861	84,133	90,279
Total core deposits	1,150,094	892,708	830,445
Noncore deposits			
Retail time deposits of $100,000 or more	169,523	144,974	151,753
Wholesale time deposits	5,652	18,606	32,517
State of California time deposits	100,000	100,000	110,000
Total noncore deposits	275,175	263,580	294,270
Total core and noncore deposits	$ 1,425,269	$ 1,156,288	$ 1,124,715

Large balance certificates of deposits (that is, balances of $100,000 or more) were $275.2 million at December 31, 2011. Large balance certificates of deposits were $263.6 million at December 31, 2010. 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 $67.9 billion of investments of which approximately $4.1 billion represented time deposits placed at various financial institutions. At December 31, 2011and 2010, State of California time deposits placed with us, with original maturities of three to six months, were $100.0 million. 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 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 deposit at maturity if higher rates are available elsewhere or if they perceive that our creditworthiness is deteriorating. At December 31, 2011 and 2010, we had no brokered deposits. At December 31, 2009, we had brokered deposits of $25.7 million, all of which had maturities within the following 12 months.

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 $5.7 million of these reciprocal deposits, categorized as wholesale time deposits in the table above, at December 31, 2011. We had $7.0 million and $6.8 million of these reciprocal deposits at the end of 2010 and 2009, respectively.

The following table presents the maturity of large balance certificates of deposits for the periods indicated:

	For the Years Ending December 31,													
	2011				2010				2009					
	Amount (in thousands)		Percentage		Amount		Percentage		Amount		Percentage			
Three months or less	$	132,043	48	%	$	131,710	50	%	$	156,720	58	%		
Over three months through six months		26,871	10	%		23,815	9	%		31,165	12	%		
Over six months through one year		41,644	15	%		44,002	17	%		40,136	15	%		
Over one year		74,617	27	%		63,890	24	%		40,516	15	%		
Total	$	275,175	100	%	$	263,417	100	%	$	268,537	100	%		

Borrowings

Borrowings are comprised of federal funds purchased from other financial institutions, FHLB advances and securities sold under agreements to repurchase. At December 31, 2011, we had $117.7 million of borrowings outstanding, of which $30.0 million was comprised of securities sold under agreements to repurchase and $87.7 million of FHLB advances. For our FHLB advances, the following table presents the amounts and weighted average interest rates outstanding.

	Year Ended December 31, 2011				Year Ended December 31, 2010			
	Federal Home Loan Bank Advances (in thousands)		Weighted average interest rate		Federal Home Loan Bank Advances		Weighted average interest rate	
Amount outstanding at end of period	$	87,719	3.01	%	$	86,500	3.11	%
Maximum amount outstanding at any month-end during the period	$	138,750	2.69	%	$	118,000	2.53	%
Average amount outstanding during the period	$	98,290	2.66	%	$	88,995	3.69	%

The following table presents the maturities of FHLB advances at December 31, 2011.

	Amount (in thousands)		Maturity Year	Weighted Average Interest Rate	
Term advances	$	25,551	2012	3.56	%
Term advances		7,168	2013	2.88	%
Term advances		32,500	2014	2.95	%

Term advances	15,000	2015	1.76	%
Term advances	7,500	2017	4.07	%
	$ 87,719			

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The following table presents the maturities of securities sold under agreements to repurchase at December 31, 2011.

Amount		Maturity Year	Weighted Average Interest Rate	
		(in thousands)		
$	20,000	February 2013	3.60	%
	10,000	December 2014	3.72	%
$	30,000			

Junior Subordinated Debentures

At December 31, 2011, we had $26.8 million of junior subordinated debentures outstanding from two issuances of trust preferred securities. The $10.3 million debentures due December 2035 have a variable rate of interest that resets quarterly – at March, June, September, December for each year - equal to the 3-month LIBOR rate plus 1.55%. At December 31, 2011, this rate was 2.10%. These debentures are redeemable at par and at the Company’s option at any time. The $16.5 million debentures due March 2037 have a fixed rate of interest of 6.80% until March 2012 after which they have a variable rate of interest that resets quarterly equal to the 3-month LIBOR rate plus 1.60%. These debentures are redeemable, at par, and at the Company’s option at any time on or after March 15, 2012. The weighted average interest rate paid on the debentures for 2011 was 5.00 percent and 2010 was 6.48 percent. Our interest payments for 2011 were $1.3 million and for 2010 were $1.7 million.

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 will become 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. 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. 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 December 31, 2011, we reserved 329,431 of common shares for the conversion of the preferred stock series A.

On December 19, 2008, we participated in the U.S. Treasury Capital Purchase Program, under which we received $25 million in exchange for issuing 25,000 preferred stock series B shares and a warrant to purchase common stock to the Treasury. The common stock warrant entitled the Treasury to purchase 599,042 shares of our common stock at an exercise price of $6.26 for a term of ten years. On July 14, 2011, we redeemed all 25,000 preferred stock series B shares and exited the CPP program. On August 24, 2011, we purchased the 10-year warrant from the Treasury for $599,042. In connection with the redemption of the preferred stock series B shares, the Company accelerated the amortization of the remaining difference between the par amount and the initially recorded fair value of the preferred stock series B shares. This $1.1 million deemed dividend reduced the amount of net income available to common shareholders in 2011.

We redeemed the $25 million of preferred stock series B shares with the $25 million of proceeds received in exchange for issuing 25,000 preferred stock series C shares to the Treasury as a participant in the Small Business Lending Fund (SBLF) program. The preferred stock series C shares will 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 eight quarters and is a function of the growth in qualified small business loans each quarter.

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.

On March 3, 2010, the Company's stockholders approved an amendment to the Company's Amended and Restated Certificate of Incorporation to increase the number of authorized shares of the Company's common stock, par value $0.01 per share, from 25,000,000 shares to 100,000,000 shares, and to increase the number of authorized shares of all classes of the Company's stock from 27,500,000 shares to 102,500,000 shares.

In March 2010, we consummated an underwritten public offering of common stock at a price of $2.50 per share. We sold 16,560,000 common shares, which include the exercise by the underwriter of its over-allotment option, for net proceeds of $38.9 million. We contributed $36.0 million to our bank subsidiary. We intend to use the net proceeds of this public offering for general corporate purposes, including funding working capital requirements, supporting the growth of our business from internal efforts and from whole bank or failed bank acquisitions, and regulatory capital needs related to any such growth and acquisitions.

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

	Actual Amount (in thousands)	Ratio	For Capital Adequacy Purposes Amount	Ratio
December 31, 2011				
Total capital (to risk weighted assets)	$ 194,694	17.32 %	$ 89,924	≥ 8.00 %
Tier I capital (to risk weighted assets)	$ 180,597	16.07 %	$ 44,962	≥ 4.00 %
Tier I capital (to average assets)	$ 180,597	10.33 %	$ 69,906	≥ 4.00 %

	Actual Amount (in thousands)	Ratio	For Capital Adequacy Purposes Amount	Ratio
December 31, 2010				
Total capital (to risk weighted assets)	$ 172,599	16.79 %	$ 82,242	≥ 8.00 %
Tier I capital (to risk weighted assets)	$ 159,695	15.53 %	$ 41,121	≥ 4.00 %
Tier I capital (to average assets)	$ 159,695	11.00 %	$ 58,052	≥ 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 December 31, 2011, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2011, the Bank exceeded the minimum ratios to be well-capitalized under the prompt corrective action provisions. There are no conditions or events since December 31, 2011 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:

December 31, 2011	Actual Amount (in thousands)	Ratio	For Capital Adequacy Purposes Amount	Ratio	To be Well Capitalized Under Prompt Corrective Action Provision Amount	Ratio
Total capital (to risk weighted assets)	$ 192,227	17.10 %	$ 89,944	≥ 8.00 %	$ 112,430	≥ 10.00 %
Tier I capital (to risk weighted assets)	$ 178,126	15.84 %	$ 44,972	≥ 4.00 %	$ 67,458	≥ 6.00 %
Tier I capital (to average assets)	$ 178,126	10.18 %	$ 69,968	≥ 4.00 %	$ 87,460	≥ 5.00 %

December 31, 2010	Actual Amount (in thousands)	Ratio	For Capital Adequacy Purposes Amount	Ratio	To be Well Capitalized Under Prompt Corrective Action Provision Amount	Ratio
Total capital (to risk weighted assets)	$ 167,395	16.31 %	$ 82,090	≥ 8.00 %	$ 102,613	≥ 10.00 %
Tier I capital (to risk weighted assets)	$ 154,515	15.06 %	$ 41,045	≥ 4.00 %	$ 61,568	≥ 6.00 %
Tier I capital (to average assets)	$ 154,515	10.63 %	$ 58,134	≥ 4.00 %	$ 72,668	≥ 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.

Commitments, contingent liabilities, contractual obligations and off-balance sheet arrangements

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 do 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. Commitments to extend credit were $159.5 million at December 31, 2011 compared with $199.9 million at December 31, 2010. Commercial and stand-by letters of credit were $1.5 million and $1.6 million at December 31, 2011 and December 31, 2010, respectively. The known contractual obligations of the Company at

December 31, 2011 are as follows:

	Payments Due				
	Twelve months and less	After one year but within three years	After three years but within five years	After five years	Total
	(in thousands)				
FHLB term advances	$25,551	$39,668	$15,000	$7,500	$87,719
Securities sold under agreements to repurchase	—	30,000	—	—	30,000
Salary continuation benefits	—	—	—	752	752
Deferred compensation benefits	106	—	—	—	106
Severance benefits	177	—	—	—	177
Junior subordinated debentures	—	—	—	26,805	26,805
Operating lease obligations	2,758	4,766	3,047	4,157	14,728
Total	$28,592	$74,434	$18,047	$39,214	$160,287

We have entered into deferred compensation agreements with several of our key employees. We suspended participation and contributions to these agreements in 2007. In June 2009, we terminated the plan and we distributed employee account balances as of June 2010 to the participants who elected a lump sum payment in June 2010.

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 bank interest 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 0.16% within a 12-month time horizon for an assumed 100 basis point decrease in prevailing interest rates or decrease approximately 0.19% for an assumed 100 basis point increase in prevailing interest rates. In addition, we estimated that net interest income would decrease approximately 0.35% 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	2 Years	3 Years
	-100 bps	-0.16 %	-1.14%	-3.39%
	+100 bps	-0.19%	-0.63%	0.51%
	+200 bps	-0.35%	-1.72%	1.53%
	+400 bps	-0.35%	0.15%	5.33%

All interest-earning assets, interest-bearing liabilities and related derivative contracts are included in the interest rate sensitivity analysis at December 31, 2011. At December 31, 2011, approximately 49 percent of our loans had a fixed rate of interest and approximately 51 percent had a variable interest rate. Of loans with a variable rate of interest, approximately 34 percent use an interest rate that floats with a specified index rate such as the Wall Street Journal Prime Rate or 3-month LIBOR rate. Approximately 24 percent of our variable interest rate loans use an interest rate that adjusts periodically, such as monthly, quarterly or annually, with a specified interest rate. Finally, approximately 42 percent of our variable interest rate loans have an interest rate that remains fixed for a period of time, such as 1, 3 or 5 years, then adjusts periodically with a specified index rate.

In addition, approximately 82 percent of our variable interest rate loans have a minimum, or floor, rate of interest. Of these, 48 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 66 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 7A. Quantitative and Qualitative Disclosures About Market Risk

Not Applicable.

Item 8. Financial Statements and Supplementary Data

Report of Independent Registered Public Accounting Firm

(c) Report of Independent Registered Public Accounting Firm:

To the Board of Directors and Shareholders
First California Financial Group, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of First California Financial Group, Inc. and Subsidiaries (the "Company") as of December 31, 2011 and 2010, and the related consolidated statements of operations, comprehensive income (loss), changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2011. We also have audited the Company's internal control over financial reporting as of December 31, 2011 based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Controls over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall consolidated financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of First California Financial Group, Inc. and Subsidiaries as of December 31, 2011 and

2010, and the consolidated results of their operations and their cash flows each of the three years in the period ended December 31, 2011, in conformity with generally accepted accounting principles in the United States of America. Also in our opinion, First California Financial Group, Inc. and Subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

/s/ MOSS ADAMS LLP
Portland, OR
March 15, 2012

FIRST CALIFORNIA FINANCIAL GROUP, INC. AND SUBSIDIARIES
Consolidated Balance Sheets

	December 31, 2011	December 31, 2010
	(in thousands, except share data)	
ASSETS		
Cash and due from banks	$40,202	$25,487
Interest bearing deposits with other banks	21,230	62,516
Securities available-for-sale, at fair value	453,735	272,439
Non-covered loans, net	918,356	930,704
Covered loans	135,412	53,878
Premises and equipment, net	18,480	19,710
Goodwill	60,720	60,720
Other intangibles, net	13,887	9,915
FDIC shared-loss receivable	68,083	16,725
Non-covered foreclosed property	20,349	26,011
Covered foreclosed property	14,616	977
Deferred tax assets, net	—	4,563
Cash surrender value of life insurance	12,670	12,232
Accrued interest receivable and other assets	34,924	25,457
Total assets	$1,812,664	$1,521,334
LIABILITIES AND SHAREHOLDERS' EQUITY		
Non-interest checking	$482,156	$331,648
Interest checking	107,077	88,638
Savings and money market	486,000	388,289
Certificates of deposit, under $100,000	74,861	84,296
Certificates of deposit, $100,000 and over	275,175	263,417
Total deposits	1,425,269	1,156,288
Securities sold under agreements to repurchase	30,000	45,000
Federal Home Loan Bank advances	87,719	86,500
Junior subordinated debentures	26,805	26,805
Deferred tax liabilities, net	7,370	—
FDIC shared-loss liability	3,757	988
Accrued interest payable and other liabilities	8,637	7,712
Total liabilities	1,589,557	1,323,293
Commitments and Contingencies (Note 22)		
Perpetual preferred stock – authorized 2,500,000 shares		
Series A—$0.01 par value, 1,000 shares issued and outstanding as of December 31, 2011 and 2010	1,000	1,000
Series B—$0.01 par value, no shares issued and outstanding as of December 31, 2011 and 25,000 shares at December 31, 2010	—	23,627
Series C—$0.01 par value, 25,000 shares issued and outstanding as of December 31, 2011 and no shares at December 31, 2010	25,000	—
	292	282

Common stock, $0.01 par value; authorized 100,000,000 shares; 29,220,079 shares issued at December 31, 2011 and 28,517,161 at December 31, 2010; 29,220,079 and 28,170,760 shares outstanding as of December 31, 2011 and 2010		
Additional paid-in capital	173,062	175,102
Treasury stock, no shares at cost at December 31, 2011 and 346,401 at December 31, 2010	—	(3,061)
Retained earnings	25,427	4,827
Accumulated other comprehensive loss	(1,674)	(3,736)
Total shareholders' equity	223,107	198,041
Total liabilities and shareholders' equity	$1,812,664	$1,521,334

See accompanying notes to consolidated financial statements.

FIRST CALIFORNIA FINANCIAL GROUP, INC. AND SUBSIDIARIES
Consolidated Statements of Operations

	For the Year Ended December 31,		
	2011	2010	2009
	(in thousands, except per share data)		
Interest income:			
Interest and fees on loans	$65,945	$53,240	$52,439
Interest on securities	6,303	5,914	12,086
Interest on federal funds sold and interest bearing deposits	350	196	416
Total interest income	72,598	59,350	64,941
Interest expense:			
Interest on deposits	8,012	7,973	12,131
Interest on borrowings	3,750	4,945	5,924
Interest on junior subordinated debt	1,342	1,736	1,832
Total interest expense	13,104	14,654	19,887
Net interest income before provision for loan losses	59,494	44,696	45,054
Provision for loan losses	5,346	8,337	16,646
Net interest income after provision for loan losses	54,148	36,359	28,408
Noninterest income:			
Service charges on deposit accounts	3,447	3,225	3,516
Earnings on cash surrender value of life insurance	438	441	437
Net gain on sale of securities	1,022	2,014	6,469
Impairment losses on securities	(1,387)	(749)	(1,507)
Market gain on foreclosed assets	429	691	—
Gain on acquisitions	36,922	2,312	—
Other income	3,738	862	1,119
Total noninterest income	44,609	8,796	10,034
Noninterest expense:			
Salaries and employee benefits	26,510	19,014	20,867
Premises and equipment	6,298	6,268	6,538
Data processing	3,500	2,564	2,403
Legal, audit, and other professional services	5,570	2,033	2,719
Printing, stationary, and supplies	366	258	757
Telephone	800	841	986
Director’s fees	460	428	521
Advertising and marketing	1,637	918	1,380
Postage	222	212	245
Insurance and regulatory assessments	2,199	2,944	3,376
Loss on and expense of foreclosed property, net	5,178	2,954	1,563
Market value loss on loans held-for-sale	—	—	709
Amortization of intangible assets	2,289	1,666	1,626
Other expenses	3,435	2,705	3,166
Total noninterest expense	58,464	42,805	46,856
Income (loss) before provision for income taxes	40,293	2,350	(8,414)
Provision (benefit) for income taxes	16,910	940	(3,753)
Net income (loss)	$23,383	$1,410	$(4,661)
Net income (loss) available to common shareholders	$20,828	$160	$(5,793)

Earnings (loss) per common share:			
Basic	$0.73	$0.01	$(0.50)
Diluted	$0.71	$0.01	$(0.50)

See accompanying notes to consolidated financial statements.

FIRST CALIFORNIA FINANCIAL GROUP, INC. AND SUBSIDIARIES
Consolidated Statements of Comprehensive Income (Loss)

	For the Year Ended December 31,		
	2011	2010	2009
		(in thousands)	
Comprehensive income (loss)			
Unrealized gain on securities available-for-sale	$ 3,674	$ 4,671	$ 8,998
Unrealized gain/(loss) on interest rate caps	(522)	81	12
Reclassification adjustment for impairments realized in net income	1,387	749	1,507
Reclassification adjustments for gains included in net income	(1,022)	(2,014)	(6,469)
Other comprehensive income, before taxes	3,517	3,487	4,048
Income tax expense related to items of other comprehensive income	(1,455)	(1,278)	(973)
Other comprehensive income, net of tax	2,062	2,209	3,075
Net income (loss)	23,383	1,410	(4,661)
Total comprehensive income (loss)	$ 25,445	$ 3,619	$ (1,586)

See accompanying notes to consolidated financial statements.

FIRST CALIFORNIA FINANCIAL GROUP, INC. AND SUBSIDIARIES
Consolidated Statements of Changes in Shareholders' Equity

	Preferred Stock Series A		Preferred Stock Series B		Preferred Stock Series C		Common Stock, $.01 par value		Additional Paid in	Treasury Stock	
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Capital	Shares	Amou
						(in thousands, except share data)					
Balance at December 31, 2008	1,000	$1,000	25,000	$22,713	—	$—	11,462,964	$118	$135,603	344,660	$(3,0
Stock options exercised	—	—	—	—	—	—	3,125	—	14	—	—
Issuance of restricted stock	—	—	—	—	—	—	169,075	—	—	—	—
Forfeiture of restricted stock	—	—	—	—	—	—	(10,530)	—	—	—	—
Dividends on preferred stock Series B	—	—	—	—	—	—		—	—	—	—
Amortization of preferred stock Series B discount	—	—	—	457	—	—		—	—	—	—
Stock-based compensation cost	—	—	—	—	—	—		—	1,018	—	—
Forfeiture of restricted stock in lieu of taxes	—	—	—	—	—	—	(1,741)	—	—	1,741	(11
Comprehensive income:											
Other comprehensive income, net of tax	—	—	—	—	—	—		—	—	—	—
Net(loss)	—	—	—	—	—	—		—	—	—	—
Balance at December 31, 2009	1,000	$1,000	25,000	$23,170	—	$—	11,622,893	$118	$136,635	346,401	$(3,0
Issuance of common stock	—	—	—	—	—	—	16,560,000	166	37,925	—	—
Forfeiture of restricted stock	—	—	—	—	—	—	(12,133)	(2)	—	—	—
Dividends on preferred stock Series B	—	—	—	—	—	—	—	—	—	—	—
Amortization of preferred	—	—	—	457	—	—	—	—	—	—	—

stock Series B discount											
Stock-based compensation cost	—	—	—	—	—	—	—	—	542	—	—
Adjustment for derivatives	—	—	—	—	—	—	—	—	—	—	—
Comprehensive income:											
Other comprehensive income, net of tax	—	—	—	—	—	—	—	—	—	—	—
Net income	—	—	—	—	—	—	—	—	—	—	—
Balance at December 31, 2010	1,000	$1,000	25,000	$23,627	—	$—	28,170,760	$282	$175,102	346,401	$(3,0
Issuance of restricted stock	—	—	—	—	—	—	1,100,564	10	(3,071)	(346,401)	3,06
Forfeiture of restricted stock	—	—	—	—	—	—	(51,245)	—	—	—	—
Issuance of preferred stock	—	—	—	—	25,000	25,000	—	—	—	—	—
Redemption of preferred stock	—	—	(25,000)	(25,000)	—	—	—	—	—	—	—
Repurchase of warrant	—	—	—	—	—	—	—	—	(599)	—	—
Dividends on preferred stock Series B	—	—	—	—	—	—	—	—	—	—	—
Dividends on preferred stock Series C	—	—	—	—	—	—	—	—	—	—	—
Amortization of preferred stock Series B discount	—	—	—	1,373	—	—	—	—	—	—	—
Stock-based compensation cost	—	—	—	—	—	—	—	—	1,630	—	—
Comprehensive income:											
Other comprehensive income, net of tax	—	—	—	—	—	—	—	—	—	—	—
Net income	—	—	—	—	—	—	—	—	—	—	—
Balance at December 31, 2011	1,000	$1,000	—	$—	25,000	$25,000	29,220,079	$292	$173,062	—	$—

See accompanying notes to consolidated financial statements.

FIRST CALIFORNIA FINANCIAL GROUP, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows

	For the Year Ended December 31,		
	2011	2010	2009
	(in thousands)		
Net income (loss)	$23,383	$1,410	$(4,661)
Adjustments to reconcile net income (loss) to net cash (used in) provided by operating activities:			
Provision for loan losses	5,346	8,337	16,646
Stock-based compensation costs	1,630	542	1,018
Gain on sales of securities	(1,022)	(2,014)	(6,469)
Gain on acquisitions	(36,922)	(2,312)	—
Loss on sale and valuation adjustments of foreclosed property	3,634	1,380	1,205
Market value loss on loans held-for-sale	—	—	709
Impairment loss on securities	1,387	749	1,507
Amortization of net premiums on securities available-for-sale	3,878	3,711	1,313
Depreciation and amortization of premises and equipment	2,045	1,927	1,822
Amortization of intangible assets	2,289	1,666	1,626
Change in FDIC shared-loss asset	(3,116)	—	—
(Gain) loss on disposal of premises and equipment	(133)	49	78
Proceeds from sale of, and payments received from, loans held-for-sale	—	—	181
Increase in cash surrender value of life insurance	(438)	(441)	(437)
Decrease in deferred tax assets, net of effects from acquisitions	4,563	975	(5,171)
(Increase) decrease in accrued interest receivable and other assets, net of effects from acquisitions	(2,015)	1,367	(3,746)
(Decrease) increase in accrued interest payable and other liabilities, net of effects from acquisitions	(7,449)	59	(599)
Net cash (used in) provided by operating activities	(2,940)	17,405	5,022
Purchases of securities available-for-sale, net of effects from acquisitions	(330,796)	(308,107)	(363,486)
Proceeds from repayments and maturities of securities available-for-sale	150,661	149,941	63,590
Proceeds from sales of securities available-for-sale	38,958	237,965	250,613
Proceeds from redemption of Federal Home Loan Bank and other stock	1,989	954	—
Purchases of Federal Home Loan Bank and other stock	(5)	(49)	(119)
Net change in interest bearing deposits with other banks, net of effects from acquisitions	103,376	(19,398)	128,768
Loan originations and principal collections, net of effects from acquisitions	50,756	(40,915)	(34,226)
Purchases of premises and equipment, net of effects from acquisitions	(2,145)	(1,424)	(1,097)
Proceeds from sale of premises and equipment	1,269	—	—
Proceeds from FDIC shared-loss asset	22,051	—	—
Proceeds from sale of non-covered foreclosed property	3,019	2,237	1,041
Proceeds from sale of covered foreclosed property	21,607	763	—

Net cash acquired (paid) in acquisitions	122,119	8,194	(48,790)
Net cash provided by (used in) investing activities	182,859	30,161	(3,706)
Net increase (decrease) in noninterest-bearing deposits, net of effects from acquisitions	49,257	(9,389)	34,352
Net decrease in interest-bearing deposits, net of effects from acquisitions	(137,443)	(64,340)	1,954
Net decrease in FHLB advances and other borrowings, net of effects from acquisitions	(75,322)	(11,948)	(23,448)
Dividends paid on preferred stock	(1,097)	(1,250)	(1,132)
Proceeds from exercise of stock options	—	—	14
Purchases of treasury stock	—	—	(11)
Redemption of preferred stock series B	(25,000)	—	—
Issuance of preferred stock series C	25,000	—	—
Repurchase of warrant	(599)	—	—
Issuance of common stock	—	38,091	—
Net cash (used in) provided by financing activities	(165,204)	(48,836)	11,729
Change in cash and due from banks	14,715	(1,270)	13,045
Cash and due from banks, beginning of period	25,487	26,757	13,712
Cash and due from banks, end of period	$40,202	$25,487	$26,757
Supplemental cash flow information:			
Cash paid for interest	$13,236	$14,434	$19,728
Cash paid for income taxes	$8,200	$1,000	$950
Supplemental disclosure of noncash items:			
Net change in fair value of securities available-for-sale, net of tax	$2,343	$2,162	$3,068
Net change in fair value of cash flow hedges, net of tax	$(278)	$47	$7
Non-covered loans transferred to foreclosed property	$3,356	$25,660	$6,891
Covered loans transferred to foreclosed property	$22,587	$—	$—
Dividend declared	$312	$—	$—
Acquisitions:			
Assets acquired	$458,642	$108,628	$320,002
Liabilities acquired	$437,220	$107,241	$271,212

See accompanying notes to consolidated financial statements.

FIRST CALIFORNIA FINANCIAL GROUP, INC.
Notes to Consolidated Financial Statements

NOTE 1—ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and nature of operations—First California Financial Group, Inc., or First California or the Company, was incorporated under the laws of the State of Delaware on June 7, 2006. The Company was formed as a wholly-owned subsidiary of National Mercantile Bancorp, a California corporation, or National Mercantile, for the purposes of effecting the merger and capital stock exchange with National Mercantile and acquisition of FCB Bancorp, a California corporation, or FCB, which was completed in March 2007.

On January 23, 2009, the Bank assumed the insured, non-brokered deposits of 1st Centennial Bank, totaling approximately $270 million, from the FDIC. Under the terms of the purchase and assumption agreement between the Bank and the FDIC, the Bank also purchased certain assets from the FDIC at the close of the transaction. The Bank paid cash consideration of $48.8 million to the FDIC for the assets acquired and liabilities assumed. The Bank continues to operate the former 1st Centennial Bank's six branch locations as part of the Bank's branch network.

On November 5, 2010, the Bank assumed certain liabilities and acquired certain assets and substantially all of the operations of Western Commercial Bank, or WCB, located in Woodland Hills, California, from the FDIC. The Bank acquired, received and recognized certain assets with an estimated fair value of approximately $109 million, including $55 million of loans, $32 million of cash, $16.7 million of a FDIC shared-loss asset, $2 million of securities and $3 million of other assets. Liabilities with an estimated fair value of approximately $107 million were also assumed and recognized, including $105 million of deposits and $2 million of other liabilities. The Bank recorded a pre-tax bargain purchase gain of $2.3 million in connection with this transaction. The transaction increased the number of the Bank's full-service branch locations to 18 and the Bank fully integrated the former WCB branch into its full-service branch network prior to December 31, 2010.

On February 18, 2011, the Bank assumed certain liabilities and acquired certain assets and substantially all of the operations of San Luis Trust Bank, or SLTB, located in San Luis Obispo, California, from the FDIC. The Bank acquired, received and recognized certain assets with an estimated fair value of approximately $367 million, including $139 million of loans, $99 million of cash and federal funds sold, $70 million of a FDIC shared-loss asset, $41 million of securities, $13 million of foreclosed property and $5 million of other assets. Liabilities with an estimated fair value of approximately $346 million were also assumed and recognized, including $266 million of deposits, $62 million of Federal Home Loan Bank advances, $15 million in a deferred tax liability, $3 million of a FDIC shared-loss liability and $0.4 million of other liabilities. The Bank recorded a pre-tax bargain purchase gain of $36.5 million in connection with this transaction. This transaction increased the number of the Bank's full-service branch locations to 19 and the Bank fully integrated the former SLTB branch into its full-service branch network in June 2011.

On April 8, 2011, the Bank completed the acquisition of the Electronic Banking Solutions division of Palm Desert National Bank. The transaction included the division's customer base, core deposits, and employees. The Electronic Payment Services Division, or the EPS division, its new name under the Bank, issues prepaid cards and sponsors merchant acquiring services for all national and regional networks, including Visa, MasterCard, and Discover throughout all 50 states and U.S. territories. The Bank acquired cash of $85.4 million, recognized intangible assets of $6.0 million, assumed $91 million of deposits and recognized a pre-tax bargain purchase gain of $0.5 million in connection with this transaction.

The Company serves the comprehensive banking needs of businesses and consumers in Los Angeles, Orange, Ventura, San Diego, Riverside, San Luis Obispo and San Bernardino counties through 19 full-service branch locations.

Basis of presentation and consolidation—The accompanying consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and general practices within the banking industry. The consolidated financial statements include, in conformity with generally accepted accounting principles, the accounts of the Company, the Bank, Wendy Road Office Development, LLC, a subsidiary of the Bank which manages and disposes of real estate, and SC Financial, an inactive subsidiary of First California. The Company has not consolidated the accounts of the First California Capital Trust I and FCB Statutory Trust I in its consolidated financial statements. As a result, the junior subordinated debentures issued by the Company to the Trusts are reflected on the Company's consolidated balance sheet as junior subordinated debentures. Results of operations for the year ended December 31, 2011 include the effects of the FDIC-assisted San Luis Trust Bank and the Electronic Payment Services division transactions from the date of the acquisition. All material intercompany transactions have been eliminated in consolidation. In preparing these financial statements, the Company has evaluated events and transactions subsequent to December 31, 2011 for potential recognition or disclosure.

Reclassifications—Certain reclassifications have been made to the 2010 and 2009 consolidated financial statements to conform to current year presentation. These reclassifications have no impact on previously reported earnings (loss) or retained earnings.

Management's estimates and assumptions—The preparation of the consolidated financial statements, in conformity with generally accepted accounting principles, requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheets, and revenues and expenses for the reporting periods. Actual results could differ significantly from those estimates. Significant estimations made by us primarily involve the calculation of the allowance for loan losses, the carrying amount of deferred tax assets, the carrying amount of covered loans, the carrying amount of foreclosed property, the carrying amount of the FDIC shared-loss asset and liability, the assessments for impairment related to goodwill and securities, the estimated fair value of financial instruments and the effectiveness of derivative instruments in offsetting changes in fair value or cash flows of hedged items.

Cash and due from banks—Cash and due from banks include amounts the Company is required to maintain to meet certain average reserve and compensating balance requirements of the Federal Reserve Bank of San Francisco. As of December 31, 2011 and 2010, the Company had met all reserve requirements. At December 31, 2011, the Company had an insignificant amount of cash deposits at other financial institutions in excess of FDIC insured limits.

Securities— Securities are classified as available-for-sale if the instrument may be sold in response to such factors as (1) changes in market interest rates and related changes in the prepayment risk, (2) need for liquidity, (3) changes in the availability of and the yield on alternative instruments, and (4) changes in funding sources and terms. Unrealized holding gains and losses, net of taxes, on securities available-for-sale are reported as other comprehensive income and carried as accumulated comprehensive income or loss within shareholders' equity until realized. Fair values for securities are based on quoted market prices. Realized gains and losses on the sale of securities available-for-sale are determined using the specific-identification method.

Premiums and discounts on available-for-sale securities are recognized in interest income using the effective interest method over the period to maturity.

The fair values of investment securities are evaluated according to FASB accounting standards codification guidance. Declines in the fair value of individual securities available-for-sale below their cost that are other-than-temporary result in write-downs of the individual securities to their fair value. The portion of the write-down related to credit is included in earnings as realized losses. The portion of the write-down related to other factors is included in other comprehensive income in stockholders' equity. At each financial statement date, management assesses each investment to determine if investments are temporarily impaired or if the impairment is other-than- temporary based upon the positive and negative evidence available. Evidence evaluated includes, but is not limited to, industry analyst reports, credit market conditions, and interest rate trends.

Non-covered loans, net of allowance for loan losses and net deferred loan fees/costs—Non-covered loans are stated at the amount of unpaid principal, reduced by an allowance for loan losses and net deferred loan fees/costs. Interest on non-covered loans is calculated by the simple-interest method on daily balances of the principal amount outstanding. Loan origination fees net of certain direct origination costs are capitalized and recognized as an adjustment of the yield over the life of the related non-covered loan.

The Company does not accrue interest on non-covered loans for which payment in full of principal and interest is doubtful, or which payment of principal or interest has been in default 90 days or more, unless the loan is well-secured and in the process of collection. Nonaccrual non-covered loans are considered impaired loans. Impaired loans are carried at the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's market price, or the fair value of collateral if the loan is collateral dependent. When it is doubtful the full principal and interest due on a non-covered loan will be collected, interest accrual is discontinued. Interest income is subsequently recognized only to the extent cash payments are received or when the non-covered loan is removed from nonaccrual status. Large groups of smaller balance, homogeneous non-covered loans are collectively evaluated for impairment.

Accordingly, the Company does not separately identify individual consumer and residential non-covered loans for evaluation of impairment.

The allowance for loan losses is established through a provision charged to expense. Loans are charged against the allowance when management believes that the collectability of principal is unlikely. The allowance is an amount that management believes will be adequate to absorb estimated probable losses on existing loans that may become uncollectable, based on evaluations of the collectability of loans and prior loan loss experience. The 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-one quarters. Individual loans are also evaluated for impairment and if a portion of a loan is impaired, the impaired amount is charged-off or a specific reserve is allocated for that loan. Various regulatory agencies, as a regular part of their examination process, periodically review the Company’s allowance for loan losses. Such agencies may require the Company to recognize additions to the allowance based on their judgment of information available to them at the time of their examinations.

Non-covered loans are reported as restructured when the Bank grants a concession(s) to a borrower experiencing financial difficulties that it would not otherwise consider. Examples of such concessions include forgiveness of principal or accrued interest, extending the maturity date or providing a lower interest rate than would be normally available for a transaction of similar risk. As a result of these concessions, restructured non-covered loans are impaired as the Bank will not collect all amounts due, both principal and interest, in accordance with the terms of the original loan agreement. Impairment reserves on non-collateral dependent restructured non-covered loans are measured by comparing the present value of expected future cash flows on the restructured loans discounted at the interest rate of the original loan agreement to the loan's carrying value. These impairment reserves are recognized as a specific component to be provided for in the allowance for non-covered loan and lease losses.

Covered loans—Loans acquired in a FDIC-assisted acquisition that are subject to a shared-loss agreement are referred to as "covered loans" and reported separately in our consolidated balance sheets. Covered loans are reported exclusive of the expected cash flow reimbursements expected from the FDIC. Acquired loans are aggregated into pools based on individually evaluated common risk characteristics and aggregate expected cash flows are estimated for each pool. A pool is accounted for as a single asset with a single interest rate, cumulative loss rate and cash flow expectation. The Bank aggregated all of the loans acquired in the FDIC-assisted acquisitions into different pools based on common risk characteristics such as accrual status, underlying collateral, type of interest rate (fixed or variable), types of amortization and other similar factors. A loan will be removed from a pool of loans only if the loan is sold, foreclosed, or assets are received in full satisfaction of the loan, and will be removed from the pool at its carrying value. If an individual loan is removed from a pool of loans, the difference between its relative carrying amount and its cash, fair value of the collateral, or other assets received will be recognized prospectively in the effective yield used to recognize the accretable yield on the remaining pool.

The cash flows expected to be received over the life of the pool were estimated by management with the assistance of a third party valuation specialist. These cash flows were input into a FASB ASC 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality, or ASC 310-30, compliant loan accounting system which calculates the carrying value of the pools and underlying loans, book yields, effective interest income and impairment, if any, based on actual and projected events. Default rates, loss severity, and prepayment speeds assumptions are periodically reassessed and updated within the accounting system to update our expectation of future cash flows. The excess of the cash flows expected to be collected over a pool's carrying value is considered to be the accretable yield and is recognized as interest income over the estimated life of the loan or pool using the effective yield method. The accretable yield may change due to changes in the timing and amounts of expected cash flows.

The excess of the undiscounted contractual balances due over the cash flows expected to be collected is considered to be the nonaccretable difference. The nonaccretable difference represents our estimate of the credit losses expected to occur and was considered in determining the fair value of the loans as of the acquisition date. Subsequent to the acquisition date, any increases in expected cash flows over those expected at acquisition date in excess of fair value are adjusted through an increase to the accretable yield on a prospective basis. Any subsequent decreases in expected cash flows attributable to credit deterioration are recognized by recording a provision for covered loan losses.

Premises and equipment—Premises and equipment are stated at cost, less accumulated depreciation. Depreciation is computed by the straight-line and accelerated methods over the estimated useful lives of the assets, which range from 3 to 7 years for furniture and equipment, and 10 to 39 years for building premises. Leasehold improvements are amortized over the estimated life of the lease or life of the asset, whichever is shorter. Maintenance and repairs are expensed as incurred, while major additions and improvements are capitalized. Gains and losses on dispositions are included in current operations.

Goodwill and other intangible assets—The Company has goodwill, which represents the excess of purchase price over the fair value of net assets acquired in business combinations. In accordance with generally accepted accounting principles, goodwill is not amortized and is reviewed for impairment on an annual basis or on an interim basis if an event occurs or circumstances change that would reduce the fair value of the acquired business below its carrying value. Other intangible assets consist of tradename, core deposit intangibles and contracts and customer relationship intangible. Tradename, which represents the fair value of the First California Bank name, is amortized using the straight-line method over a period of ten years. Core deposit intangibles, which represent the fair value of depositor relationships resulting from deposit liabilities assumed in acquisitions, are amortized using the straight-line method over the projected useful lives of the deposits. The contract and customer relationship intangible, which represents the fair value of the customer relationships and contracts, is amortized using the straight-line method over a period of ten years. Core deposit, contracts and customer relationship and trade name intangibles are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Impairment of goodwill and other intangibles is permanently recognized by writing down the asset to the extent that the carrying value exceeds the estimated fair value.

FDIC shared-loss asset— In conjunction with the FDIC-assisted Western Commercial Bank and San Luis Trust Bank transactions, the Bank entered into shared-loss agreements with the FDIC related to covered loans and covered foreclosed property. The FDIC shared-loss asset is initially recorded at fair value, based on the discounted value of expected future cash flows under the shared-loss agreements. The difference between the present value and the undiscounted cash flows the Company expects to collect from the FDIC is accreted into non-interest income over the life of the FDIC shared-loss asset. The FDIC shared-loss asset is reviewed quarterly and adjusted for any changes in expected cash flows based on recent performance and expectations for future performance of the covered portfolio. These adjustments are measured 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. Generally, 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. Increases and decreases to the FDIC shared-loss asset are recorded as adjustments to other non-interest income.

Non-covered foreclosed property— The Company acquires, through foreclosure or through full or partial satisfaction of a non-covered 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 non-covered foreclosed property received; we credit earnings for the fair value amount of the non-covered foreclosed property in excess of the non-covered loan due. Subsequent to foreclosure, the Company periodically assesses our disposition efforts and the estimated fair value less costs to sell of the non-covered 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 non-covered foreclosed property is included in earnings as are any ultimate gains or losses on the sale of the non-covered foreclosed property. Our recognition of gain is, however, dependent on the buyer’s initial investment in the purchase of the non-covered foreclosed property meeting certain criteria.

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. Covered foreclosed property is reported exclusive of expected reimbursement cash flows from the FDIC. Foreclosed covered loan collateral is transferred into covered foreclosed property at the collateral’s net realizable value, less estimated selling costs.

Covered foreclosed property was initially recorded at its estimated fair value on the acquisition date based on similar market comparable valuations less estimated selling costs. Any subsequent valuation adjustments due to declines in fair value will be charged to non-interest expense, and will be mostly offset by non-interest income representing the corresponding increase to the FDIC shared-loss asset for the offsetting loss reimbursement amount. Any recoveries of previous valuation adjustments will be credited to non-interest expense with a corresponding charge to non-interest income for the portion of the recovery that is due to the FDIC.

Securities sold under repurchase agreements—The Company sells securities under repurchase agreements. These transactions are accounted for as collateralized financing transactions and recorded at the amounts at which the securities were sold. The Company has provided collateral related to these agreements and may have to provide additional collateral to the counterparty, as necessary, if the fair value of the collateral fluctuates below required levels.

Federal Home Loan Bank stock and other non-marketable securities—Federal Home Loan Bank stock represents the Company’s investment in the Federal Home Loan Bank of San Francisco, or the FHLB, stock and is carried at cost because it can only be redeemed at par value. The Company’s investment in FHLB stock was $10.0 million and $7.9 million at December 31, 2011 and 2010, respectively, and is included in accrued interest receivable and other assets in the consolidated balance sheets. As a member of the FHLB system, the Company is required to maintain a minimum level of investment in FHLB stock based on specific percentages of its outstanding mortgages, total assets or FHLB advances. The Company may request redemption at par value of any stock in excess of the minimum required investment. Stock redemptions are at the discretion of the FHLB. The Company also has stock investments in other companies for CRA and other bank-related purposes. These stock investments were $1.5 million and $1.6 million at December 31, 2011 and December 31, 2010, respectively, and are carried at cost which reasonably approximates its fair value. The Company reviews its investments accounted for under the cost method at least quarterly for possible impairment. This review typically includes an analysis of facts and circumstances of each investment, the expectations of the investment’s future cash flows and capital needs, and trends in the investment’s business and cash flows. The Company would reduce the investment value when the declines in value are considered to be permanent. The Company would recognize the estimated loss as an impairment loss on investment securities, a component of non-interest income. The Company recognized an impairment loss of $41,000 on one of these CRA-related cost basis investments in 2010.

Junior subordinated debentures—The Company has two statutory business trusts that are wholly-owned subsidiaries of the Company. In private placement transactions, the trusts issued fixed rate capital securities representing undivided preferred beneficial interests in the assets of the trusts. The Company is the owner of all the beneficial interests represented by the common securities of the trusts. The purpose of issuing the capital securities was to provide the Company with a cost-effective means of obtaining Tier I capital under regulatory capital rules.

Income taxes—Deferred income tax assets and liabilities are determined based on the tax effects of the differences between the book and tax basis of the various balance sheet assets and liabilities. Deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. Deferred tax assets are recognized subject to management's 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 December 31, 2011 or December 31, 2010.

Accounting standards codification guidance clarifies the accounting for income taxes by prescribing a minimum recognition threshold is required for a tax position to meet before being recognized in the financial statements. The Company had no unrecognized tax benefits or uncertain tax positions at December 31, 2011 and December 31, 2010. The Company recognizes interest accrued and penalties related to unrecognized tax benefits in income tax expense. During the years ended December 31, 2011 and 2010, the Company recognized no interest or penalties in income tax expense. The Company files income tax returns in the U.S. federal jurisdiction and in California and is no longer subject to U.S. federal and California income tax examinations by tax authorities for years before 2008 and 2007, respectively.

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 designated hedged transactions on a quarterly basis. The Company recognizes the unrealized gains or losses of derivative instruments directly in current period earnings to the extent these instruments are not effective. At December 31, 2011, the Company had $37.1 million notional interest rate caps to limit the variable interest rate payments on our $26.8 million junior subordinated debentures. Our 2011 fourth quarter effectiveness assessment indicated that these instruments were effective. At December 31, 2011, the Bank also had $120 million notional interest rate caps that do not meet the criteria for hedge accounting to manage the interest rate risk associated with our fixed rate securities and loans. The Company may enter into derivative contracts that are intended to economically hedge certain of its risks, even though hedge accounting does not apply or the Company elects not to apply hedge accounting. Derivatives not designated as hedges are marked-to-market each period through earnings.

Off-balance sheet financial instruments—In the ordinary course of business, the Company enters into off-balance sheet financial instruments consisting of commitments to extend credit, commitments under credit card arrangements, commercial letters of credit, and standby letters of credit. These financial instruments are recorded in the financial statements when they are funded or related fees are incurred or received. The Company maintains a reserve for off-balance sheet items, included as an accrued liability. The reserve is an amount that management believes will be adequate to absorb possible losses associated with off-balance sheet credit risk. The evaluations take into consideration such factors as changes in the nature and volume of the commitments to extend credit and undisbursed balances of existing lines of credit and letters of credit.

Stock-based compensation—Stock-based compensation generally includes grants of stock options and restricted stock to employees and nonemployee directors. We account for stock-based payments, including stock options, in accordance with accounting standards guidance related to share-based compensation, and recognize them in the statement of operations based on their fair values. The fair value of stock options are being measured using a lattice option pricing model while the fair value of restricted stock awards are based on the quoted price of the Company’s common stock on the date of grant.

Advertising—Advertising costs are charged to expense during the year in which they are incurred. Advertising expenses were $273,000, $48,000 and $261,000 for the years ended December 31, 2011, 2010 and 2009, respectively.

Earnings (loss) per share—Basic earnings (loss) per common share is computed by dividing net income (loss) available to common shareholders by the weighted average number of common shares outstanding (excluding unvested restricted stock) during the period, after giving retroactive effect to stock dividends and splits. Diluted earnings (loss) per common share is calculated in a manner similar to basic earnings per share, but adjusted by assuming conversion of all potentially dilutive common stock equivalents, which include stock options and restricted shares using the treasury stock method. Diluted earnings (loss) per common share exclude common stock equivalents whose effect is antidilutive. Earnings (loss) available to common shareholders represent reported earnings (loss) less preferred stock dividends, if any.

Business combinations—Business combinations are accounted for under the acquisition method of accounting in accordance with ASC 805, Business Combinations. Under the acquisition method the acquiring entity in a business combination recognizes 100 percent of the acquired assets and assumed liabilities, regardless of the percentage owned, at their estimated fair values as of the date of acquisition. Any excess of the purchase price over the fair value of net assets and other identifiable intangible assets acquired is recorded as goodwill. To the extent the fair value of net assets acquired, including other identifiable assets, exceed the purchase price, a bargain purchase gain is recognized. Assets acquired and liabilities assumed from contingencies must also be recognized at fair value, if the fair value can be determined during the measurement period. Results of operations of an acquired business are included in the statement of operations from the date of acquisition. Acquisition-related costs, including conversion and restructuring charges, are expensed as incurred.

Fair value of financial instruments—FASB ASC 820, Fair Value Measurements and Disclosure, or ASC 820, defines fair value as 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. ASC 820 establishes a three-level hierarchy for disclosure of assets and liabilities recorded at fair value. The classification of assets and liabilities within the hierarchy is based on whether the inputs to the valuation methodology used for measurement are observable or unobservable. Observable inputs reflect market-derived or market-based information obtained from independent sources, while unobservable inputs reflect our estimates about market data. In general, fair values determined by Level 1 inputs utilize quoted prices for identical assets or liabilities traded in active markets that the Company has the ability to access. 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 assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company’s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

NOTE 2—RECENTLY ISSUED AND ADOPTED ACCOUNTING PRONOUNCEMENTS

In December 2010, the FASB issued ASU No. 2010-29, Business Combinations (Topic 805): Disclosure of Supplementary Pro Forma Information for Business Combinations. This update clarifies that if comparative financial statements are presented in disclosure of supplementary pro forma information for a business combination, revenue and earnings of the combined entity should be disclosed as though the business combination occurred as of the beginning of the comparable annual prior annual reporting period only. Additionally, supplemental pro forma disclosures should include a description of the nature and amount of material, nonrecurring pro forma adjustments included in the reported pro forma revenue and earnings. This update is effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The adoption of the ASU did not have a material impact on the Company's consolidated financial statements.

In April 2011, the FASB issued ASU No. 2011-02, A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring. This update provides additional guidance relating to when creditors should classify loan modifications as troubled debt restructurings. The ASU also ends the deferral issued in January 2011 of the disclosures about troubled debt restructurings required by ASU No. 2010-20. The Company adopted the provisions of ASU No. 2011-02 and the disclosure requirements of ASU No. 2010-20 in the interim reporting period ending September 30, 2011, and applied its provisions retrospectively to any restructurings that occurred. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements although additional disclosures regarding troubled debt restructurings have been included in the notes to the consolidated financial statements.

In May 2011, the FASB issued ASU No. 2011-04, Fair Value Measurements (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. ASU 2011-04 was issued concurrently with IFRS 13, Fair Value Measurements, to provide mainly identical guidance about fair value measurement and disclosure requirements. For U.S. GAAP, most of the changes are clarifications of existing guidance or wording changes to align with IFRS 13. ASU 2011-04 is effective during interim and annual periods beginning after December 15, 2011. Early adoption is not permitted. The Company does not expect the adoption of this ASU to have a material effect on its consolidated financial statements.

In June 2011, the FASB issued ASU No. 2011-05, Comprehensive Income (Topic 220): Presentation of Comprehensive Income. ASU 2011-05 will require companies to present the components of net income and other comprehensive income either as one continuous statement or as two consecutive statements. This standard eliminates the option to present components of comprehensive income as part of the statement of changes in stockholders' equity. This standard does not change the items which must be reported in other comprehensive income, how such items are measured, or when they must be reclassified to net income. This standard is effective for interim and annual periods beginning after December 15, 2011. Early adoption is permitted. Adoption of ASU 2011-05 is not expected to have a material effect on the Company's consolidated financial statements.

In September 2011, the FASB issued ASU 2011-08, Intangibles – Goodwill and Other – Testing Goodwill for Impairment. ASU 2011-08 provides guidance on the application of a qualitative assessment of impairment indicators in the review of goodwill impairment. The ASU provides that in the event that the qualitative review indicates that it is more likely than not that no impairment has occurred, the Company would not be required to perform a quantitative review. The provisions of ASU 2011-08 will be effective for years beginning after December 15, 2011 for both public and nonpublic entities, although earlier adoption is allowed. The Company does not expect that adoption of this standard will have a significant impact on the Company's consolidated financial statements.

In December 2011, the FASB issued ASU 2011-11, Disclosures about Offsetting Assets and Liabilities. ASU 2011-11 provides convergence to International Financial Reporting Standards, or IFRS, to provide common disclosure requirements for the offsetting of financial instruments. Existing GAAP guidance allowing balance sheet offsetting, including industry-specific guidance, remains unchanged. The new guidance is effective on a retrospective basis, including all prior periods presented, for interim and annual periods beginning on or after January 1, 2013. The Company does not expect that adoption of this standard will have a significant impact on the Company's consolidated financial statements.

In December 2011, the FASB issued ASU 2011-12, Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05. ASU 2011-12 defers the requirements of ASU 2011-05 to display reclassification adjustments for each component of other comprehensive income in both net income and other comprehensive income and to present the components of other comprehensive income in interim financial statements. During 2012, the FASB will reconsider the reclassification requirements and the timing of their implementation. Management is currently evaluating the impact both of these ASU's will have on the disclosures in the Company's consolidated financial statements.

NOTE 3—ACQUISITIONS

On April 8, 2011, or the EPS Transaction Date, the Bank completed the acquisition of the Electronic Banking Solutions division of Palm Desert National Bank. The transaction included the division's customer base, core deposits, and employees. The Bank paid cash consideration of $5.5 million to purchase the EPS division. The Bank acquired cash of $85.4 million, recognized intangible assets of $6.0 million, assumed $91 million of deposits and recognized a pre-tax bargain purchase gain of $0.5 million in connection with this transaction. The Bank desired this transaction to expand its product and service offerings and diversify its sources of revenue.

Under the acquisition method of accounting, the Bank recorded the assets acquired and liabilities assumed based on their estimated fair values as of the EPS Transaction Date. Results of operations for the year ended December 31, 2011 include the effects of the EPS acquisition from the EPS Transaction Date.

The following table summarizes the estimated fair values of the assets acquired, received and recognized and the liabilities assumed and recognized as of the EPS Transaction Date.

	(Dollars in thousands)
Assets Acquired:	
Cash	$ 85,389
Intangible assets	6,005
Other assets	89
Total assets acquired	$ 91,483
Liabilities Assumed:	
Deposits	$ 91,018
Deferred taxes	195
Total liabilities assumed	91,213
Net assets acquired (after-tax bargain purchase gain)	270
Total liabilities and net assets acquired	$ 91,483

The Bank based the allocation of the purchase price above on the fair values of the assets acquired and the liabilities assumed. The net gain represents the excess of the estimated fair value of the assets acquired over the estimated fair value of the liabilities assumed. The gain was recognized as non-interest income in the Company's Condensed Consolidated Statements of Operations. Non-interest expense for the second quarter of 2011 included integration and conversion expenses related to the EPS division acquisition of approximately $350,000. The "Salaries and employee benefits", "Data processing" and "Legal, audit, and other professional services" categories were affected on the Company's Condensed Consolidated Statements of Operations.

On February 18, 2011, or the SLTB Transaction Date, the Bank assumed certain liabilities and acquired certain assets and substantially all of the operations of SLTB from the FDIC, acting in its capacity as receiver of SLTB, pursuant to the terms of a purchase and assumption agreement entered into by the Bank and the FDIC, or the Purchase Agreement. The Bank acquired, received, and recognized certain assets with a fair value of approximately $367 million, including $139 million in loans, $99 million of cash and cash equivalents, $41 million of securities and $13 million of foreclosed property related to the transaction. These acquired assets represented approximately 20 percent of consolidated total assets at March 31, 2011. The Bank also assumed approximately $266 million of deposits and $62 million of FHLB advances related to the transaction. The Bank also recorded an FDIC shared-loss asset of $70 million, a core deposit intangible of $0.3 million, deferred tax liabilities of $15 million, a FDIC shared-loss liability of $2.6 million and a premium on time deposits acquired of $0.8 million related to the transaction. The Bank continues to operate the one former SLTB branch location as part of the Bank's 19 branch locations. The Bank desired this transaction to expand its footprint into the California central coast region.

As part of the Purchase Agreement, the Bank and the FDIC entered into shared-loss agreements, whereby the FDIC will cover a substantial portion of any future losses on loans (and related unfunded loan commitments), foreclosed property and accrued interest on loans for up to 90 days. We refer to the acquired assets subject to the shared-loss agreements collectively as covered assets. Under the terms of the shared-loss agreements, the FDIC will absorb 80 percent of losses and share in 80 percent of loss recoveries. The shared-loss agreements for commercial and residential mortgage loans are in effect for 5 years and 10 years, respectively, from the SLTB Transaction Date and the loss recovery provisions are in effect for 8 years and 10 years, respectively, from the SLTB Transaction Date.

In March 2021, approximately ten years following the SLTB Transaction Date, the Bank is 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 ($99.0 million) minus (ii) the sum of (a) 20 percent of the net loss amount, plus (b) 25 percent of the asset discount bid ($58.0 million), plus (c) 3.5 percent of total loss share assets at acquisition. At the SLTB Transaction Date, the Bank estimated a liability, on a present value basis, of $2.6 million under this provision.

Under the acquisition method of accounting, the Bank recorded the assets acquired and liabilities assumed based on their estimated fair values as of the SLTB Transaction Date. Results of operations for the year ended December 31, 2011 include the effects of the SLTB acquisition from the SLTB Transaction Date.

The following table summarizes the estimated fair values of the assets acquired, received and recognized and the liabilities assumed and recognized as of the SLTB Transaction Date.

	(Dollars in thousands)
Assets Acquired:	
Cash and cash equivalents	$98,820
Securities	40,972
Covered loans	138,792
Covered foreclosed property	12,772
FDIC shared-loss asset	70,293
Other assets	5,510
Total assets acquired	$367,159
Liabilities Assumed:	
Deposits	$266,149
FHLB advances	61,541
FDIC shared-loss liability	2,564
Deferred taxes	15,316
Other liabilities	437
Total liabilities assumed	346,007
Net assets acquired (after-tax bargain purchase gain)	21,152
Total liabilities and net assets acquired	$367,159

The Bank based the allocation of the purchase price above on the fair values of the assets acquired and the liabilities assumed. The net gain represents the excess of the estimated fair value of the assets acquired over the estimated fair value of the liabilities assumed and is influenced significantly by the FDIC-assisted transaction process. Under the FDIC-assisted transaction process, only certain assets and liabilities are transferred to the acquirer and, depending on the nature and amount of the acquirer’s bid, the FDIC may be required to make a cash payment to the acquirer. The Bank received a cash payment from the FDIC for $34.4 million. The book value of net assets transferred to the Bank was $23.6 million (i.e., the cost basis). The pre-tax gain of $36.5 million or the after-tax gain of $21.1 million recognized by the Company is considered a bargain purchase transaction under ASC 805 “Business Combinations” since the total acquisition-date fair value of the identifiable net assets acquired exceeded the fair value of the consideration transferred. The gain was recognized as non-interest income in the Company’s Condensed Consolidated Statements of Operations. Non-interest expense for the first quarter of 2011 included integration and conversion expenses related to the SLTB acquisition of approximately $515,000. The “Salaries and employee benefits”, “Data processing” and “Legal, audit, and other professional services” categories were affected on the Company’s Condensed Consolidated Statements of Operations.

In August 2011, the Bank exercised its option to purchase at fair value approximately $100,000 of furniture, fixtures and equipment related to the one SLTB branch location from the FDIC. The Bank also negotiated and executed a new five-year lease approximating current market rent for the one branch location.

The acquisition of assets and liabilities of SLTB were significant at a level to require disclosure of one year of historical financial information and related pro forma disclosure. However, given the pervasive nature of the shared-loss agreements entered into with the FDIC, the historical information of SLTB are much less relevant for purposes of assessing the future operations of the combined entity. In addition, prior to closure, SLTB had not completed an audit of their financial statements, and the Company determined that audited financial statements would not be reasonably available for the year ended December 31, 2010. Given these considerations, the Company requested, and received, relief from the Securities and Exchange Commission from submitting certain historical and pro forma financial information of SLTB.

On November 5, 2010, or the WCB Acquisition Date, the Bank acquired certain assets and assumed certain liabilities and substantially all of the operations of WCB from the FDIC, acting in its capacity as receiver of WCB, pursuant to the terms of a purchase and assumption agreement entered into by the Bank and the FDIC, or the Purchase Agreement. The Bank acquired, received and recognized certain assets with an estimated fair value of approximately $109 million, including $55 million of loans, $32 million of cash, $16.7 million of a FDIC shared-loss asset, $2 million of securities and $3 million of other assets. Liabilities with an estimated fair value of approximately $107 million were also assumed and recognized, including $105 million of deposits and $2 million of other liabilities. As part of the purchase and assumption agreement, the Bank and the FDIC entered into shared-loss agreements, whereby the FDIC will cover a substantial portion of any future losses on loans (and related unfunded loan commitments), foreclosed property and accrued interest on loans for up to 90 days. Under the terms of the shared-loss agreements, the FDIC will absorb 80 percent of losses and share in 80 percent of loss recoveries. The shared-loss agreements for commercial and residential mortgage loans are in effect for 5 years and 10 years, respectively, from November 5, 2010 and the loss recovery provisions are in effect for 8 years and 10 years, respectively, from November 5, 2010. The Bank operates the one former WCB branch location as part of the Bank’s 19 branch locations. The Bank desired this transaction to increase its penetration and market share in its existing markets.

The Bank received a cash payment from the FDIC for $2.4 million. The book value of assets transferred to the Bank was $111.1 million. The pre-tax gain of $2.3 million or the after-tax gain of $1.4 million recognized by the Company is considered a bargain purchase gain and was recognized as non-interest income in the Company's Consolidated Statements of Operations for the year ended December 31, 2010.

NOTE 4 — SECURITIES

Securities have been classified in the consolidated balance sheets according to management's intent and ability as available-for-sale. The amortized cost, unrealized gains, unrealized losses and estimated fair values of securities available-for-sale at December 31, 2011 and 2010, are summarized as follows:

	December 31, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(in thousands)			
U.S. Treasury notes/bills	$45,151	$14	$(4)	$45,161
U.S. government agency notes	59,212	257	(23)	59,446
U.S. government agency mortgage-backed securities	132,141	1,616	(82)	133,675
U.S. government agency collateralized mortgage obligations	168,158	384	(368)	168,174
Private label collateralized mortgage obligations	15,853	—	(2,811)	13,042
Municipal securities	28,572	813	(60)	29,325
Other domestic debt securities	7,151	—	(2,239)	4,912
Securities available-for-sale	$456,238	$3,084	$(5,587)	$453,735

	December 31, 2010			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(in thousands)			
U.S. Treasury notes/bills	$51,118	$44	$(8)	$51,154
U.S. government agency notes	59,426	13	(522)	58,917
U.S. government agency mortgage-backed securities	47,505	348	(528)	47,325
U.S. government agency collateralized mortgage obligations	90,120	130	(370)	89,880
Private label collateralized mortgage obligations	20,409	—	(3,515)	16,894
Municipal securities	3,159	—	(157)	3,002
Other domestic debt securities	7,244	—	(1,977)	5,267
Securities available-for-sale	$278,981	$535	$(7,077)	$272,439

At December 31, 2011, and 2010, there were no trading securities or securities held-to-maturity.

The following table shows the gross unrealized losses and amortized cost of the Company's securities with unrealized losses aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2011 and 2010. In the opinion of management, these securities are considered only temporarily impaired due to the fluctuation in market interest rates since purchase and temporary disruption in the credit markets as well as the Company’s intent and ability to hold them until fair values recover.

	At December 31, 2011					
	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. Treasury notes/bills	$ 10,029	$ (4)	$ —	$ —	$ 10,029	$ (4)
U.S. government agency notes	10,000	(23)	—	—	10,000	(23)
U.S. government agency mortgage-backed securities	40,889	(82)	—	—	40,889	(82)
U.S. government agency collateralized mortgage obligations	99,894	(368)	—	—	99,894	(368)
Private-label collateralized mortgage obligations	—	—	15,853	(2,811)	15,853	(2,811)
Municipal securities	4,039	(60)	—	—	4,039	(60)
Other domestic debt securities	—	—	7,151	(2,239)	7,151	(2,239)
	$ 164,851	$ (537)	$ 23,004	$ (5,050)	$ 187,855	$ (5,587)

	At December 31, 2010					
	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. Treasury notes/bills	$ 20,107	$ (8)	$ —	$ —	$ 20,107	$ (8)
U.S. government agency notes	41,401	(522)	—	—	41,401	(522)
U.S. government agency mortgage-backed securities	33,584	(528)	—	—	33,584	(528)
U.S. government agency collateralized mortgage obligations	57,069	(370)	—	—	57,069	(370)
Private-label collateralized mortgage obligations	—	—	20,409	(3,515)	20,409	(3,515)
Municipal securities	3,069	(157)	—	—	3,069	(157)
Other domestic debt securities	2,500	(28)	4,744	(1,949)	7,244	(1,977)
	$ 157,730	$ (1,613)	$ 25,153	$ (5,464)	$ 182,883	$ (7,077)

At December 31, 2011, there were five securities that have been in a continuous unrealized loss position for 12 months or more and forty-two securities that have been in a continuous unrealized loss position for less than 12 months. At December 31, 2010, there were five securities that have been in a continuous unrealized loss position for 12 months or more and fifty securities that have been in a continuous unrealized loss position for less than 12 months.

On a quarterly basis, the Company evaluates its individual available-for-sale securities in an unrealized loss position for OTTI. As part of this evaluation, the Company considers whether it intends to sell each security and whether it is more likely than not that it will be required to sell the security before its anticipated recovery of the amortized cost basis. If either of these conditions is met, the Company recognizes an OTTI 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, the Company considers whether it expects to recover the entire amortized cost basis of the security by comparing its best estimate of the present value of the cash flows expected to be collected from the security with the amortized cost basis of the security. If the Company's best estimate of the present value of the cash flows expected to be collected is less than the amortized cost basis, the difference is considered the credit loss.

For all the securities in its available-for-sale portfolio, the Company does not intend to sell any security and it is not more likely than not that the Company will be required to sell any security before its anticipated recovery of the remaining amortized cost basis.

The Company has determined that, as of December 31, 2011, all of the gross unrealized losses on its U.S. Treasury notes/bills, U.S. government agency notes, U.S. government agency mortgage-backed securities, U.S. government collateralized mortgage obligations and municipal securities are temporary because the gross unrealized losses were caused mainly by movements in interest rates and not by the deterioration of the issuers' creditworthiness; these securities were all with credit agency ratings of at least A+ at December 31, 2011. For its U.S. Treasury notes/bills, U.S. government agency notes, U.S. government agency mortgage-backed securities and U.S. government collateralized mortgage obligations the Company expects to recover the entire amortized cost basis of these securities because it determined that the strength of the issuers' guarantees through direct obligations or support from the U.S. government is sufficient to protect the Company from losses based upon current expectations. As a result, the Company expects to recover the entire amortized cost basis of these securities.

The Company owns one pooled trust preferred security, rated triple-A at purchase, with an amortized cost basis of $4.7 million and an unrealized loss of $2.1 million at December 31, 2011. 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. One credit rating agency has now rated the security Baa3 while another has rated the security triple-C-. The senior tranche owned by the Company has a collateral balance well in excess of the amortized cost basis of the tranche at December 31, 2011. Eighteen of the fifty-six issuers in the security have deferred or defaulted on their interest payments as of December 31, 2011. The Company’s analysis determined that approximately half of the issuers would need to default on their interest payments before the senior tranche owned by the Company would be at risk of loss. As the Company’s estimated present value of expected cash flows to be collected is in excess of the amortized cost basis, the Company considers the gross unrealized loss on this security to be temporary.

The majority of gross unrealized losses at December 31, 2011 relate to a type of mortgage-backed security also known as private-label collateralized mortgage obligations, or CMOs. As of December 31, 2011, the fair value of these securities was $13.0 million, representing 3 percent of our securities portfolio. Gross unrealized losses related to these securities amounted to $2.8 million, or 18 percent of the amortized cost basis of these securities as of December 31, 2011. The gross unrealized losses on these securities were primarily due to extraordinarily high investor yield requirements resulting from an illiquid market, significant uncertainty about the future condition of the mortgage market and the economy, and continued deterioration in the credit performance of loan collateral underlying these securities, causing these securities to be valued at significant discounts to their acquisition cost. Three private-label CMO’s had credit agency ratings of less than investment grade at December 31, 2011. To assess whether it expects to recover the entire amortized cost basis of its private-label CMO’s, the Company performed a cash flow analysis for the three securities rated less than investment grade at December 31, 2011. In performing the cash flow analysis for each security, the Company utilized a third-party model which considers borrower characteristics and the particular attributes of the loans underlying the Company’s securities, which estimates future cash flows based upon the estimated prepayments, default rates and loss severities input by the Company. The Company estimated the prepayments, default rates and loss severities of each individual security based upon the 3-month historical collateral performance of each security. This model then allocated the projected loan level cash flows and losses to the various security classes in each security structure in accordance with the structure’s prescribed cash flow and loss allocation rules. When the credit enhancement for the senior securities in a structure is derived from the presence of subordinated securities, losses are generally allocated first to the subordinated securities until their principal balance is reduced to zero. The projected cash flows are based on a number of assumptions and expectations, and the results from this model can vary significantly with changes in assumptions and expectations.

Based upon this analysis, three private-label CMO’s were determined to be other-than-temporarily impaired as of December 31, 2011 (that is, securities for which the Company determined that it was more likely than not that the entire amortized cost basis would not be recovered), and a credit loss of $321,000 was recognized in earnings in the fourth quarter of 2011. The Company had previously recognized a $1,066,000 OTTI credit loss on these three securities in the first quarter of 2011. The Company does not intend to sell these securities and it is not more likely than not that the Company will be required to sell these securities before its anticipated recovery of the remaining amortized cost basis. If current conditions in the mortgage markets and general business and economic conditions continue to deteriorate further, the fair value of the Company’s mortgage-related securities may decline further and the Company may experience OTTI of additional securities in future periods, as well as further impairment of securities that were identified as other-than-temporarily impaired at December 31, 2011. The Company cannot predict whether it will be required to record additional OTTI charges on its securities in the future.

The Company has committed to contribute capital of $1.0 million to participate in a community development-related investment fund whose purpose is to develop and revitalize economically depressed areas. As of December 31, 2011 and 2010 the Company had contributed capital, net of distributions, of $816,000 and $855,000, respectively. During 2010, the fund recognized impairment losses on certain investments within the fund and the Company recognized its proportionate share of those impairment losses of $41,000. The Company will continue to monitor the investment values within the fund at each reporting date and can provide no assurance there will not be an other-than-temporary impairment in future periods.

The following table presents the other-than-temporary impairment activity related to credit loss, which is recognized in earnings, for the years ended December 31, 2011 and 2010.

	For the Years Ended December 31,		
	2011	2010	2009
		(in thousands)	
Beginning balance	$2,256	$1,507	$—
Addition of other-than-temporary impairment that was not previously recognized	—	120	1,507
Additional increases to the amount related to the credit loss for which an other-than-temporary impairment was previously recognized	1,387	664	—
Reduction for securities sold during the period	—	(35)	—
Ending balance	$3,643	$2,256	$1,507

Proceeds from the sale of securities for the year ended December 31, 2011 amounted to $39.0 million resulting in gross realized gains of $1.1 million and gross realized losses of $0.1 million, respectively. Proceeds from sale of securities for the year ended December 31, 2010 were $238.0 million resulting in gross realized gains of $2.4 million and gross realized losses of $0.4 million, respectively. Proceeds from the sale of securities for the year ended December 31, 2009 were $251.1 million and resulted in gross realized gains of $6.9 million and gross realized losses of $0.4 million, respectively.

The amortized cost and estimated fair value of securities by contractual maturities are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Mortgage-backed securities may mature earlier than their contractual maturities because of principal prepayments.

	At December 31, 2011	
	Amortized Cost	Fair Value
	(in thousands)	
Due in one year or less	$ 66,440	$ 66,472
Due after one year through five years	40,503	40,598
Due after five years through ten years	96,907	96,928
Due after ten years	252,388	249,737
	$ 456,238	$ 453,735

As of December 31, 2011, securities with an estimated fair value of $49.2 million were pledged to secure public and other deposits, as required by law, repurchase agreements, and the Federal Reserve Bank's discount window.

NOTE 5 – NON-COVERED LOANS AND ALLOWANCE FOR NON-COVERED LOAN LOSSES

The loans not acquired in the SLTB and WCB acquisitions and which are not covered by the related shared-loss agreements with the FDIC are referred to as non-covered loans. The non-covered loan portfolio by type consists of the following:

(in thousands)	At December 31, 2011	At December 31, 2010
Commercial mortgage	$393,376	$399,634
Commercial loans and lines of credit	180,421	213,576
Home mortgage	106,350	108,076
Multifamily	187,333	135,639
Construction and land loans	35,082	55,260
Home equity loans and lines of credit	28,645	29,828
Installment and credit card	4,896	5,724
Total non-covered loans	936,103	947,737
Allowance for loan losses	(17,747)	(17,033)
Non-covered loans, net	$918,356	$930,704

At December 31, 2011, loans with a balance of $668.2 million were pledged as security for Federal Home Loan Bank of San Francisco, or FHLB, advances. Non-covered loan balances include net deferred loan costs of $3.4 million and

$0.4 million at December 31, 2011 and December 31, 2010, respectively.

Most of the Company's lending activity is with customers located in Los Angeles, Orange, Ventura, Riverside, San Bernardino, San Diego and San Luis Obispo Counties and most loans are secured by or dependent on real estate. Although the Company has no significant exposure to any individual customer, economic conditions, particularly the recent sustained decline in real estate values in Southern California, could adversely affect customers and their ability to satisfy their obligations under their loan agreements.

Changes in the allowance for non-covered loan losses were as follows:

(in thousands)	Twelve months ended December 31, 2011	2010	2009
Beginning balance	$17,033	$16,505	$8,048
Provision for loan losses	5,346	8,337	16,646
Loans charged-off	(5,177)	(8,535)	(8,580)
Recoveries on loans previously charged-off	545	726	391
Balance, end of period	$17,747	$17,033	$16,505

The following table details activity in the allowance for non-covered loan losses by portfolio segment for the year ended December 31, 2011. Allocation of a portion of the allowance to one segment of the loan portfolio does not preclude its availability to absorb losses in other segments.

(in thousands)	Commercial Mortgage	Commercial	Multifamily	Construction and Land	Home Mortgage	Home Equity	Installment	Total
Allowance for credit losses:								
Beginning balance	$ 6,134	$ 4,934	$ 2,273	$ 1,698	$1,496	$416	$ 82	$17,033
Charge-offs	(312)	(3,988)	(71)	(191)	(475)	(39)	(101)	(5,177)
Recoveries	—	508	17	15	—	—	5	545
Provision	269	4,767	667	(708)	253	13	85	5,346
Ending balance	$ 6,091	$ 6,221	$ 2,886	$ 814	$1,274	$390	$ 71	$17,747
Ending balance; individually evaluated for impairment	$ —	$ 3,057	$ —	$ —	$—	$—	$ —	$3,057
Ending balance; collectively evaluated for impairment	6,091	3,164	2,886	814	1,274	390	71	14,690
Non-covered loan balances:								
Ending balance	$ 393,376	$ 180,421	$ 187,333	$ 35,082	$106,350	$28,645	$ 4,896	$936,103
Ending balance; individually evaluated for	$ —	$ 11,594	$ 837	$ —	$1,387	$—	$ 42	$13,860

impairment								
Ending balance; collectively evaluated for impairment	$ 393,376	$ 168,827	$ 186,496	$ 35,082	$104,963	$28,645	$ 4,854	$922,243

The following table details activity in the allowance for non-covered loan losses by portfolio segment for the year ended December 31, 2010. Allocation of a portion of the allowance to one segment of the loan portfolio does not preclude its availability to absorb losses in other segments.

(in thousands)	Commercial Mortgage	Commercial	Multifamily	Construction and Land	Home Mortgage	Home Equity	Installment	Total
Allowance for credit losses:								
Beginning balance	$ 4,850	$ 4,796	$ 3,277	$ 2,460	$605	$453	$ 64	$16,505
Charge-offs	(648)	(5,480)	(1,170)	(560)	(422)	(199)	(56)	(8,535)
Recoveries	138	225	—	177	174	—	12	726
Provision	1,794	5,393	166	(379)	1,139	162	62	8,337
Ending balance	$ 6,134	$ 4,934	$ 2,273	$ 1,698	$1,496	$416	$ 82	$17,033
Ending balance; individually evaluated for impairment	$ —	$ 1,627	$ 150	$ 168	$18	$—	$ —	$1,963
Ending balance; collectively evaluated for impairment	6,134	3,307	2,123	1,530	1,478	416	82	15,070
Non-covered loan balances:								
Ending balance	$ 399,634	$ 213,576	$ 135,639	$ 55,260	$108,076	$29,828	$ 5,724	$947,737
Ending balance; individually evaluated for impairment	$ 1,458	$ 12,376	$ 668	$ 698	$1,967	$—	$ —	$17,167
Ending balance; collectively evaluated for impairment	$ 398,176	$ 201,200	$ 134,971	$ 54,562	$106,109	$29,828	$ 5,724	$930,570

Nonaccrual loans are those loans for which management has discontinued accrual of interest because reasonable doubt exists as to the full and timely collection of either principal or interest. Nonaccrual loans are also considered impaired loans. Total non-covered nonaccrual loans totaled $13.9 million at December 31, 2011 as compared to $18.2 million at December 31, 2010. The allowance for loan losses maintained for non-covered nonaccrual loans was $3.1 million and $2.0 million at December 31, 2011 and December 31, 2010, respectively. Had these loans performed according to their original terms, additional interest income of $0.8 million and $1.6 million would have been recognized in the twelve months ended December 31, 2011 and 2010, respectively.

The following table sets forth the amounts and categories of our non-covered nonaccrual loans at the dates indicated.

	At December 31, 2011	At December 31, 2010
Nonaccrual loans		
Aggregate loan amounts		
Construction and land	$ —	$ 698
Commercial mortgage	—	1,458
Multifamily	837	668
Commercial loans	11,594	13,450
Home mortgage	1,387	1,967
Installment	42	—
Total non-covered nonaccrual loans	$ 13,860	$ 18,241

Included in non-covered nonaccrual loans at December 31, 2011 were nine restructured loans totaling $2.8 million. The nine loans consist of one home mortgage loan and eight commercial loans. Interest income recognized on these loans was $34,000 for the twelve months ended December 31, 2011. We have no commitments to lend additional funds to these borrowers.

Included in non-covered nonaccrual loans at December 31, 2010 were eight restructured loans totaling $2.3 million. The eight loans consist of one home mortgage loan and seven commercial loans. Interest income recognized on these loans was $27,000 for the year ended December 31, 2010. We had no commitments to lend additional funds to these borrowers.

Credit Quality Indicators

All loans are risk rated based on analysis of the current state of the borrower's credit quality. This analysis of credit quality includes a review of all sources of repayment, the borrower's current financial and liquidity status and all other relevant information. The Company utilizes a ten grade risk rating system, where a higher grade represents a higher level of credit risk. The ten grade risk rating system can be generally classified by the following categories: Pass, Special Mention, Substandard, Doubtful and Loss. The risk ratings reflect the relative strength of the sources of repayment.

Pass loans are generally considered to have sufficient sources of repayment in order to repay the loan in full in accordance with all terms and conditions. These borrowers may have some credit risk that requires monitoring, but full repayment is expected. Special Mention loans are considered to have potential weaknesses that warrant close attention by management. Special Mention is considered a transitory grade and generally, the Company does not have a loan stay graded Special Mention for longer than six months. If any potential weaknesses are resolved, the loan is upgraded to a Pass grade. If negative trends in the borrower's financial status or other information is presented that indicates the repayment sources may become inadequate, the loan is downgraded to a Substandard grade. Substandard loans are considered to have well-defined weaknesses that jeopardize the full and timely repayment of the loan. Substandard loans have a distinct possibility of loss if the deficiencies are not corrected. Additionally, when management has assessed a potential for loss but a distinct possibility of loss is not recognizable, the loan is still classified as Substandard. Doubtful loans have insufficient sources of repayment and a high probability of loss. Loss loans are considered to be uncollectible and of such little value that they are no longer considered bankable assets. These internal risk ratings are reviewed continuously and adjusted due to changes in borrower status and likelihood of loan repayment.

The table below presents the non-covered loan portfolio by credit quality indicator as of December 31, 2011.

	Pass	Special Mention	Substandard	Doubtful	Loss	Total
			(in thousands)			
Home mortgage	$ 103,239	$ 1,326	$ 1,785	$ —	$ —	$ 106,350
Commercial mortgage	366,078	17,798	9,500	—	—	393,376
Construction and land	31,623	196	3,263	—	—	35,082
Multifamily	178,064	2,972	6,297	—	—	187,333
Commercial loans and lines	155,850	4,030	11,937	8,604	—	180,421
Home equity loans and lines	28,139	—	506	—	—	28,645

Installment		4,516		268		112		—		—		4,896
Total	$	867,509	$	26,590	$	33,400	$	8,604	$	—	$	936,103

The table below presents the non-covered loan portfolio by credit quality indicator as of December 31, 2010.

	Pass	Special Mention	Substandard	Doubtful	Loss	Total
			(in thousands)			
Home mortgage	$ 103,669	$ —	$ 4,407	$ —	$ —	$ 108,076
Commercial mortgage	372,961	20,899	5,774	—	—	399,634
Construction and land	46,137	133	8,990	—	—	55,260
Multifamily	127,549	4,187	3,903	—	—	135,639
Commercial loans and lines	188,548	4,401	20,449	178	—	213,576
Home equity loans and lines	28,378	1,405	45	—	—	29,828
Installment	5,412	289	23	—	—	5,724
Total	$ 872,654	$ 31,314	$ 43,591	$ 178	$ —	$ 947,737

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 non-covered loans, segregated by class of loan, as of December 31, 2011 and December 31, 2010.

	At December 31, 2011						
	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	Nonaccrual past due loans	Current loans	Total
				(in thousands)			
Commercial loans and lines	$ 41	$ 1,071	$ —	$ 1,112	$ 11,594	$ 167,715	$ 180,421
Commercial mortgage	648	—	—	648	—	392,728	393,376
Multifamily	1,010	—	—	1,010	837	185,486	187,333
Construction and land	—	—	—	—	—	35,082	35,082
Home mortgage	—	—	—	—	1,387	104,963	106,350
Home equity loans and lines	406	100	—	506	—	28,139	28,645
Installment	172	1	—	173	42	4,681	4,896
Total	$ 2,277	$ 1,172	$ —	$ 3,449	$ 13,860	$ 918,794	$ 936,103

	At December 31, 2010						
	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	Nonaccrual past due loans	Current loans	Total

	(in thousands)						
Commercial loans and lines	$ 896	$ 449	$ —	$ 1,345	$ 13,449	$ 198,782	$ 213,576
Commercial mortgage	658	686	—	1,344	1,458	396,832	399,634
Multifamily	632	—	—	632	668	134,339	135,639
Construction and land	—	8,293	—	8,293	698	46,269	55,260
Home mortgage	—	—	—	—	1,968	106,108	108,076
Home equity loans and lines	—	—	—	—	—	29,828	29,828
Installment	7	9	—	16	—	5,708	5,724
Total	$ 2,193	$ 9,437	$ —	$ 11,630	$ 18,241	$ 917,866	$ 947,737

The Company considers a loan to be impaired when, based on current information and events, the Company does not expect to be able to collect all amounts due according to the loan contract, including scheduled interest payments. Impaired loans are determined by periodic evaluation on an individual loan basis. The average investment in non-covered impaired loans was $17.6 million and $26.0 million in the twelve months ended December 31, 2011 and 2010, respectively. There was no interest income recognized on non-covered impaired loans in the twelve months ended December 31, 2011 and 2010, respectively. Non-covered impaired loans were $13.9 million and $17.2 million at December 31, 2011 and December 31, 2010, respectively. Of the $13.9 million of non-covered impaired loans at December 31, 2011, $11.1 million had specific reserves totaling $3.1 million. Of the $17.2 million of non-covered impaired loans at December 31, 2010, $12.5 million had specific reserves totaling $2.0 million.

Impaired non-covered loans as of December 31, 2011 are set forth in the following table.

(in 000's)	Unpaid Principal Balance	Recorded Investment with no Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
Commercial loans and lines	$ 13,776	$ 471	$ 11,123	$ 11,594	$ 3,057	$ 9,374	$ —
Multifamily	837	837	—	837	—	140	—
Home mortgage	1,887	1,387	—	1,387	—	1,035	—
Installment	42	42	—	42	—	4	—
Total	$ 16,542	$ 2,737	$ 11,123	$ 13,860	$ 3,057	$ 10,553	$ —

Impaired non-covered loans as of December 31, 2010 are set forth in the following table.

(in 000's)	Unpaid Principal Balance	Recorded Investment with no Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
Commercial loans and lines	$ 19,211	$ 1,691	$ 10,685	$ 12,376	$ 1,627	$ 5,701	$ —
Commercial mortgage	1,458	1,458	—	1,458	—	486	—
Multifamily	905	—	668	668	150	670	—
Home mortgage	2,542	1,530	437	1,967	18	1,189	—
Construction	698	—	698	698	168	223	—
Total	$ 24,814	$ 4,679	$ 12,488	$ 17,167	$ 1,963	$ 8,269	$ —

The average recorded investment in impaired non-covered loans shown in the above tables represents the average investment for the period in the non-covered loans impaired at each respective period-end.

Troubled Debt Restructurings

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

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

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

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

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

Combination modification – Any other type of modification, including the use of multiple categories above.

The following tables present non-covered loan troubled debt restructurings as of December 31, 2011 and 2010.

	December 31, 2011					
	Accrual Status		Nonaccrual Status		Total Modifications	
	#	$	#	$	#	$
Commercial mortgage	6	$ 878	—	$ —	6	$ 878
Commercial loans & lines	—	—	8	2,665	8	2,665
Multifamily	1	725	—	—	1	725
Home mortgage	—	—	1	158	1	158
Total	7	$ 1,603	9	$ 2,823	16	$ 4,426

	December 31, 2010					
	Accrual Status		Nonaccrual Status		Total Modifications	
	#	$	#	$	#	$
Commercial mortgage	1	$ 658	—	$ —	1	$ 658
Commercial loans & lines	3	1,276	7	2,132	10	3,408
Multifamily	—	—	—	—	—	—
Home mortgage	—	—	1	158	1	158
Total	4	$ 1,934	8	$ 2,290	12	$ 4,224

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 non-covered loans that occurred during the twelve months ended December 31, 2011 and 2010, respectively.

	Twelve months ended December 31, 2011							
	Term Modifications		Payment Modifications		Combo Modifications		Total Modifications	
	#	$	#	$	#	$	#	$
Pre-modification outstanding recorded investment:	(in thousands)							
Commercial loans & lines	—	$—	2	$83	3	$1,280	5	$1,363
Multifamily	—	—	—	—	1	626	1	626
Installment	—	—	—	—	1	5	1	5
Total	—	$—	2	$83	5	$1,911	7	$1,994

	Twelve months ended December 31, 2011							
	Term Modifications		Payment Modifications		Combo Modifications		Total Modifications	
	#	$	#	$	#	$	#	$
Post-modification outstanding recorded investment:	(in thousands)							
	—	$ —	2	$ 83	3	$ 1,280	5	$ 1,363

Commercial loans & lines											
Multifamily	—		—	—		—	1		614	1		614
Installment	—		—	—		—	1		5	1		5
Total	—	$	—	2	$	83	5	$	1,899	7	$	1,982

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	Twelve months ended December 31, 2010							
	Term Modifications		Payment Modifications		Combo Modifications		Total Modifications	
	#	$	#	$	#	$	#	$
Pre-modification outstanding recorded investment:				(in thousands)				
Commercial loan & lines	2	$545	3	$2,487	7	$617	12	$3,649
Home mortgage	—	—	—	—	1	158	1	158
Total	2	$545	3	$2,487	8	$775	13	$3,807

	Twelve months ended December 31, 2010							
	Term Modifications		Payment Modifications		Combo Modifications		Total Modifications	
	#	$	#	$	#	$	#	$
Post-modification outstanding recorded investment:				(in thousands)				
Commercial loans & lines	2	$ 545	3	$ 2,487	7	$ 579	12	$ 3,611
Home mortgage	—	—	—	—	1	158	1	158
Total	2	$ 545	3	$ 2,487	8	$ 737	13	$ 3,769

During the twelve months ended December 31, 2011, one non-covered loan for $4,000 modified as a troubled debt restructuring had a payment default occurring within 12 months of the restructure date. There were no non-covered loans modified as a troubled debt restructuring and had a payment default occurring within 12 months of the restructure date during the twelve months ended December 31, 2010.

NOTE 6 – 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 table presents a reconciliation of the undiscounted contractual cash flows, nonaccretable difference, accretable yield, and the fair value of covered loans for each respective acquired loan portfolio at the acquisition dates.

	Western Commercial November 5, 2010	San Luis Trust Bank February 18, 2011	Total
Undiscounted contractual cash flows	$81,431	$252,263	$333,694
Undiscounted cash flows not expected to be collected (nonaccretable difference)	(20,094)	(81,586)	(101,680)
Undiscounted cash flows expected to be collected	61,337	170,677	232,014
Accretable yield at acquisition	(5,848)	(31,885)	(37,733)
Estimated fair value of loans acquired at acquisition	$55,489	$138,792	$194,281

The following tables present the changes in the accretable yield for the twelve months ended December 31, 2011 and 2010 for each respective acquired loan portfolio.

	Twelve months ended December 31, 2011		
	Western Commercial	San Luis Trust Bank	Total
Balance, beginning of period	$5,457	$—	$5,457
Additions resulting from acquisitions	—	31,885	31,885
Accretion to interest income	(3,836)	(10,089)	(13,925)
Reclassifications (to)/from nonaccretable difference	7,778	33,522	41,300
Balance, end of period	$9,399	$55,318	$64,717

	Twelve months ended December 31, 2010		
	Western Commercial	San Luis Trust Bank	Total
Balance, beginning of period	$—	$—	$—
Additions resulting from acquisition	5,848	—	5,848
Accretion to interest income	(391)	—	(391)
Reclassifications (to)/from nonaccretable difference	—	—	—
Balance, end of period	$5,457	$—	$5,457

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

Covered loans by property type (in thousands)	At December 31, 2011	At December 31, 2010
Commercial mortgage	$37,804	$26,046
Home mortgage	36,736	2,046
Construction and land loans	22,875	6,143
Multifamily	15,944	2,688
Commercial loans and lines of credit	11,206	16,820
Home equity loans and lines of credit	10,841	135
Installment and credit card	6	—
Total covered loans	$135,412	$53,878

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 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 $68.1 million at December 31, 2011 and $16.7 million at December 31, 2010.

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 twelve months ended December 31, 2011.

	Twelve months ended December 31, 2011		
(in thousands)	WCB	SLTB	Total
Balance, beginning of period	$16,725	$—	$16,725
Acquisition	—	70,293	70,293
FDIC share of additional losses	740	2,189	2,929
Cash payments received from FDIC	(8,379)	(13,672)	(22,051)
Net accretion	73	114	187
Balance, end of period	$9,159	$58,924	$68,083

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 $3.8 million and $1.0 million at December 31, 2011 and December 31, 2010.

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 exceed 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 December 31, 2011 and December 31, 2010, 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 December 31, 2011 and December 31, 2010.

	At December 31, 2011						
	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	Nonaccrual past due loans	Current loans	Total
				(in thousands)			
Commercial loans and lines	$ 109	$ —	$ —	$ 109	$ 1,338	$ 9,759	$ 11,206
Commercial mortgage	—	—	—	—	3,043	34,761	37,804
Multifamily	97	—	—	97	3,670	12,177	15,944
Construction and land	755	—	—	755	3,920	18,200	22,875
Home mortgage	793	909	511	2,213	6,389	28,134	36,736
Home equity loans and lines	243	—	—	243	187	10,411	10,841
Installment	—	—	—	—	—	6	6
Total	$ 1,997	$ 909	$ 511	$ 3,417	$ 18,547	$ 113,448	$ 135,412

	At December 31, 2010						
	Accruing loans 30-59	Accruing loans 60-89	Accruing loans 90+	Total Accruing	Nonaccrual past due	Current loans	Total

	days past due	days past due	days past due	past due loans (in thousands)	loans		
Commercial loans and lines	$ 1,056	$ 180	$ 400	$ 1,636	$ 1,074	$ 14,110	$ 16,820
Commercial mortgage	1,353	—	—	1,353	1,024	23,669	26,046
Multifamily	—	—	—	—	428	2,260	2,688
Construction and land	2,289	—	—	2,289	1,799	2,055	6,143
Home mortgage	—	—	—	—	—	2,046	2,046
Home equity loans and lines	—	—	—	—	—	135	135
Total	$ 4,698	$ 180	$ 400	$ 5,278	$ 4,325	$ 44,275	$ 53,878

The increases in these amounts since December 31, 2010 were due to the FDIC-assisted San Luis Trust Bank acquisition in February 2011. At December 31, 2011, included in covered non-accrual loans were restructured loans totaling $9.6 million.

At December 31, 2010, included in covered non-accrual loans was one restructured commercial mortgage loan for $0.9 million. Interest income recognized on this loan was $18,000 for the year ended December 31, 2010. We had no commitment to lend additional funds to this borrower.

The table below presents the covered loan portfolio by credit quality indicator as of December 31, 2011.

	Pass	Special Mention	Substandard	Doubtful	Loss	Total
			(in thousands)			
Home mortgage	$11,213	$5,953	$19,570	$—	$—	$36,736
Commercial mortgage	17,888	10,737	9,179	—	—	37,804
Construction and land	4,447	4,129	14,299	—	—	22,875
Multifamily	9,247	—	6,697	—	—	15,944
Commercial loans and lines of credit	3,076	2,057	5,952	121	—	11,206
Home equity loans and lines	8,513	1,327	1,001	—	—	10,841
Installment	2	—	4	—	—	6
	$54,386	$24,203	$56,702	$121	$—	$135,412

The table below presents the covered loan portfolio by credit quality indicator as of December 31, 2010.

	Pass	Special Mention	Substandard	Doubtful	Loss	Total
			(in thousands)			
Home mortgage	$1,210	$—	$836	$—	$—	$2,046
Commercial mortgage	18,171	2,855	4,849	171	—	26,046
Construction and land	231	—	4,803	1,109	—	6,143
Multifamily	2,260	—	428			