COMMUNITY WEST BANCSHARES /
Form 10-Q
May 14, 2012

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

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2012

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: 000-23575

COMMUNITY WEST BANCSHARES
(Exact name of registrant as specified in its charter)

California (State or other jurisdiction of incorporation or organization)	77-0446957 (I.R.S. Employer Identification No.)
445 Pine Avenue, Goleta, California (Address of principal executive offices)	93117 (Zip Code)

(805) 692-5821
(Registrant's telephone number, including area code)

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. x 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x YES o NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition 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 o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company x

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

Number of shares of common stock of the registrant outstanding as of May 9, 2012: 5,989,510 shares

TABLE OF CONTENTS

The financial statements included in this Form 10-Q should be read in conjunction with Community West Bancshares' Annual Report on Form 10-K for the fiscal year ended December 31, 2011

Table of Contents

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Community West Bancshares
Consolidated Balance Sheets

(in thousands, except shares)	March 31, 2012 (unaudited)	December 31, 2011
Assets		
Cash and due from banks	$43,120	$ 22,547
Federal funds sold	25	25
Cash and cash equivalents	43,145	22,572
Time and interest bearing deposits in other financial institutions	5,403	347
Investment securities available-for-sale, at fair value; amortized cost of $17,889 at March 31, 2012 and $23,350 at December 31, 2011	17,876	23,588
Investment securities held-to-maturity, at amortized cost; fair value of $14,973 at March 31, 2012 and $16,067 at December 31, 2011	14,270	15,335
Federal Home Loan Bank stock, at cost	4,013	4,214
Federal Reserve Bank stock, at cost	1,343	1,343
Loans:		
Loans held for sale, at lower of cost or fair value	58,460	77,303
Loans held for investment, net of allowance for loan losses of $14,705 at March 31, 2012 and $15,270 at December 31, 2011	446,181	455,413
Total loans	504,641	532,716
Foreclosed real estate and repossessed assets	5,776	6,701
Premises and equipment, net	3,067	3,090
Other assets	23,691	23,442
Total assets	$623,225	$ 633,348
Liabilities		
Deposits:		
Non-interest-bearing demand	$54,986	$ 49,894
Interest-bearing demand	291,529	289,796
Savings	19,579	19,429
Time deposits	144,705	152,143
Total deposits	510,799	511,262
Other borrowings	51,000	61,000
Convertible debentures	7,852	7,852
Other liabilities	2,464	2,608
Total liabilities	572,115	582,722
Stockholders' equity		
Preferred stock, no par value; 10,000,000 shares authorized; 15,600 shares issued and outstanding	15,141	15,074
Common stock, no par value; 20,000,000 shares authorized; 5,989,510 shares issued and outstanding at March 31, 2012 and December 31, 2011	33,430	33,422
Retained earnings	2,548	1,991
Accumulated other comprehensive income, net	(9)	139
Total stockholders' equity	51,110	50,626

Total liabilities and stockholders' equity	$623,225	$ 633,348

See accompanying notes

3

Table of Contents

Community West Bancshares
Consolidated Income Statements (unaudited)

	Three Months Ended March 31,	
(in thousands, except per share amounts)	2012	2011
Interest income		
Loans	$ 8,082	$ 9,044
Investment securities and other	239	286
Total interest income	8,321	9,330
Interest expense		
Deposits	1,265	1,670
Other borrowings and convertible debentures	528	591
Total interest expense	1,793	2,261
Net interest income	6,528	7,069
Provision for loan losses	1,983	983
Net interest income after provision for loan losses	4,545	6,086
Non-interest income		
Other loan fees	250	230
Gains from loan sales, net	1,097	82
Document processing fees	92	105
Loan servicing, net	151	148
Service charges	120	130
Other	178	43
Total non-interest income	1,888	738
Non-interest expenses		
Salaries and employee benefits	2,885	3,109
Occupancy and equipment expenses	495	505
FDIC assessment	426	302
Professional services	325	215
Advertising and marketing	57	70
Depreciation and amortization	77	98
Loss on sale and write-down of foreclosed real estate and repossessed assets	409	459
Data processing	135	127
Other operating expenses	805	924
Total non-interest expenses	5,614	5,809
Income before provision for income taxes	819	1,015
Provision for income taxes	-	420
Net income	$ 819	$ 595
Preferred stock dividends	262	262
Net income applicable to common stockholders	$ 557	$ 333
Earnings per common share:		
Basic	$ 0.09	$ 0.06
Diluted	$ 0.08	$ 0.05
Basic weighted average number of common shares outstanding	5,990	5,960
Diluted weighted average number of common shares outstanding	8,233	8,245

See accompanying notes

Table of Contents

Community West Bancshares
Consolidated Statements of Comprehensive Income (unaudited)

	Three Months Ended March 31,	
(in thousands)	2012	2011
Net income	$ 819	$ 595
Other comprehensive loss, net of tax:		
Net unrealized loss on securities available-for-sale	(148)	(35)
Comprehensive income	$ 671	$ 560

See accompanying notes

Table of Contents

Community West Bancshares
Consolidated Statement of Stockholders' Equity

(in thousands)	Preferred Stock	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balances at January 1, 2012	$15,074	5,990	$33,422	$1,991	$ 139	$ 50,626
Stock option expense, recognized in earnings			8			8
Comprehensive income:						
Net income				819		819
Change in unrealized gain (loss)					(148)	(148)
Securities available-for-sale, net						
Dividends on preferred stock	67			(262)		(195)
Balances at March 31, 2012	$15,141	5,990	$33,430	$2,548	$ (9)	$ 51,110

See accompanying notes

Community West Bancshares
Consolidated Statement of Stockholders' Equity

(in thousands)	Preferred Stock	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balances at January 1, 2011	$14,807	5,916	$33,133	$13,523	$ 179	$ 61,642
Stock option expense, recognized in earnings			7			7
Conversion of debentures		60	210			210
Exercise of stock options		5	19			19
Comprehensive income:						
Net income				595		595
Change in unrealized gain (loss)					(35)	(35)
Securities available-for-sale, net						
Dividends on preferred stock	67			(262)		(195)
Balances at March 31, 2011	$14,874	5,981	$33,369	$13,856	$ 144	$ 62,243

See accompanying notes

6

Table of Contents

Community West Bancshares
Consolidated Statements of Cash Flows

	Three Months Ended March 31, 2012	2011
	(in thousands)	
Cash flows from operating activities:		
Net income	$ 819	$ 595
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,983	983
Depreciation and amortization	77	98
Deferred income taxes	338	-
Stock-based compensation	8	7
Net amortization of discounts and premiums for investment securities	(6)	(22)
Net loss (gain) on:		
Sale and write-downs of foreclosed real estate and repossessed assets	409	459
Sale of loans held for sale	(1,097)	(82)
Sale of available-for-sale securities	(121)	-
Loan originated for sale and principal collections, net	2,429	3,171
Changes in:		
Servicing rights, net of amortization	(248)	29
Other assets	(87)	(1,993)
Other liabilities	(292)	(216)
Net cash provided by operating activities	4,212	3,029
Cash flows from investing activities:		
Purchase of available-for-sale securities	-	(2,362)
Principal pay downs and maturities of available-for-sale securities	1,460	2,407
Proceeds from sale of available-for-sale securities	4,137	-
Redemptions of Federal Home Loan Bank stock	201	200
Principal pay downs and maturities of held-to-maturity securities	1,056	1,125
Loan originations and principal collections, net	22,308	6,396
Proceeds from sale of foreclosed real estate and repossessed assets	2,967	824
Net increase in time and interest bearing deposits in other financial institutions	(5,056)	-
Purchase of premises and equipment, net	(54)	(130)
Net cash provided by investing activities	27,019	8,460
Cash flows from financing activities:		
Preferred stock dividends	(262)	(262)
Amortization of discount on preferred stock	67	67
Exercise of stock options	-	19
Net increase in demand deposits and savings accounts	6,975	32,215
Net decrease in time certificates of deposit	(7,438)	(34,490)
Repayment of Federal Home Loan Bank advances	(10,000)	-
Net cash used in financing activities	(10,658)	(2,451)
Net increase in cash and cash equivalents	20,573	9,038
Cash and cash equivalents, beginning of year	22,572	6,226
Cash and cash equivalents, end of period	$ 43,145	$ 15,264
Supplemental Disclosure of Cash Flow Information:		
Cash paid for interest	$ 1,687	$ 2,495
Cash paid for income taxes	$ 616	$ 815
Supplemental Disclosure of Noncash Investing Activity:		

Transfers to foreclosed real estate and repossessed assets	$ 2,451	$ 2,469

See accompanying notes

Table of Contents

COMMUNITY WEST BANCSHARES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

The interim consolidated financial statements reflect all adjustments and reclassifications that, in the opinion of management, are necessary for the fair presentation of the results of operations and financial condition for the interim period. The unaudited consolidated financial statements include Community West Bancshares (CWBC) and its wholly-owned subsidiary, Community West Bank, N.A. (CWB or the Bank). CWBC and CWB are referred to herein collectively as the “Company”. The accompanying unaudited Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) and with the instructions to Form 10-Q and Article 8-03 of Regulation S-X promulgated by the Securities and Exchange Commission (SEC). Accordingly, they do not include all of the information and footnotes required for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been reflected in the financial statements. The results of operations for the three-month period ended March 31, 2012 are not necessarily indicative of the results to be expected for the full year.

These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Loans Held for Investment – Loans are recognized at the principal amount outstanding, net of unearned income, loan participations and amounts charged off. Unearned income includes deferred loan origination fees reduced by loan origination costs. Unearned income on loans is amortized to interest income over the life of the related loan using the level yield method. The following is a description of the loan categories held for investment.

Commercial Loans
In addition to traditional term commercial loans made to business customers, the Company grants revolving business lines of credit. Under the terms of the revolving lines of credit, the Company grants a maximum loan amount, which remains available to the business during the loan term. Generally, as part of the loan requirements, the business agrees to maintain its primary banking relationship with the Company. The Company does not extend material loans of this type in excess of two years.

Commercial Real Estate
Commercial real estate and construction loans are primarily made for the purpose of purchasing, improving or constructing single-family residences, commercial or industrial properties. This loan category also includes SBA 504 loans and land loans.

A substantial portion of the Company's real estate construction loans are first and second trust deeds on the construction of owner-occupied single family dwellings. The Company also makes real estate construction loans on commercial properties. These consist of first and second trust deeds collateralized by the related real property. Construction loans are generally written with terms of six to eighteen months and usually do not exceed a loan to appraised value of 80%.

Commercial and industrial real estate loans are secured by nonresidential property. Office buildings or other commercial property primarily secure these loans. Loan to appraised value ratios on nonresidential real estate loans are generally restricted to 80% of appraised value of the underlying real property if occupied by the owner or owner’s business; otherwise, these loans are generally restricted to 75% of appraised value of the underlying real property.

SBA 504 loans are made in conjunction with Certified Development Companies. These loans are granted to purchase or construct real estate or acquire machinery and equipment. The loan is structured with a conventional first trust deed provided by a private lender and a second trust deed which is funded through the sale of debentures. The predominant structure is terms of 10% down payment, 50% conventional first loan and 40% debenture.

Conventional and investor loans are sometimes funded by our secondary-market partners and the Company receives a premium for these transactions.

Table of Contents

SBA Loans

The SBA loans consist of 7(a) and Business and Industry loans ("B&I"). The 7(a) loan proceeds are used for working capital, machinery and equipment purchases, land and building purposes, leasehold improvements and debt refinancing. In general, the SBA guarantees up to 85% of the loan amount depending on loan size. In certain instances, the Company sells a portion of the loans, however, under the SBA 7(a) loan program, the Company is required to retain a minimum of 5% of the principal balance of each loan it sells into the secondary market.

B&I loans are guaranteed by the U.S. Department of Agriculture. The guaranteed amount is generally 80%. B&I loans are similar to the 7(a) loans but are made to businesses in designated rural areas. These loans can also be sold into the secondary market.

Single Family Real Estate Loans

The Company originates loans that consist of first and second mortgage loans secured by trust deeds on one to four family homes. These loans are made to borrowers for purposes such as purchasing a home, refinancing an existing home, interest rate reduction, home improvement, or debt consolidation. Generally, these loans are underwritten to specific investor guidelines and are committed for sale to that investor. Although the majority of these loans are sold servicing released into the secondary market, a relatively small percentage is held as part of the Company's portfolio.

Manufactured Housing Loans

The Company originates loans secured by manufactured homes located in approved mobile home parks in our primary lending area of Santa Barbara and Ventura Counties as well as along the California coast. The loans are serviced internally and are originated under one of two programs: fixed rate loans written for terms of 10 to 20 years; adjustable rate loans written for a term of 30 years with the initial interest rates fixed for the first 5 or 10 years and then adjusting annually subject to caps and floors.

HELOC

The Company provides lines of credit collateralized by residential real estate, home equity lines of credit (HELOC), for consumer related purposes. Typically, HELOCs are collateralized by a second deed of trust.

Other Installment Loans

Installment loans consist of automobile and general-purpose loans made to individuals. These loans are primarily fixed rate.

Provision and Allowance for Loan Losses – The Company maintains a detailed, systematic analysis and procedural discipline to determine the amount of the allowance for loan losses ("ALL"). The ALL is based on estimates and is intended to be adequate to provide for probable losses inherent in the loan portfolio. This process involves deriving probable loss estimates that are based on migration analysis/historical loss rates and qualitative factors that are based on management's judgment. The migration analysis and historical loss rate calculations are based upon the annualized loss rates utilizing a twelve quarter loss history. Migration analysis is utilized for the Commercial Real Estate, Commercial, and SBA portfolios. The historical loss rate method is utilized for the homogeneous loan categories which include Manufactured Housing, HELOC's, Single Family Residential, and Consumer loans. The migration analysis takes into account the risk rating of loans that are charged off in each loan category. In loan categories that historic loss rates are utilized, management increases the reserve requirement for Special Mention and Substandard loans. Loans that are considered Doubtful are typically charged off. The following is a description of the characteristics of loans graded Pass, Special Mention, Substandard, Doubtful, and Loss. Loan ratings are reviewed as part of our normal loan monitoring process, but, at a minimum, updated on an annual basis.

Pass

Loans rated in this category are acceptable loans, appropriately underwritten, bearing an ordinary risk of loss to the Company. Loans in this category are loans to quality borrowers with financial statements presenting a good primary source as well as an adequate secondary source of repayment. In the case of individuals, borrowers deserving of this rating are quality borrowers demonstrating a reasonable level of secure income, a net worth adequate to support the loan and presenting a good primary source as well as an adequate secondary source of repayment.

Special Mention

A Special Mention loan has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or in the institution's credit position at some future date.

Table of Contents

Substandard
A Substandard loan is inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Loss potential, while existing in the aggregate amount of substandard loans does not have to exist in individual loans classified Substandard.

Doubtful
A loan classified Doubtful has all the weaknesses inherent in one classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors, which may work to the advantage and strengthening of the loan, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition or liquidation procedures, capital injection, perfecting liens on additional collateral, and refinancing plans.

Loss
Loans classified Loss are considered uncollectible and of such little value that their continuance as bankable loans is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this loan even though partial recovery may be affected in the future. Losses are taken in the period in which they surface as uncollectible. The following is the Company’s policy regarding charging off loans by loan categories.

Commercial, Commercial Real Estate and SBA Loans
Charge-offs on these loan categories are taken as soon as all or a portion of any loan balance is deemed to be uncollectible. A loan is considered uncollectible when the debtor is delinquent in principal or interest repayment 90 days or more and, in the opinion of the Company, improvement in the debtor's ability to repay the debt in a timely manner is doubtful. Also, collateral value is insufficient to cover the outstanding indebtedness. Loans secured by real estate on which principal or interest is due and unpaid for 90 days are evaluated for possible charge-down. Generally, loan balances are charged-down to the fair value of the property, if, based on a current appraisal, an apparent deficiency exists. In the event there is no perceived equity, the loan is charged-off in full like any other unsecured loan, which is not secured and over 90 days.

Single Family Real Estate, HELOC’s and Manufactured Housing Loans
Consumer loans and residential mortgages secured by one-to-four family residential properties, HELOC and manufactured housing loans in which principal or interest is due and unpaid for 90 days, are evaluated for possible charge-down. Loan balances are charged-down to the fair value of the property if, based on a current appraisal, an apparent deficiency exists. In the event there is no perceived equity, the loan is generally charged-off in full like any other consumer loan, which is not secured and unpaid over 90-120 days.

Consumer Loans
All consumer loans (excluding real estate mortgages, home equity loans and savings secured loans) are charged-off or charged-down to net recoverable value before becoming 120 days or 5 payments delinquent. Consumer losses are identified well before the 120 day limit whenever possible. Net recoverable value can only be determined if the collateral is in the Company's possession, and its liquidation value can be verified and realized in the near term.

The second component of the ALL covers qualitative factors related to non-impaired loans. The qualitative allowance on each of the loan pools is based on the following factors:

- Concentrations of credit
- Trends in volume, maturity, composition
- Volume and trend in delinquency
- Economic conditions
- Outside exams
- Geographic distance

Table of Contents

- Policy and procedures
- Staff experience and ability

The ALL calculation for the different loan portfolios is as follows:

- Commercial Real Estate, Commercial and SBA – Migration analysis combined with risk rating is used to determine the required allowance for all non-impaired loans. In addition, the migration results are adjusted based upon the qualitative factors previously discussed that affect this specific portfolio category. Reserves on impaired loans are determined based upon the individual characteristics of the loan.

- Manufactured Housing, Single Family Residential, HELOC and Consumer – The allowance is calculated on the basis of loss history and risk rating, which is primarily a function of delinquency. In addition, the migration results are adjusted based upon the qualitative factors previously discussed that affect this specific portfolio.

The Company evaluates and individually assesses impairment on loans greater than $100,000 classified as substandard or doubtful that are either non-performing or considered a trouble debt restructure. Measured impairment is determined on a loan-by-loan basis and in total establishes a specific reserve for impaired loans. The amount of impairment is determined by comparing the recorded investment in each loan with its value measured by one of three methods.

- The expected future cash flows are estimated and then discounted at the effective interest rate.
- The loan's observable market price, if it is of a kind for which there is a secondary market.
- The value of the underlying collateral net of selling costs. Selling costs are estimated based on industry standards, the Company's actual experience, or actual costs incurred as appropriate. When evaluating real estate collateral, the Company typically uses appraisals or valuations, no more than twelve months old at time of evaluation. When evaluating non-real estate collateral securing the loan, the Company will use audited financial statements or appraisals no more than twelve months old. Additionally for both real estate and non-real estate collateral, the Company may use other sources to determine value as deemed appropriate.

Interest income is not recognized on impaired loans except for limited circumstances in which a loan, although impaired, continues to perform in accordance with the loan contract.

The Company determines the appropriate ALL on a monthly basis. Any differences between estimated and actual observed losses from the prior month are reflected in the current period in determining the appropriate ALL determination and adjusted as deemed necessary. The review of the adequacy of the allowance takes into consideration such factors as concentrations of credit, changes in the growth, size and composition of the loan portfolio, overall and individual portfolio quality, review of specific problem loans, collateral, guarantees and economic conditions that may affect the borrowers' ability to pay and/or the value of the underlying collateral. Additional factors considered include: geographic location of borrowers, changes in the Company's product-specific credit policy and lending staff experience. These estimates depend on the outcome of future events and, therefore, contain inherent uncertainties.

The Company's ALL is maintained at a level believed adequate by management to absorb known and inherent probable losses on existing loans. A provision for loan losses is charged to expense. The allowance is charged for losses when management believes that full recovery on the loan is unlikely.

The Company has a centralized appraisal management process that tracks and monitors appraisals, appraisal reviews and other valuations. The centralization focus is to ensure the use of qualified and independent appraisers capable of providing reliable real estate values in the context of ever changing market conditions. The review process is monitored to ensure application of the appropriate appraisal methodology, agreement with the interpretation of market data and the resultant real estate value. The process also provides the means of tracking the performance quality of the appraisers on the Company's approved appraiser list. Any loan evaluation that results in the Company determining that elevated credit risk and/or default risk exists and also exhibits a lack of a timely valuation of the collateral or apparent collateral value deterioration is reappraised and reevaluated to determine the current extent of any change in collateral value and credit risk. A similar review process is conducted quarterly on all classified and criticized real estate credits to determine the timeliness and adequacy of the real estate collateral value. A detection of non-compliance is then addressed through a new appraisal or reappraisal and review.

Table of Contents

Foreclosed Real Estate and Repossessed Assets – Foreclosed real estate and other repossessed assets are recorded at fair value at the time of foreclosure less estimated costs to sell. Any excess of loan balance over the fair value less estimated costs to sell of the other assets is charged-off against the allowance for loan losses. Subsequent to the legal ownership date, management periodically performs a new valuation and the asset is carried at the lower of carrying amount or fair value less estimated costs to sell. Operating expenses or income, and gains or losses on disposition of such properties, are recorded in current operations.

Income Taxes – The Company uses the asset and liability method, which recognizes a liability or asset representing the tax effects of future deductible or taxable amounts that have been recognized in the consolidated financial statements. Due to tax regulations, certain items of income and expense are recognized in different periods for tax return purposes than for financial statement reporting. These items represent "temporary differences." Deferred income taxes are recognized for the tax effect of temporary differences between the tax basis of assets and liabilities and their financial reporting amounts at each period end based on enacted tax laws and statutory tax rates applicable to the periods in which the differences are expected to affect taxable income. A valuation allowance is established for deferred tax assets if, based on weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets may not be realized.

As of December 31, 2011, the deferred tax assets, net of valuation allowance, totaled $306,000. Management evaluates the Company's deferred tax assets for recoverability using a consistent approach which considers the relative impact of negative and positive evidence, including the Company's historical profitability and projections of future taxable income. The Company is required to establish a valuation allowance for deferred tax assets and record a charge to income if Management determines, based on available evidence at the time the determination is made, that it is more likely than not that some portion or all of the deferred tax assets may not be realized.

For the three-year period ended December 31, 2011, the Company was in a cumulative pretax loss position. For purposes of establishing a deferred tax valuation allowance, this cumulative pretax loss position was considered significant, objective evidence that the Company may not be able to realize some portion of the deferred tax asset in the future. As a result, the Company established a valuation allowance for the deferred tax asset of $6.7 million as of December 31, 2011. The net deferred tax asset of $306,000 represented the estimated amount of tax that Management has determined may be recoverable through carryback of tax losses to prior years.

Net income represents positive evidence for the reduction of the deferred tax valuation allowance. Based on net income of $819,000 for the first quarter of 2012, the deferred tax valuation allowance was reduced by 338,000 from $6.7 million at December 31, 2011 to $6.3 million at March 31, 2012. The net deferred tax asset increased from $306,000 at December 31, 2011 to $644,000 at March 31, 2012.

The Company is subject to the provisions of ASC 740, Income Taxes (ASC 740). ASC 740 prescribes a more-likely-than-not threshold for the financial statement recognition of uncertain tax positions. ASC 740 clarifies the accounting for income taxes by prescribing a minimum recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. On a quarterly basis the Company evaluates income tax accruals in accordance with ASC 740 guidance on uncertain tax positions.

Recent Accounting Pronouncements – In April 2011, the FASB issued ASU No. 2011-02, "A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring." The provisions of ASU No. 2011-02 provide additional guidance related to determining whether a creditor has granted a concession, include factors and examples for creditors to consider in evaluating whether a restructuring results in a delay in payment that is insignificant, prohibit creditors from using the borrower's effective rate test to evaluate whether a concession has been granted to the borrower, and adds factors for creditors to use in determining whether a borrower is experiencing financial difficulties. A provision in ASU No. 2011-02 also ends the FASB's deferral of the additional disclosures related to troubled debt restructurings as required by ASU No. 2010-20. The provisions of ASU No. 2011-02 were effective for the Company's reporting period beginning on or after June 15, 2011. In the third quarter of 2011, the Company adopted the provisions of ASU No. 2010-20 retrospectively to all modifications and restructuring activities that have occurred from January 1, 2011.

Table of Contents

In May 2011, the FASB issued ASU No. 2011-04, "Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs." ASU No. 2011-04 results in a consistent definition of fair value and common requirements for measurement of and disclosure about fair value between U.S. GAAP and International Financial Reporting Standards ("IFRS"). The changes to U.S. GAAP as a result of ASU No. 2011-04 are as follows: (1) The concepts of highest and best use and valuation premise are only relevant when measuring the fair value of nonfinancial assets (that is, it does not apply to financial assets or any liabilities); (2) U.S. GAAP currently prohibits application of a blockage factor in valuing financial instruments with quoted prices in active markets. ASU No. 2011-04 extends that prohibition to all fair value measurements; (3) An exception is provided to the basic fair value measurement principles for an entity that holds a group of financial assets and financial liabilities with offsetting positions in market risks or counterparty credit risk that are managed on the basis of the entity's net exposure to either of those risks. This exception allows the entity, if certain criteria are met, to measure the fair value of the net asset or liability position in a manner consistent with how market participants would price the net risk position; (4) Aligns the fair value measurement of instruments classified within an entity's shareholders' equity with the guidance for liabilities; and (5) Disclosure requirements have been enhanced for recurring Level 3 fair value measurements to disclose quantitative information about unobservable inputs and assumptions used, to describe the valuation processes used by the entity, and to describe the sensitivity of fair value measurements to changes in unobservable inputs and interrelationships between those inputs. In addition, entities must report the level in the fair value hierarchy of items that are not measured at fair value in the balance sheet but whose fair value must be disclosed. The provisions of ASU No. 2011-04 are effective for the Company's interim reporting period beginning on or after December 15, 2011. The adoption of ASU No. 2011-04 did not have a material impact on the Company's statements of income and condition.

In June 2011, the FASB issued ASU No. 2011-05, "Presentation of Comprehensive Income." The provisions of ASU No. 2011-05 allow an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income (OCI) either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of OCI along with a total for OCI, and a total amount for comprehensive income. The statement(s) are required to be presented with equal prominence as the other primary financial statements. ASU No. 2011-05 eliminates the option to present the components of OCI as part of the statement of changes in shareholders' equity but does not change the items that must be reported in OCI or when an item of OCI must be reclassified to net income. The provisions of ASU No. 2011-05 are effective for the Company's interim reporting period beginning on or after December 15, 2011, with retrospective application required. The adoption of ASU No. 2011-05 is expected to result in presentation changes to the Company's statements of income and the addition of a statement of comprehensive income. The adoption of ASU No. 2011-05 had no impact on the Company's balance sheets.

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". The amendments are being made to allow the FASB time to re-deliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and OCI for all periods presented. Entities should continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before ASU 2011-05. The adoption of ASU 2011-12 will have no impact on the Company's balance sheets.

Table of Contents

2. INVESTMENT SECURITIES

The amortized cost and estimated fair value of investment securities are as follows:

March 31, 2012	(in thousands)			
Available-for-sale securities	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Government agency: Notes	$2,497	$-	$(43)	$2,454
U.S. Government agency: MBS	166	10	-	176
U.S. Government agency: CMO	15,226	34	(14)	15,246
Total	$17,889	$44	$(57)	$17,876
Held-to-maturity securities				
U.S. Government agency: MBS	$14,270	$714	$(11)	$14,973
Total	$14,270	$714	$(11)	$14,973

December 31, 2011	(in thousands)			
Available-for-sale securities	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Government agency: Notes	$2,496	$-	$(10)	$2,486
U.S. Government agency: MBS	4,486	186	-	4,672
U.S. Government agency: CMO	16,368	66	(4)	16,430
Total	$23,350	$252	$(14)	$23,588
Held-to-maturity securities				
U.S. Government agency: MBS	$15,335	$732	$-	$16,067
Total	$15,335	$732	$-	$16,067

At March 31, 2012 and December 31, 2011, $32.1 million and $38.9 million of securities, respectively, at carrying value, was pledged to the Federal Home Loan Bank (FHLB), San Francisco, as collateral for current and future advances.

In the first quarter of 2012, the Company sold seven available-for-sale securities for a gain of $121,000. The cost basis of the securities sold was determined by specific identification.

The maturity periods and weighted average yields of investment securities at March 31, 2012 are as follows:

	Total Amount		Less than One Year		One to Five Years		Five to Ten Years	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
(dollars in thousands)								
Available-for-sale securities								
U. S. Government:								
Agency: Notes	$2,454	2.0%	$2,454	2.0%	$-	-	$-	-
Agency: MBS	176	2.5%	-	-	-	-	176	2.5%
Agency: CMO	15,246	0.9%	2,647	0.7%	12,599	0.9%	-	-
Total	$17,876	1.0%	$5,101	1.4%	$12,599	0.9%	$176	2.5%

Held-to-maturity securities												
U.S. Government:												
Agency: MBS	$14,270	3.7	%	$11	5.0	%	$2,245	5.4	%	$12,014	3.4	%
Total	$14,270	3.7	%	$11	5.0	%	$2,245	5.4	%	$12,014	3.4	%

14

Table of Contents

The following tables show all securities that are in an unrealized loss position and temporarily impaired as of:

March 31, 2012	Less than 12 months		More than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
			(in thousands)			
Available-for-sale securities						
U.S. Government agency: Notes	$2,454	$43	$-	$-	$2,454	$43
U.S. Government agency: CMO	6,390	11	1,541	3	7,931	14
Total	$8,844	$54	$1,541	$3	$10,385	$57
Held-to-maturity securities						
U.S. Government agency: MBS	$1,370	$11	$-	$-	$1,370	$11
Total	$1,370	$11	$-	$-	$1,370	$11

December 31, 2011	Less than 12 months		More than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
			(in thousands)			
Available-for-sale securities						
U.S. Government agency: Notes	$2,486	$10	$-	$-	$2,486	$10
U.S. Government agency: CMO	4,275	4	-	-	4,275	4
Total	$6,761	$14	$-	$-	$6,761	$14

As of March 31, 2012 and December 31, 2011, there were nine and five securities, respectively, in an unrealized loss position.

Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers, among other things (i) the length of time and the extent to which the fair value has been less than cost (ii) the financial condition and near-term prospects of the issuer and (iii) the Company's intent to sell an impaired security and if it is not more likely than not it will be required to sell the security before the recovery of its amortized basis.

The unrealized losses are primarily due to increases in market interest rates over the yields available at the time the underlying securities were purchased. The fair value is expected to recover as the bonds approach their maturity date or repricing date or if market yields for such investments decline. Management does not believe any of the securities are impaired due to reasons of credit quality, as all are direct or indirect agencies of the U. S. Government. Accordingly, as of March 31, 2012 and December 31, 2011, management believes the impairments detailed in the table above are temporary and no other-than-temporary impairment loss has been realized in the Company's consolidated income statements.

3. LOAN SALES AND SERVICING

SBA Loan Sales - The Company periodically sells the guaranteed portion of selected SBA loans into the secondary market, on a servicing-retained basis. The Company retains the unguaranteed portion of these loans and services the loans as required under the SBA programs to retain specified yield amounts. Historically, the Company has elected to use the amortizing method for the treatment of servicing assets and has measured for impairment on a quarterly basis through a discounted cash flow analysis prepared by an independent third party using industry prepayment speeds. As a result of the sale of $10.1 million in SBA loans during the first quarter of 2012, the Company recorded a servicing asset of $276,000 and has elected to measure this asset at fair value in accordance with ASC 825-10. The SBA program stipulates that the Company retains a minimum of 5% of the loan balance, which is unguaranteed. The percentage of each unguaranteed loan in excess of 5% may be periodically sold to a third party, typically for a cash premium. The Company records servicing liabilities for the unguaranteed loans sold calculated based on the present value of the estimated future servicing costs associated with each loan.

Table of Contents

The Company may also periodically sell certain SBA loans into the secondary market, on a servicing-released basis, typically for a cash premium.

As of March 31, 2012 and December 31, 2011, the Company had approximately $57.6 million and $74.1 million, respectively, in SBA loans included in loans held for sale. As of March 31, 2012 and December 31, 2011, the principal balance of loans serviced was $36.4 million and $27.6 million, respectively.

The following is a summary of activity for servicing rights accounted for under the amortization method:

	For the Three Months Ended March 31,	
	2012	2011
	(in thousands)	
Beginning balance	$ 625	$ 782
Additions through loan sales	-	-
Amortization	(28)	(29)
Ending balance	$ 597	$ 753

The following is a summary of activity for servicing rights accounted for under the fair value method:

	For the Three Months Ended March 31,	
	2012	2011
	(in thousands)	
Beginning balance	$ -	$ -
Additions through loan sales	276	-
Adjustment to fair value	-	-
Ending balance	$ 276	$ -

The key data and assumptions used in estimating the fair value of the Company's servicing rights as of March 31, 2012 were as follows:

	March 31, 2012
Weighted-Average Constant Prepayment Rate	1.5% to 16.9%*
Weighted-Average Life (in years)	23
Weighted-Average Discount Rate	8.0 %

* Prepayment rates varied between 1.5% to 16.9% for the pool of loans with an average weighted maturity greater than 21 years.

A sensitivity analysis of the Company's fair value of servicing rights to change in certain key assumptions as of March 31, 2012 is presented in the following table:

	March 31, 2012 (in thousands)
Discount Rate	
Increase in fair value from 100 bps decrease	$ 11
Decrease in fair value from 100 bps increase	(10)

Due to the range of prepayments speeds used in the valuation, a sensitivity analysis for changes in constant prepayment rate was not done at the time of this reporting.

This analysis generally cannot be extrapolated because the relationship of a change in one key assumption to the change in the fair value of the Company's servicing rights usually is not linear. Also, the effect of changing one key assumption without changing other assumptions is not realistic.

Table of Contents

Mortgage Loan Sales – The Company enters into mortgage loan rate lock commitments (normally for 30 days) with potential borrowers. In conjunction therewith, the Company enters into a forward sale commitment to sell the locked loan to a third party investor. This forward sale agreement requires delivery of the loan on a “best efforts” basis but does not obligate the Company to deliver if the mortgage loan does not fund.

The mortgage rate lock agreement and the forward sale agreement qualify as derivatives. The value of these derivatives is generally equal to the fee, if any, charged to the borrower at inception but may fluctuate in the event of changes in interest rates. Although the Company does not attempt to qualify these transactions for the special hedge accounting, management believes that changes in the fair value of the two commitments generally offset and create an economic hedge. At March 31, 2012 and December 31, 2011, the Company had $2.9 million and $8.0 million, respectively, in outstanding mortgage loan interest rate lock and forward sale commitments. The values of related derivative instruments were not material to the Company’s financial position or results of operations.

4. LOANS HELD FOR INVESTMENT

The composition of the Company’s loans held for investment loan portfolio follows:

	March 31, 2012	December 31, 2011
	(in thousands)	
Manufactured housing	$185,539	$ 189,331
Commercial real estate	164,437	168,812
Commercial	39,906	42,058
SBA	38,961	37,888
HELOC	20,527	20,719
Single family real estate	11,510	11,779
Consumer	362	312
	461,242	470,899
Less:		
Allowance for loan losses	14,705	15,270
Deferred costs	(100)	(101)
Purchased premiums	(7)	(8)
Discount on SBA loans	463	325
Loans held for investment, net	$446,181	$ 455,413

Table of Contents

At March 31, 2012, the aging of the Company's loans held for investment is as follows:

(in thousands)	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Current	Total Financing Receivables	Recorded Investment > 90 Days and Accruing
Manufactured housing	$732	$387	$685	$1,804	$183,735	$185,539	$-
Commercial real estate:							
Commercial real estate	-	2,812	4,569	7,381	98,675	106,056	247
504 1st TD	-	-	1,214	1,214	33,675	34,889	-
Land	-	-	-	-	5,136	5,136	-
Construction	-	-	1,519	1,519	16,837	18,356	-
Commercial	43	-	312	355	39,551	39,906	-
SBA	279	365	7,180	7,824	31,137	38,961	-
HELOC	-	-	74	74	20,453	20,527	74
Single family real estate	37	26	873	936	10,574	11,510	-
Consumer	-	-	-	-	362	362	-
Total	$1,091	$3,590	$16,426	$21,107	$440,135	$461,242	$321

Of the $7.8 million SBA loans past due, $7.7 million is guaranteed.

At December 31, 2011, the aging of the Company's loans held for investment is as follows:

(in thousands)	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Current	Total Financing Receivables	Recorded Investment > 90 Days and Accruing
Manufactured housing	$ 2,279	$ 519	$ 902	$ 3,700	$ 185,631	$ 189,331	$ -
Commercial real estate:							
Commercial real estate	247	-	3,718	3,965	104,260	108,225	-
504 1st TD	300	-	2,068	2,368	34,958	37,326	-
Land	-	-	-	-	5,230	5,230	-
Construction	-	-	1,519	1,519	16,512	18,031	-
Commercial	115	18	1,881	2,014	40,044	42,058	510
SBA	629	53	9,332	10,014	27,874	37,888	-
HELOC	258	-	75	333	20,386	20,719	74
	41	7	944	992	10,787	11,779	-

Single family real estate													
Consumer		-		-		-		-		312		312		-
Total	$	3,869	$	597	$	20,439	$	24,905	$	445,994	$	470,899	$	584

Of the $10.0 million SBA loans past due, $9.6 million is guaranteed.

Table of Contents

An analysis of the allowance for loan losses for loans held for investment follows:

	Three Months Ended March 31, 2012	2011
	(in thousands)	
Balance, beginning of period	$15,270	$13,302
Loans charged off	(2,958)	(1,194)
Recoveries on loans previously charged off	410	81
Net charge-offs	(2,548)	(1,113)
Provision for loan losses	1,983	983
Balance, end of period	$14,705	$13,172

As of March 31, 2012 and December 31, 2011, the Company also had established reserves for credit losses on undisbursed loans of $206,000 and $356,000 respectively, which are included in other liabilities in the consolidated balance sheets.

The following schedule summarizes the provision, charge-offs and recoveries by loan category for the three months ended March 31, 2012:

	Allowance 12/31/11	Provision	Charge-offs (in thousands)	Recoveries	Net Charge-offs	Allowance 3/31/12
Manufactured housing	$4,629	$1,205	$ (998)	$1	$ (997)	$4,837
Commercial real estate	3,528	162	(822)	-	(822)	2,868
Commercial	2,734	433	(629)	17	(612)	2,555
SBA	3,877	(261)	(379)	340	(39)	3,577
HELOC	349	312	(2)	50	48	709
Single family real estate	150	133	(128)	2	(126)	157
Consumer	3	(1)	-	-	-	2
Total	$15,270	$1,983	$ (2,958)	$410	$ (2,548)	$14,705

The following schedule summarizes the provision, charge-offs and recoveries by loan category for the three months ended March 31, 2011:

	Allowance 12/31/10	Provision	Charge-offs (in thousands)	Recoveries	Net Charge-offs	Allowance 3/31/11
Manufactured housing	$4,168	$368	$ (281)	$25	$ (256)	$4,280
Commercial real estate	2,532	315	(18)	2	(16)	2,831
Commercial	2,094	98	(322)	10	(312)	1,880
SBA	3,753	(48)	(423)	42	(381)	3,324
HELOC	547	36	-	1	1	584
Single family real estate	135	192	(150)	1	(149)	178
Consumer	73	22	-	-	-	95

Total	$13,302	$983	$ (1,194)	$81	$ (1,113)	$13,172

Table of Contents

The following schedule summarizes by loan category the recorded investment in loans held for investment collectively and individually evaluated for impairment and the related allowance for loan losses as of March 31, 2012:

	Loans Collectively Evaluated	Allowance For Loan Losses	Loans Individually Evaluated (in thousands)	Allowance For loan Losses	Total Loans Held for Investment	Total Allowance for Loan Losses
Manufactured housing	$ 176,086	$ 4,807	$ 9,453	$ 30	$ 185,539	$ 4,837
Commercial real estate	118,560	2,868	45,877	-	164,437	2,868
Commercial	33,916	2,555	5,990	-	39,906	2,555
SBA	36,906	3,577	2,055	-	38,961	3,577
HELOC	20,527	709	-	-	20,527	709
Single family real estate	10,580	156	930	1	11,510	157
Consumer	350	2	12	-	362	2
Total	$ 396,925	$ 14,674	$ 64,317	$ 31	$ 461,242	$ 14,705

The following schedule summarizes by loan category the recorded investment in loans held for investment collectively and individually evaluated for impairment and the related allowance for loan losses as of December 31, 2011:

	Loans Collectively Evaluated	Allowance For Loan Losses	Loans Individually Evaluated (in thousands)	Allowance For loan Losses	Total Loans Held for Investment	Total Allowance for Loan Losses
Manufactured housing	$ 188,942	$ 4,629	$ 389	$ -	$ 189,331	$ 4,629
Commercial real estate	137,243	3,322	31,569	206	168,812	3,528
Commercial	36,029	2,734	6,029	-	42,058	2,734
SBA	35,981	3,835	1,907	42	37,888	3,877
HELOC	20,719	349	-	-	20,719	349
Single family real estate	11,779	150	-	-	11,779	150
Consumer	301	3	11	-	312	3
Total	$ 430,994	$ 15,022	$ 39,905	$ 248	$ 470,899	$ 15,270

The following schedule summarizes impaired loans by loan class as of March 31, 2012:

	Without Specific Valuation Allowance	With Specific Valuation Allowance	Valuation Allowance (in thousands)	Impaired Loan, net
Manufactured housing	$ 6,266	$ 3,187	$ 30	$ 9,423
Commercial real estate:				
Commercial real estate	25,616	-	-	25,616
SBA 504 1st	7,119	-	-	7,119
Construction	13,142	-	-	13,142

Commercial	5,855	135	-	5,990
SBA	1,907	148	-	2,055
Single family real estate	850	80	1	929
Consumer	12	-	-	12
Total	$60,767	$ 3,550	$31	$ 64,286

Table of Contents

The following schedule summarizes impaired loans by loan class as of December 31, 2011:

	Without Specific Valuation Allowance	With Specific Valuation Allowance	Valuation Allowance	Impaired Loan, net
		(in thousands)		
Manufactured housing	$390	$ -	$-	$ 390
Commercial real estate:				
Commercial real estate	11,523	8,135	206	19,452
SBA 504 1st	7,164	-	-	7,164
Construction	4,746	-	-	4,746
Commercial	6,029	-	-	6,029
SBA	1,815	91	42	1,864
Consumer	11	-	-	11
Total	$31,678	$ 8,226	$248	$ 39,656

The following schedule summarizes the average investment in impaired loans by loan class and the interest income recognized:

	Three Months Ended March 31, 2012		Three Months Ended March 31, 2011	
	Average Investment in Impaired Loans	Interest Income Recognized	Average Investment in Impaired Loans	Interest Income Recognized
		(in thousands)		
Manufactured housing	$4,559	$ 46	$ -	$ -
Commercial real estate:				
Commercial real estate	20,971	193	11,107	92
SBA 504 1st	6,615	95	1,806	
Land	-	-	1,196	7
Construction	8,286	108	4,704	
Commercial	5,567	87	3,496	81
SBA	1,835	34	3,809	
Single family real estate	431	1	-	
Consumer	11	-	21	
Total	$48,275	$ 564	$ 26,139	$ 180

The following schedule reflects recorded investment at the dates indicated in certain types of loans:

	March 31, 2012	December 31, 2011
	(dollars in thousands)	
Nonaccrual loans	$50,529	$ 42,343
SBA guaranteed portion of loans included above	(12,239)	(13,673)
Nonaccrual loans, net	$38,290	$ 28,670

Troubled debt restructured loans, gross	$22,847		$ 17,885	
Loans 30 through 89 days past due with interest accruing	$140		$ 3,114	
Allowance for loan losses to gross loans held for investment	3.19	%	3.24	%

CWB generally repurchases the guaranteed portion of SBA loans from investors when those loans become past due 120 days. After the foreclosure and collection process is complete, the SBA reimburses CWB for this principal balance. Although these balances do not earn interest during this period, they generally do not result in a loss of principal to CWB; therefore a repurchase reserve has not been established related to these loans.

Table of Contents

The composition of the Company's net nonaccrual loans is as follows:

	March 31, 2012	December 31, 2011
	(in thousands)	
Manufactured housing	$11,211	$ 3,397
Commercial real estate:		
Commercial real estate	16,818	12,716
504 1st	2,005	3,148
Construction	4,727	4,746
Commercial	1,180	2,031
SBA	1,388	1,659
HELOC	28	29
Single family real estate	930	944
Consumer	3	-
Nonaccrual loans, net	$38,290	$ 28,670

At March 31, 2012, the recorded investment in loans by rating is as follows:

	Pass	Special Mention	Substandard	Doubtful	Total
(in thousands)					
Manufactured housing	$172,336	$ -	$13,203	$-	$185,539
Commercial real estate:					-
Commercial real estate	67,024	8,661	30,372	-	106,057
SBA 504 1st	27,424	345	7,119	-	34,888
Land	3,913	300	923	-	5,136
Construction	5,214	-	13,142	-	18,356
Commercial	29,160	3,271	7,146	329	39,906
SBA	17,172	400	1,326	19	18,917
HELOC	9,580	6,572	4,375	-	20,527
Single family real estate	10,462	-	1,048	-	11,510
Consumer	350	-	9	3	362
Total non-guaranteed	$342,635	$ 19,549	$78,663	$351	$441,198
SBA guarantee	-		13,097	6,947	20,044
Total	$342,635	$ 19,549	$91,760	$7,298	$461,242

At December 31, 2011, the recorded investment in loans by rating is as follows:

	Pass	Special Mention	Substandard	Doubtful	Total
(in thousands)					
Manufactured housing	$183,893	$ -	$5,438	$-	$189,331
Commercial real estate:					
Commercial real estate	74,083	11,273	22,869	-	108,225
SBA 504 1st	28,699	349	8,278	-	37,326
Land	3,932	1,298	-	-	5,230
Construction	4,868	-	9,935	3,228	18,031
Commercial	29,360	3,578	7,756	1,364	42,058

SBA	19,510	397	2,470	34	22,411
HELOC	15,068	4,614	1,037	-	20,719
Single family real estate	10,718	-	1,061	-	11,779
Consumer	298	-	11	3	312
Total non-guaranteed	$370,429	$ 21,509	$ 58,855	$4,629	$455,422
SBA guarantee	-	-	8,541	6,936	15,477
Total	$370,429	$ 21,509	$ 67,396	$11,565	$470,899

Table of Contents

The following table reflects troubled debt restructurings (TDR) that occurred in the three months ended March 31, 2012:

	Book Balance (thousands)	Effect on Allowance for Loan Loss (thousands)	Book Balance of Loans with Rate Reduction (thousands)	Average Rate Reduction (bps)	Book Balance of Loans with Term Extension (thousands)	Average Extension (months)
Manufactured Housing	$519	$ -	$442	420	$519	248
RE Commercial	2,709	-	2,709	350	2,709	120
Construction	3,208	-	3,208	300	3,208	15
Commercial	819	8	561	350	259	21
SBA	410	14	-	-	410	65
Consumer	9	-	-	-	9	6
Total	$7,674	$ 22	$6,920	383	$7,114	136

A loan is considered a TDR when concessions have been made to the borrower and the borrower is in financial difficulty. These concessions include but are not limited to term extensions, rate reductions and principal reductions. Forgiveness of principal is rarely granted and modifications for all classes of loans are predominantly term extensions. TDR loans are also considered impaired. A loan is considered impaired when, based on current information, it is probable that the Company will be unable to collect the scheduled payments of principal and/or interest under the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and/or interest payments. Loans that experience insignificant payment delays or payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays or payment shortfalls on a case-by-case basis. When determining the possibility of impairment, management considers the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. For collateral-dependent loans, the Company uses the fair value of collateral method to measure impairment. All other loans are measured for impairment based on the present value of future cash flows. Impairment is measured on a loan-by-loan basis for all loans in the portfolio.

One restructured loan, a SBA 504 1st, experienced default during the first quarter of 2012. The loan was transferred to foreclosed real estate and repossessed assets and is currently in escrow.

5. FAIR VALUE MEASUREMENT

Fair value is the exchange price that would be received for an asset or the price that would be paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. U. S. GAAP establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Three levels of inputs may be used to measure fair value:

Level 1 – Inputs to the valuation methodology are quoted prices, unadjusted, for identical assets or liabilities in active markets. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available. A contractually binding sales price also provides reliable evidence of fair value.

23

Table of Contents

Level 2 – Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; inputs to the valuation methodology include quoted prices for identical or similar assets or liabilities in markets that are not active; or inputs to the valuation methodology that utilize model-based techniques for which all significant assumptions are observable in the market.

Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement; inputs to the valuation methodology that utilize model-based techniques for which significant assumptions are not observable in the market; or inputs to the valuation methodology that requires significant management judgment or estimation, some of which may be internally developed.

The following summarizes the fair value measurements of assets measured on a recurring basis as of March 31, 2012 and December 31, 2011 and the relative levels of inputs from which such amounts were derived:

		Fair value measurements at March 31, 2012 using		
Description	Total	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
		(in thousands)		
Investment securities available-for-sale	$17,876	$ -	$ 17,876	$ -
Interest only strips (included in other assets)	483			483
Servicing asset (included in other assets)	276	-	-	276
Total	$18,635	$ -	$ 17,876	$ 759

		Fair value measurements at December 31, 2011 using		
Description	Total	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
		(in thousands)		
Investment securities available-for-sale	$23,588	$ -	$ 23,588	$ -
Interest only strips (included in other assets)	419	-	-	419
Total	$24,007	$ -	$ 23,588	$ 419

Market valuations of our investment securities which are classified as level 2 are provided by an independent third party. The fair values are determined by using several sources for valuing fixed income securities. Their techniques include pricing models that vary based on the type of asset being valued and incorporate available trade, bid and other market information. In accordance with the fair value hierarchy, the market valuation sources include observable market inputs and are therefore considered Level 2 inputs for purposes of determining the fair values.

On certain SBA loan sales that occurred prior to 2003, the Company retained interest only strips ("I/O strips"), which represent the present value of excess net cash flows generated by the difference between (a) interest at the stated rate paid by borrowers and (b) the sum of (i) pass-through interest paid to third-party investors and (ii) contractual servicing fees. I/O strips are classified as level 3 in the fair value hierarchy. The fair value is determined on a quarterly basis through a discounted cash flow analysis prepared by an independent third party using industry prepayment speeds. The I/O strips were valued at $419,000 as of December 31, 2011 and a valuation adjustment of $64,000 was recorded in income during the first three months of 2012. No other changes in the balance have occurred related to the I/O strips and such valuation adjustments are included as additions or offsets to loan servicing income.

Table of Contents

Historically, the Company has elected to use the amortizing method for the treatment of servicing assets and has measured for impairment on a quarterly basis through a discounted cash flow analysis prepared by an independent third party using industry prepayment speeds. As a result of the sale of $10.1 million in SBA loans during the first quarter of 2012, the Company recorded a servicing asset of $276,000 and has elected to measure this asset at fair value in accordance with ASC 825-10. Significant assumptions in the valuation of servicing rights include estimated loan repayment rates, the discount rate, and servicing costs, among others. Servicing rights are classified as Level 3 measurements due to the use of significant unobservable inputs, as well as significant management judgment and estimation.

The Company also has assets that under certain conditions are subject to measurement at fair value on a non-recurring basis. These assets include loans held for sale, foreclosed real estate and repossessed assets and loans that are considered impaired per generally accepted accounting principles.

Loans held for sale are carried at the lower of cost or market. The fair value of loans held for sale is based on what secondary markets are currently offering for portfolios with similar characteristics or based on the agreed upon sale price. As such, the Company classifies the fair value of loans held for sale as a non-recurring valuation within Level 2 of the fair value hierarchy. At March 31, 2012 and December 31, 2011, the Company had loans held for sale with an aggregate carrying value of $58.5 million and $77.3 million respectively.

Foreclosed real estate and repossessed assets are carried at the lower of book value or fair value less estimated cost to sell. Fair value is based upon independent market prices obtained from certified appraisers or the current listing price, if lower. When the fair value of the collateral is based on a current appraised value, the Company reports the fair value of the foreclosed collateral as non-recurring Level 2. When a current appraised value is not available or if management determines the fair value of the collateral is further impaired, the Company reports the foreclosed collateral as non-recurring Level 3.

The Company records certain loans at fair value on a non-recurring basis. When a loan is considered impaired, an allowance for a loan loss is established. The fair value measurement and disclosure requirement applies to loans measured for impairment using the practical expedients method permitted by accounting guidance for impaired loans. Impaired loans are measured at an observable market price, if available or at the fair value of the loans collateral, if the loan is collateral dependent. The fair value of the loan’s collateral is determined by appraisals or independent valuation. When the fair value of the loan’s collateral is based on an observable market price or current appraised value, given the current real estate markets, the appraisals may contain a wide range of values and accordingly, the Company classifies the fair value of the impaired loans as a non-recurring valuation within Level 2 of the valuation hierarchy. For loans in which impairment is determined based on the net present value of cash flows, the Company classifies these as a non-recurring valuation within Level 3 of the valuation hierarchy.

The following summarizes the fair value measurements of assets measured on a non-recurring basis as of March 31, 2012 and December 31, 2011 and the relative levels of inputs from which such amounts were derived:

		Fair value measurements at March 31, 2012 using		
Description	Total	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
		(in thousands)		
Impaired loans	$64,286	$ -	$ 39,650	$ 24,636

Loans held for sale	61,923	-	61,923	-
Foreclosed real estate and repossessed assets	5,776	-	5,776	-
Total	$131,985	$ -	$ 107,349	$ 24,636

Table of Contents

Description	Total	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
	Fair value measurements at December 31, 2011 using			
	(in thousands)			
Impaired loans	$39,656	$ -	$ 23,490	$ 16,166
Loans held for sale	79,545	-	79,545	-
Foreclosed real estate and repossessed assets	6,701	-	6,701	-
Total	$125,902	$ -	$ 109,736	$ 16,166

6. BORROWINGS

Federal Home Loan Bank Advances – CWB has a blanket lien credit line with the Federal Home Loan Bank (FHLB). Advances are collateralized in the aggregate by CWB's eligible loans and securities. Total FHLB advances were $51.0 million and $61.0 million at March 31, 2012 and December 31, 2011, respectively, borrowed at fixed rates. In March and April 2012, the Bank prepaid $5.0 million and $17.0 million, respectively, of FHLB advances.. At March 31, 2012, CWB had securities and loans pledged to the FHLB with a carrying value of $32.1 million and $61.4 million, respectively. At December 31, 2011, CWB had securities and loans pledged with a carrying value of $38.9 million and $58.2 million, respectively. Total FHLB interest expense for the three months ended March 31, 2012 and 2011 was $352,000 and $416,000, respectively. At March 31, 2012, CWB had $67.0 million available for additional borrowing.

Federal Reserve Bank – CWB has established a credit line with the Federal Reserve Bank ("FRB"). Advances are collateralized in the aggregate by eligible loans for up to 28 days. There were no outstanding FRB advances as of March 31, 2012 and December 31, 2011. CWB had $78.8 million in borrowing capacity as of March 31, 2012.

Convertible Debentures - On August 9, 2010, the Company completed an offering of $8,085,000 convertible subordinated debentures. The debentures are a general unsecured obligation and are subordinated in right of payment to all present and future senior indebtedness. The debentures pay interest at 9% until conversion, redemption or maturity and will mature on August 9, 2020. The debentures may be redeemed by the Company after January 1, 2014. Prior to maturity or redemption, the debentures can be converted into common stock at the election of the holder at $3.50 per share if converted on or prior to July 1, 2013, $4.50 per share between July 2, 2013 and July 1, 2016 and $6.00 per share from July 2, 2016 until maturity or redemption. At March 31, 2012 and December 31, 2011, the balance of the convertible debentures was $7,852,000.

7. STOCKHOLDERS' EQUITY

Preferred Stock

On December 19, 2008, as part of the United States Department of the Treasury's ("Treasury") Troubled Asset Relief Program - Capital Purchase Program ("TARP Program"), the Company entered into a Letter Agreement with the Treasury, pursuant to which the Company issued to the Treasury, in exchange for an aggregate purchase price of $15.6 million in cash: (i) 15,600 shares of the Company's Fixed Rate Cumulative Perpetual Preferred Stock, Series A, no par value, having a liquidation preference of $1,000 per share (the "Series A Preferred Stock"), and (ii) a warrant (the "Warrant") to purchase up to 521,158 shares of the Company's common stock, no par value ("Common Stock"), at an exercise price of $4.49 per share.

Series A Preferred Stock pays cumulative dividends at a rate of 5% per year for the first five years and at a rate of 9% per year thereafter, but will be paid only if, as and when declared by the Company's Board of Directors. The Series A Preferred Stock has no maturity date and ranks senior to the Common Stock with respect to the payment of dividends and distributions and amounts payable upon liquidation, dissolution and winding up of the Company. The Series A Preferred Stock is generally non-voting, other than class voting on certain matters that could adversely affect the Series A Preferred Stock. In the event that dividends payable on the Series A Preferred Stock have not been paid for the equivalent of six or more quarters, whether or not consecutive, the Company's authorized number of Directors will be automatically increased by two and the holders of the Series A Preferred Stock, voting together with holders of any then outstanding voting parity stock, will have the right to elect those Directors at the Company's next annual meeting of shareholders or at a special meeting of shareholders called for that purpose. These Directors will be elected annually and will serve until all accrued and unpaid dividends on the Series A Preferred Stock have been paid. Notwithstanding the terms of the Series A Preferred Stock, the Treasury has issued guidance that permits institutions that participated in the TARP Program, such as the Company, to redeem the Series A Preferred Stock and to repurchase the warrants issued to the Treasury subject to prior consultation with the institutions primary federal banking regulator.

Table of Contents

Common Stock Warrant

The Warrant issued as part of the TARP provide for the purchase of up to 521,158 shares of the common stock, at an exercise price of $4.49 per share ("Warrant Shares"). The Warrant is immediately exercisable and has a 10-year term. The exercise price and the ultimate number of shares of common stock that may be issued under the Warrant are subject to certain anti-dilution adjustments, such as upon stock splits or distributions of securities or other assets to holders of the common stock, and upon certain issuances of the common stock at or below a specified price relative to the then current market price of the common stock. Pursuant to the Securities Purchase Agreement, the Treasury has agreed not to exercise voting power with respect to any Warrant Shares.

8. EARNINGS PER SHARE

The following table presents a reconciliation of basic earnings per share and diluted earnings per share:

	Three Months Ended March 31,	
	2012	2011
	(dollars in thousands, except per share data)	
Net income	$ 819	$ 595
Less: Preferred stock dividends	262	262
Net income applicable to common stockholders	$ 557	$ 333
Add: Debenture interest expense and costs, net of income taxes	107	111
Net income for diluted calculation of earnings per common share	$ 664	$ 444
Basic weighted average number of common shares outstanding	5,990	5,960
Dilutive weighted average number of common shares outstanding	8,233	8,245
Earnings per common share:		
Basic	$ 0.09	$ 0.06
Diluted	$ 0.08	$ 0.05

9. FAIR VALUES OF FINANCIAL INSTRUMENTS

The estimated fair values of financial instruments have been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is required to interpret market data to develop estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

Table of Contents

The following table represents the estimated fair values:

	March 31, 2012		December 31, 2011	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in thousands)			
Assets:				
Cash and cash equivalents	$43,145	$43,145	$22,572	$22,572
Time and interest bearing deposits in other financial institutions	5,403	5,403	347	347
Federal Reserve and Federal Home Loan Bank stock	5,356	5,356	5,557	5,557
Investment securities	32,146	32,849	38,923	39,655
Loans	504,641	484,403	532,716	512,524
Liabilities:				
Deposits (other than time deposits)	366,094	366,094	359,119	359,119
Time deposits	144,705	147,212	152,143	154,484
Other borrowings	58,852	60,396	68,852	70,975

The methods and assumptions used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value are explained below:

Cash and cash equivalents - The carrying amounts approximate fair value because of the short-term nature of these instruments.

Time deposits in other financial institutions - The carrying amounts approximate fair value because of the relative short-term nature of these instruments.

Federal Reserve Stock - The carrying value approximates the fair value because the stock can be sold back to the Federal Reserve at any time at par.

Federal Home Loan Bank Stock - The carrying value approximates the fair value.

Investment securities – Market valuations of our investment securities are provided by an independent third party. The fair values are determined by using several sources for valuing fixed income securities. Their techniques include pricing models that vary based on the type of asset being valued and incorporate available trade, bid and other market information. In accordance with the fair value hierarchy, the market valuation sources include observable market inputs and are therefore considered Level 2 inputs for purposes of determining the fair values.

Loans – For most loan categories, the fair value is estimated using discounted cash flows utilizing an appropriate discount rate and historical prepayment speeds. For certain adjustable loans that reprice on a frequent basis carrying value approximates fair value. In accordance with the fair value hierarchy, the market valuation sources include observable market inputs and are therefore considered Level 2 inputs for purposes of determining the fair values.

Deposits – The amount payable at demand at report date is used to estimate the fair value of demand and savings deposits. The estimated fair values of fixed-rate time deposits are determined by discounting the cash flows of segments of deposits that have similar maturities and rates, utilizing a discount rate that approximates the prevailing rates offered to depositors as of the measurement date. In accordance with the fair value hierarchy, the market valuation for time deposit include observable market inputs and are therefore considered Level 2 inputs for purposes of determining the fair values.

Other borrowings – The fair value is estimated using a discounted cash flow analysis based on rates for similar types of borrowing arrangements. The carrying value of FRB advances approximates the fair value due to the short term nature of these borrowings. In accordance with the fair value hierarchy, the market valuation for other borrowings include observable market inputs and are therefore considered Level 2 inputs for purposes of determining the fair values.

Commitments to Extend Credit, Commercial and Standby Letters of Credit – Due to the proximity of the pricing of these commitments to the period end, the fair values of commitments are immaterial to the financial statements.

The fair value estimates presented herein are based on pertinent information available to management as of March 31, 2012 and December 31, 2011. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since those dates and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

Table of Contents

ITEM 2.MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION ANDRESULTS OF OPERATIONS

This discussion is designed to provide insight into management's assessment of significant trends related to the Company's consolidated financial condition, results of operations, liquidity, capital resources and interest rate sensitivity. It should be read in conjunction with the Company's unaudited interim consolidated financial statements and notes thereto the audited consolidated financial statement and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011, and the other financial information appearing elsewhere in this report.

The following discussion should be read in conjunction with the Company's financial statements and the related notes provided under "Item 1—Financial Statements" above.

Overview of Earnings Performance

For the 1Q12, net income was $819,000 compared to net income of $595,000 for 1Q11.

The significant factors impacting net income for 1Q12 were:

- Sale of $10.1 million in SBA loans resulting in a gain of $973,000 in 1Q12. There were no SBA loan sales in 1Q11.

- Provision for loan losses of $2.0 million for 1Q12 compared to $1.0 million for 1Q11 as net charge-offs increased to $2.5 million for 1Q12 from $1.1 million for 1Q11.

- A decline in interest income of $1.0 million resulting from a combination of lower average earning assets, $586.4 million for 1Q12 compared to $633.2 million for 1Q11 and lower yields on earning assets of 5.71% for 1Q12 compared to 5.98% for 1Q11.

- Margin declined for 1Q12 to 4.48% compared to 4.53% for 1Q11. The decline in rates paid on funding sources from 1.64% for 1Q11 to 1.37% for 1Q12 partially offset the lower yields on interest earning assets.

- Closed remaining (CO, OR, UT and WA) out-of-state SBA lending operations in February 2012.

- Sold $4 million of investment securities at a net gain of $121,000.

Recent Regulatory Actions

Office of the Comptroller of the Currency

As previously announced, the Board of Directors of the Bank signed an Agreement (OCC Agreement) with the Office of the Comptroller of the Currency (OCC), its primary regulator, on January 26, 2012. The Agreement includes, among other things, the following requirements:

- Achieving and maintaining a Tier 1 Leverage Capital ratio of 9.00% and Total Risk-Based Capital ratio of 12.00%;

- Writing a 3-year strategic plan, which would incorporate the capital component;

-

Continue to improve on the Bank's credit quality and administration thereof, including the monitoring of problem assets and the allowance for loan losses;

- Continue to adhere to and implement the Bank's liquidity risk management program.

Federal Reserve Bank of San Francisco

On April 23, 2012, the Company entered into a written agreement, (FRB Agreement) with the Federal Reserve Bank of San Francisco. Without admitting or denying any of the alleged charges of unsafe or unsound banking practices and any violations of law, the Company has agreed to take the following corrective actions to address certain alleged violations of law and/or regulation:

Table of Contents

- Take appropriate steps to fully utilize the Company's financial and managerial resources to serve as a source of strength to the Bank, including taking steps to ensure the Bank's compliance with the OCC Agreement issued to it by the Comptroller of the Currency, effective as of January 26, 2012, and any other supervisory action taken by the Bank's federal and state regulators;
- Refrain from declaring or paying dividends absent prior regulatory approval;
- Refrain from taking dividends or any form of payment from the Bank representing a reduction in the Bank's capital absent prior regulatory approval;
- Refrain from incurring, increasing or guaranteeing any debt or repurchasing or redeeming any shares of its stock absent prior regulatory approval;
- Develop and submit for regulatory approval a written capital plan to maintain sufficient capital on a consolidated basis, which capital plan should, at a minimum, address, consider and include current and future capital requirements on a consolidated basis and compliance with federal regulations and guideline; the adequacy of the Bank's capital, the sources and timing of funds necessary to fulfill future capital requirements; and the requirements of federal law that the Company serve as a source of strength to the Bank;
- Develop and submit for regulatory approval a cash flow projection of the Company's planned sources and uses of cash for debt service, operating expenses and other purposes;
- Comply with appropriate regulatory notice and approval requirements when appointing any new directors or senior executive officers or changing the responsibilities of any senior executive officer and comply with the limitations on indemnification and severance payments set forth in Section 18(k) of the Federal Deposit Insurance Act (12 USC 1828(i)) and Part 359 of the FDIC's implementing regulations; and
- Furnish written progress reports to the FRB detailing the form and manner of any actions taken to secure compliance with the Regulatory Agreement.

In accordance with the FRB Agreement, the Company requested the Reserve Bank's approval to pay the dividend due on May 15, 2012, on the Company's Fixed Rate Cumulative Perpetual Preferred Stock, Series A, no par value having a liquidation preference of $1,000 per share (Preferred Shares). That request was denied. Consequently, the Company will not pay that dividend. As indicated in the FRB Agreement, all future dividends are subject to regulatory approval.

Since the appointment of a new Chief Executive Officer and Chief Credit Officer, the Bank has maintained an intense focus on addressing the areas of concern that have been raised by the regulators. As a result, many of the prudent actions required in the Agreements have been addressed, or will be addressed in the near future.

The Bank completed the following actions within the last 90 days to streamline the balance sheet and enhance its capital position:

- Closed remaining (CO, OR, UT and WA) out-of-state SBA lending operations in February 2012.
- Sold $10.1 million of guaranteed SBA loans in March 2012, generating a net gain of $973,000.
- Prepaid $5 million of FHLB advances in March 2012 and another $17 million in April 2012.
- Sold $4 million of investment securities at a net gain of $121,000.
- As of April 30, 2012, achieved Tier 1 capital ratio of 9.06% and total risk-based capital ratio of 12.44%.

The Board and Management will continue to work closely with the OCC and FRB to achieve compliance with the terms of the Agreements and to improve the Company's and Bank's strength, security and performance.

Critical Accounting Policies

A number of critical accounting policies are used in the preparation of the Company's consolidated financial statements. These policies relate to areas of the financial statements that involve estimates and judgments made by management. These include provision and allowance for loan losses and servicing rights. These critical accounting policies are discussed in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2011 with a description of how the estimates are determined and an indication of the consequences of an over or under estimate.

Table of Contents

Results of Operations - First Quarter Comparison

The following table sets forth for the periods indicated, certain items in the consolidated statements of income of the Company and the related changes between those periods:

	Three Months Ended March 31, 2012	2011	Increase (Decrease)
	(dollars in thousands, except per share amounts)		
Interest income	$ 8,321	$ 9,330	$ (1,009)
Interest expense	1,793	2,261	(468)
Net interest income	6,528	7,069	(541)
Provision for loan losses	1,983	983	1,000
Net interest income after provision for loan losses	4,545	6,086	(1,541)
Non-interest income	1,888	738	1,150
Non-interest expenses	5,614	5,809	(195)
Income before provision for income taxes	819	1,015	(196)
Provision for income taxes	-	420	(420)
Net income	$ 819	$ 595	$ 224
Preferred stock dividends	262	262	-
Net income applicable to common shareholders	$ 557	$ 333	$ 224
Earnings per common share:			
Basic	$ 0.09	$ 0.06	$ 0.03
Diluted	$ 0.08	$ 0.05	$ 0.03
Dividends per common share	$ -	$ -	$ -
Comprehensive income (loss)	$ 671	$ 560	$ 111

The following table sets forth the changes in interest income and expense attributable to changes in rate and volume:

	Total change	Three Months Ended March 31, 2012 versus 2011 Changes due to Rate	Volume
	(in thousands)		
Loans, net	$ (962)	$ (223)	$ (739)
Investment securities and other	(47)	(36)	(11)
Total interest-earning assets	(1,009)	(259)	(750)
Deposits	(405)	(280)	(125)
Other borrowings	(63)	(17)	(46)
Total interest-bearing liabilities	(468)	(297)	(171)
Net interest income	$ (541)	$ 38	$ (579)

Net Interest Income

Net interest income declined by $541,000 for 1Q12 compared to 1Q11. Total interest income declined by $1.0 million. Of this decline, $750,000 was due to the decline in average earning assets from $633.2 million for 1Q11 to $586.4 million for 1Q12. The yield on interest earning assets also declined from 5.98% for 1Q11 to 5.71% for 1Q12.

The decline in interest expense of $468,000 resulted from both lower rates paid on interest bearing liabilities, 1.37% for 1Q12 compared to 1.64% for 1Q11, and a decline in the average balance of interest-bearing liabilities from $560.4 million for 1Q11 to $527.5 million for 1Q12. The net impact of the decline in yields on interest earning assets and the decline in rates on interest-bearing liabilities was a decline in the margin from 4.53% for 1Q11 to 4.48% for 1Q12.

Table of Contents

Provision for Loan Losses

The provision for loan losses was $2.0 million for 1Q12 compared to $1.0 million for 1Q11. Net charge-offs increased to $2.5 million for 1Q12 compared to $1.1 million for 1Q11.

The following schedule summarizes the provision, charge-offs and recoveries by loan category for the three months ended March 31, 2012:

	Allowance 12/31/11	Provision	Charge-offs (in thousands)	Recoveries	Net Charge-offs	Allowance 3/31/12
Manufactured housing	$4,629	$1,205	$ (998)	$1	$ (997)	$4,837
Commercial real estate	3,528	162	(822)	-	(822)	2,868
Commercial	2,734	433	(629)	17	(612)	2,555
SBA	3,877	(261)	(379)	340	(39)	3,577
HELOC	349	312	(2)	50	48	709
Single family real estate	150	133	(128)	2	(126)	157
Consumer	3	(1)	-	-	-	2
Total	$15,270	$1,983	$ (2,958)	$410	$ (2,548)	$14,705

The following schedule summarizes the provision, charge-offs and recoveries by loan category for the three months ended March 31, 2011:

	Allowance 12/31/10	Provision	Charge-offs (in thousands)	Recoveries	Net Charge-offs	Allowance 3/31/11
Manufactured housing	$4,168	$368	$ (281)	$25	$ (256)	$4,280
Commercial real estate	2,532	315	(18)	2	(16)	2,831
Commercial	2,094	98	(322)	10	(312)	1,880
SBA	3,753	(48)	(423)	42	(381)	3,324
HELOC	547	36	-	1	1	584
Single family real estate	135	192	(150)	1	(149)	178
Consumer	73	22	-	-	-	95
Total	$13,302	$983	$ (1,194)	$81	$ (1,113)	$13,172

Included in the Company’s held-to-maturity portfolio are home equity loans, “HELOC”, which guidance issued by the SEC characterizes as higher-risk. The HELOC portfolio of $20.5 million consists of credits secured by residential real estate in Santa Barbara and Ventura counties. In 1Q12, there were $48,000 in charge-offs in this portfolio. As of March 31, 2012, $74,000 was past due in this portfolio. The allowance for loan losses for this portfolio is $709,000, or 3.5%. The Company monitors this portfolio to insure adequate support of the real estate collateral.

The percentage of net nonaccrual loans to the total loan portfolio has increased to 7.4% as of March 31, 2012 from 5.2% at December 31, 2011.

The allowance for loan losses compared to net nonaccrual loans has declined to 38.4% as of March 31, 2012 from 53.3% as of December 31, 2011.

Non-Interest Income

Non-interest income includes gains from sale of loans, loan document fees, service charges on deposit accounts, loan servicing fees and other revenues not derived from interest on earning assets. Total non-interest income increased by $1.2 million, or 155.8%, for 1Q12 compared to 1Q11, due to the sale of $10.1 million in SBA loans with the resulting gain of $973,000 and the sale of $4.0 million of investment securities resulting in a gain of $121,000.

Table of Contents

Non-Interest Expenses
The decline in non-interest expenses of $195,000, or 3.4%, for 1Q12 compared to 1Q11 resulted from reductions in several areas including salaries and employee benefits which was $2.9 million for 1Q12 compared to $3.1 million for 1Q11. Partially offsetting the declines in expense was an increase of $124,000 in the FDIC assessment.

Interest Rates and Differentials
The following table illustrates average yields on interest-earning assets and average rates on interest-bearing liabilities for the periods indicated:

	Three Months Ended March 31,			
	2012		2011	
Interest-earning assets:	(dollars in thousands)			
Federal funds sold and interest-earning deposits:				
Average balance	$3,039		$1,252	
Interest income	2		3	
Average yield	0.25	%	0.88	%
Investment securities:				
Average balance	$42,597		$44,758	
Interest income	237		283	
Average yield	2.23	%	2.56	%
Gross loans:				
Average balance (includes non-accrual loans)	$540,763		$587,193	
Interest income	8,082		9,044	
Average yield	6.01	%	6.25	%
Total interest-earning assets:				
Average balance	$586,399		$633,203	
Interest income	8,321		9,330	
Average yield	5.71	%	5.98	%
Interest-bearing liabilities:				
Interest-bearing demand deposits:				
Average balance	$290,484		$274,485	
Interest expense	627		800	
Average cost of funds	0.87	%	1.18	%
Savings deposits:				
Average balance	$19,398		$20,743	
Interest expense	83		108	
Average cost of funds	1.71	%	2.12	%
Time certificates of deposit:				
Average balance	$151,454		$193,229	
Interest expense	555			