Farmers & Merchants Bank®

Together, we're keeping our communities healthy.

2012 ANNUAL REPORT

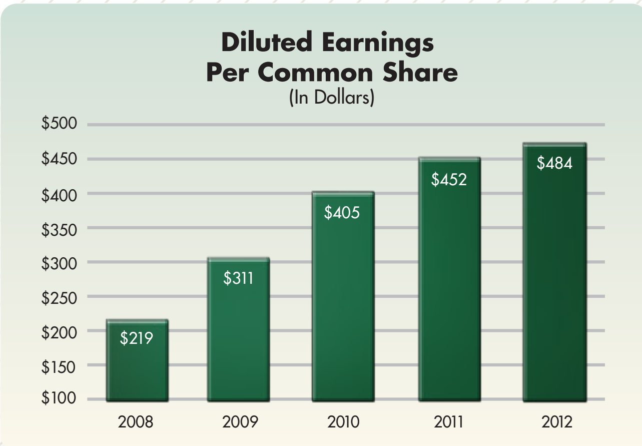
CORPORATE PROFILE

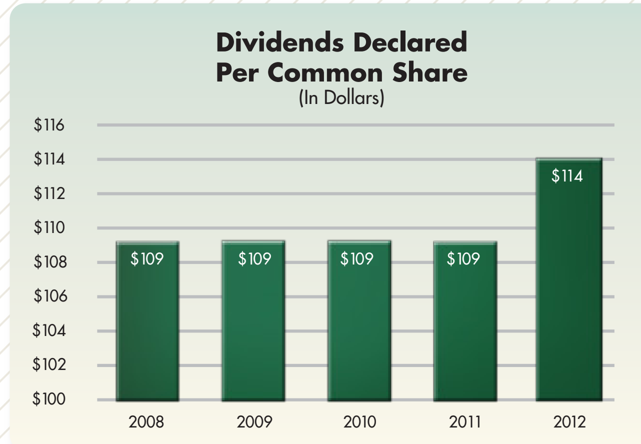
Farmers & Merchants Bank of Long Beach is a full-service, California-state-chartered community bank with $4.99 billion in total assets as of December 31, 2012. Founded in Long Beach in 1907 by C.J. Walker, the Bank specializes in commercial and small business banking, along with business loan programs, and has 21 offices located throughout Los Angeles and Orange County.

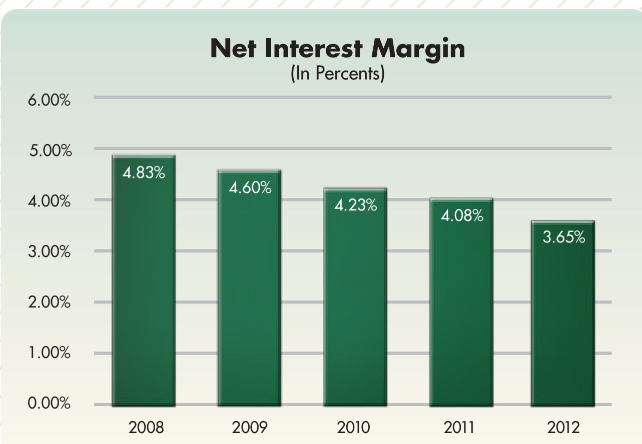
Farmers & Merchants Bank is one of the strongest banks in the country as measured by a variety of industry standards, and continues to uphold its founder's philosophy that safeguarding our clients' money is a sacred trust and giving back to the community is the wisest investment a business can make.

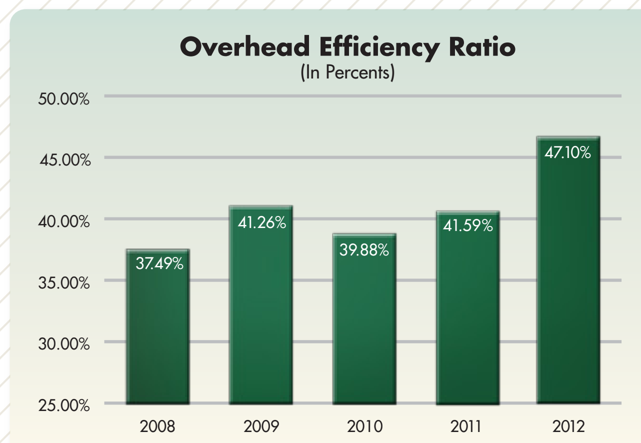
PARTNERS IN HEALTHCARE

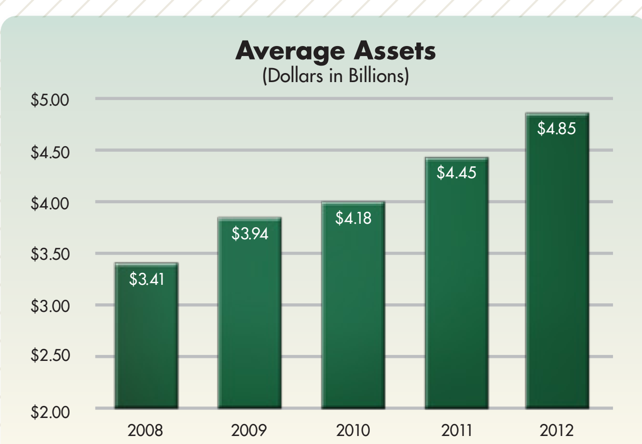
Recent studies suggest that financial health is linked to physical well-being, and the same can be said about the effects of physical well-being on financial health. The theme for this year's annual report, "Partners in Healthcare," is a testament to how deeply we value our relationships with our healthcare clients. Together, we are striving to keep the communities we serve as healthy as possible. From providing resources that make it easier for hospitals to serve patients, to helping doctors manage their finances with ease, F&M values the strength and achievements of its partners. We invite you to read the profiles on the following pages to see how F&M is partnering with healthcare professionals to enhance the community.

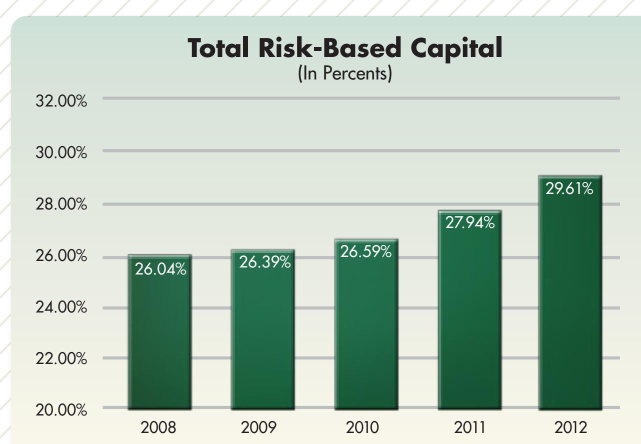

Diluted Earnings
Per Common Share
(In Dollars)
$500
$450
$400
$350
$300
$250
$200
$150
$100
$219
$311
$405
$452
$484
2008
2009
2010
2011
2012


Dividends Declared
Per Common Share
(In Dollars)
$116
$114
$112
$110
$108
$106
$104
$102
$100
$109
$109
$109
$109
$114
2008
2009
2010
2011
2012


Net Interest Margin
(In Percents)
6.00%
5.00%
4.00%
3.00%
2.00%
1.00%
0.00%
4.83%
4.60%
4.23%
4.08%
3.65%
2008
2009
2010
2011
2012


Overhead Efficiency Ratio
(In Percents)
50.00%
45.00%
40.00%
35.00%
30.00%
25.00%
37.49%
41.26%
39.88%
41.59%
47.10%
2008
2009
2010
2011
2012


Average Assets
(Dollars in Billions)
$5.00
$4.50
$4.00
$3.50
$3.00
$2.50
$2.00
$3.41
$3.94
$4.18
$4.45
$4.85
2008
2009
2010
2011
2012


Total Risk-Based Capital
(In Percents)
32.00%
30.00%
28.00%
26.00%
24.00%
22.00%
20.00%
26.04%
26.39%
26.59%
27.94%
29.61%
2008
2009
2010
2011
2012

Dear Fellow Shareholders:

Between 2008 and 2012, total deposits increased 38% at Farmers & Merchants Bank during one of the worst economic periods our country has experienced since the Great Depression. At the same time, we maintained strong capital ratios and continued to pay quarterly and special dividends.

The theme of this year's annual report, "Partners in Healthcare," is fitting because the financial health of a banking partner has an effect on clients much like that of a quality healthcare provider on patients' well-being.

In 1981, the strong bond between Farmers & Merchants and healthcare providers inspired Ken Walker to open an office inside Long Beach Memorial Hospital. An office location inside a medical center represents another bank service innovation pioneered by F&M. To this day, the office is located in the west wing of the hospital and serves all of the Memorial campuses, including Orange Coast and Saddleback.

At F&M, we are fortunate to not only serve some of the top healthcare providers in Southern California, but to do it with the financial vigor and stability that clients have counted on for more than a century.

Our solid financial performance in 2012 is a testament to the Bank's health and longevity, as we reported an increase in net income for the fourth consecutive year, despite an anemic economy and challenging regulatory environment.

Interest income for the year ended December 31, 2012, was $171.1 million, compared with $178.6 million for the same period in 2011. Interest expense for the year declined to $7.0 million from $9.5 million in 2011. The Bank's overall cost of funds reflected the low interest rate environment, as non-interest-bearing demand accounts grew 17% and time deposits decreased 7% in 2012.

Farmers & Merchants did not have a provision for loan losses for the year ended December 31, 2012, as the asset quality of the Bank's loan portfolio continued to stabilize. The Bank's allowance for loan losses as a percentage of loans outstanding was 2.57% at December 31, 2012, compared with 2.80% at December 31, 2011.

Non-interest expense for the year ended December 31, 2012, was $94.9 million, compared with $83.8 million last year.

The Bank's net income for 2012 rose to $63.4 million, or $484.14 per diluted share, from $59.1 million, or $451.53 per diluted share, for 2011.

Additionally, we made several key appointments during the year, including a new chief credit officer, chief auditor, chief information officer and supporting staff, which will further enhance our position of strength in 2013.

Healthy and Stable

Under the guidance of Chief Financial Officer John Hinrichs, we continued to maintain a healthy and stable balance sheet in 2012. The Bank's robust balance sheet has long been a defining characteristic of Farmers & Merchants when compared with other financial institutions throughout the region.

At December 31, 2012, net loans totaled $1.93 billion, compared with $2.03 billion at December 31, 2011. The Bank's deposits grew to $3.69 billion at the end of 2012, from $3.39 billion at December 31, 2011. Non-interest-bearing deposits represented 40.0% of total deposits at December 31, 2012, versus 37.2% of total deposits at December 31, 2011. Total assets increased to $4.99 billion at the close of 2012 from $4.66 billion at December 31, 2011.

Farmers & Merchants remained "well-capitalized" under all regulatory categories at December 31, 2012, with a total risk-based capital ratio of 29.61%, a Tier 1 risk-based capital ratio of 28.35%, and a Tier 1 leverage ratio of 14.24%. The minimum ratios for capital adequacy for a well-capitalized bank are 10.00%, 6.00% and 5.00%, respectively.

Now that the Bank is nearly halfway through its 106th year of serving Southern California, we are grateful for the strong relationships we continue to form within the community, including the tenured history we have with healthcare providers.

It is difficult to place a value on health, and yet the Bank's 2012 financial performance reflects an excellent prognosis for the future. We look forward to continuing to serve new and existing clients with strength, integrity and unparalleled service.

On behalf of our Board of Directors and management team, we thank our employees, clients and shareholders for their continued support in making Farmers & Merchants one of the healthiest banks in California.

Daniel K. Walker

Daniel K. Walker
CEO and Chairman of the Board

W. Henry Walker

W. Henry Walker
President

ROBERT MCCANN
CHIEF EXECUTIVE OFFICER AND EXECUTIVE DIRECTOR
OCMA – IRVINE, CALIF.

The Orange County Medical Association (OCMA) has a challenging mission: to promote the science and art of medicine, the protection of public health and the betterment of the medical profession. That isn't an easy feat in an environment where healthcare professionals are constantly adapting to new regulations.

"Physicians continue to face increasing costs that make running a practice very difficult," said Robert McCann, CEO and executive director of the OCMA, an Irvine, Calif.-based non-profit physician member organization. "We're here to assist physicians as they navigate an increasingly complex industry."

As part of that process, OCMA has partnered with Farmers & Merchants Bank to provide educational seminars on how physicians and physician groups can better manage the financial side of their practices. The more physicians know about managing their businesses, the easier it is for them to provide quality care for their patients.

"That's why banking with F&M is so valuable. Our members have access to experts who know what it takes to stay financially successful in an otherwise overwhelming environment," McCann said.

OCMA is on the front lines of several issues crucial to the future of medicine, including protecting patient access to high quality care, preserving economic stability, protecting the physician-patient relationship, as well as working closely with government officials to ensure healthcare reform is patient-centered and incorporates the physician perspective.

McCann applies a similar philosophy to banking. "We choose to do business with F&M because it is centered on the customer. The Bank, much like we are to physicians, is truly our advocate," he said.

IRENE SASAKI, M.D.
EYE TREATMENT CENTER
LONG BEACH, CALIF.

The Eye Treatment Center in Long Beach not only banks with Farmers & Merchants … its patients are F&M employees.

Call it a function of mutual respect and trust. The Center is a continuation of a practice that started in Long Beach in 1923, which has provided plenty of time for F&M and the Center's ophthalmologists to get to know each other.

Dr. Irene Sasaki, a partner at the Center, says providing patients with the highest quality eye care parallels what she expects from her bank. "I know I can pick up the phone and talk to someone at F&M who knows how to help me," she said.

Such is the case when working in an industry rife with new regulations. Dr. Sasaki recalls a recent scenario when she had to adjust the Center's credit card machine because of new privacy rules. "F&M knew what to do, and we continued to go about our business without delay."

Dr. Sasaki values F&M's ability to relate to independent businesses. With so much consolidation in the banking industry, many services have become commoditized, including what was once considered routine.

"Someone from F&M collects our deposits every day, and that kind of service, without any significant fees, is a big deal," Dr. Sasaki said.

It is noteworthy that the F&M employee who collects the Center's deposits is also a patient of Dr. Sasaki's. "It speaks to the parallels of our businesses. If someone knows who you are, they can address your needs better," Dr. Sasaki said.

RICK GRANIERE
CHIEF FINANCIAL OFFICER
MEMORIALCARE HEALTH SYSTEM – FOUNTAIN VALLEY, CALIF.

MemorialCare Health System and Farmers & Merchants Bank share a common history: they were both founded in Long Beach and have a relationship that dates back more than a century.

MemorialCare's Long Beach Memorial Medical Center became a client of the Bank when the hospital was founded in 1907. The healthcare system and the Bank have grown substantially during the last century, but their core values are rooted in the very same fundamentals that originally brought them together.

"Healthcare is a very local business and so is banking," said Rick Graniere, Chief Financial Officer of MemorialCare, which grew from a single hospital to an integrated delivery system with 11,000 employees and 2,500 affiliated doctors. "We provide community-based services, and that kind of tradition is something we have in common with Farmers & Merchants Bank."

F&M helps MemorialCare with checking, lockboxes and the processing of patient receivables. As MemorialCare expands in Southern California, its banking needs are growing. F&M recently helped MemorialCare find a solution to streamline its receivable process.

"I knew I could pick up the phone and talk to Dan Walker, CEO … and it was Ken Walker before that," Graniere said. "They are so responsive because they are the decision makers. When you go to a larger bank, you don't have that access."

Access is a critical attribute to MemorialCare when managing some of California's top-ranked hospitals, such as Saddleback Memorial Medical Center. The Laguna Hills-based hospital placed in the top 25 of "best" California hospitals in *U.S. News & World Report's* 2011-2012 rankings.

BRYNA KANE, M.D.
LASER SKIN CARE CENTER DERMATOLOGY ASSOCIATES
LONG BEACH, CALIF.

One of Dr. Bryna Kane's many memories when she moved to Long Beach in 1962 is when her family started banking with Farmers & Merchants.

"That's how my relationship started with the Bank," said Dr. Kane, who is now senior managing partner of Laser Skin Care Center Dermatology Associates in Long Beach.

Dr. Kane also recalls when Gus Walker, former chairman and president of F&M, was her neighbor. "He would give us a friendly smile, a thumbs-up and say, 'I hope you're banking at my bank.'"

Dr. Kane, her husband, Jerry Kaufman, and other family members continue to bank with F&M after nearly five decades in Long Beach. She credits the success of her own practice to the set of values she learned early in life from her family, friends and colleagues.

"I always treat my patients as if they are family, and the same goes for the way F&M treats its clients," Dr. Kane said. "Whether it's the Walkers, Mr. Hinrichs, Mr. Tiber, Mr. Miller, Mr. Bikov, or many of the other wonderful employees of F&M, I know I can pick up the phone and talk to them."

Access is important, especially to a high-profile doctor who has challenged stereotypes and bucked convention. Dr. Kane was the first female physician employed by then Memorial Medical Group and the first female physician to serve on the board of directors at the Memorial Medical Center. She is cofounder of Erase the Past, a free tattoo removal clinic for former gang members and at-risk youth.

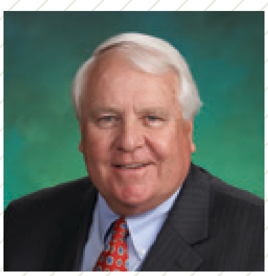
"Giving back to the community is another value I share with Farmers & Merchants," Dr. Kane said. "The community is integral to our lives, and I feel very privileged to have generations upon generations of patients, just as F&M has generations upon generations of loyal customers."

BOARD MEMBER PROFILES

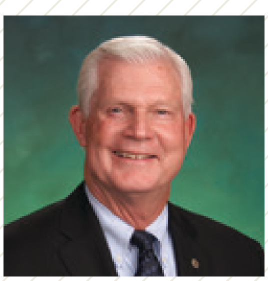
Daniel K. Walker
Chairman of the Board since 2003.
Mr. Walker is CEO of Farmers & Merchants Bank, where he has served in various positions since 1975.

Richard W. Darling
Board member since 2008.
Mr. Darling, who also served as a board member between 1994 and 2007, is the retired president of Bremco Construction, a general contractor specializing in projects for major industrial and commercial corporations, where he still serves in an advisory capacity on a daily basis.

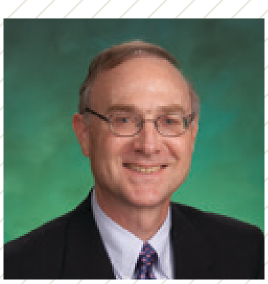
Walter M. Florie
Board member since 2007.
Mr. Florie, who formerly held executive positions at Union Bank for almost three decades, is now president and chief executive officer and director of the Earl B. and Loraine H. Miller Foundation, an organization focused on children and their healthcare needs in the greater Long Beach community.



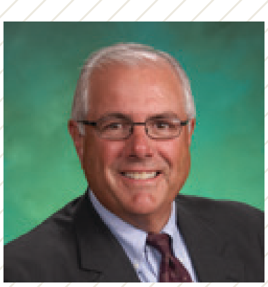
William G. Hayter
Board member since 1988.
Mr. Hayter, who previously served as president of the Pacific Hospital Foundation, director of the Long Beach YMCA, and counsel for the Boy Scouts of America, is a practicing attorney specializing in business, estate planning and trust administration.



Timothy W. Jackert
Board member since 2008.
Mr. Jackert served as chief financial officer at Memorial Medical Center Foundation in Long Beach for 38 years.



Lawrence J. McLaughlin
Board member since 1990.
Mr. McLaughlin, who formerly was a principal and managing partner of a Los Angeles-based law firm for more than three decades, is now a principal at Megandrew Mineral Co., a Girard, Texas-based petroleum development company.



Timothy M. Wilson
Board member since 2005.
Mr. Wilson is president of Mitchell Land & Improvement Co., a Southern California-based real estate development company where he previously served as executive vice president and chief operating officer.

CORPORATE INFORMATION

Board of Directors

Daniel K. Walker, Chairman of the Board
Richard W. Darling
Walter M. Florie
William G. Hayter
Timothy W. Jackert
Lawrence J. McLaughlin
Timothy M. Wilson

Principal Officers

Daniel K. Walker, Chairman of the Board and CEO
W. Henry Walker, President
Kenneth G. Walker, President, Main Office
John W.H. Hinrichs, Chief Financial Officer

Independent Auditor

KPMG LLP
600 Anton Boulevard, Suite 700
Costa Mesa, CA 92626-7651

Legal Counsel

Paul Hastings LLP
695 Town Center Drive, 17th Floor
Costa Mesa, CA 92626

Investor Relations

PondelWilkinson Inc.
1880 Century Park East, Suite 350
Los Angeles, CA 90067

Transfer Agent

American Stock Transfer and Trust Company
6201 15th Avenue
Brooklyn, NY 11219

Securities Listing

Farmers & Merchants Bank's common stock is traded on the OTC Markets system (OTCQB) under the symbol FMBL.

Corporate Headquarters

302 Pine Avenue
Long Beach, CA 90802

Certain statements in this annual report may be forward-looking statements. Readers of this annual report should understand that all such forward-looking statements are inherently subject to risk and uncertainties, some of which cannot be predicted or quantified. Future events and actual results could differ materially from those set forth in, contemplated by or underlying such forward-looking statements and the Bank's actual results or outcomes could differ materially from those anticipated.

Main—Long Beach
302 Pine Ave.
Long Beach, CA 90802
(562) 437-0011

Belmont Shore
4827 E. Second St.
Long Beach, CA 90803
(562) 621-1430

Bixby Knolls
4545 California Ave.
Long Beach, CA 90807
(562) 984-3600

East Long Beach
3140 E. Anaheim St.
Long Beach, CA 90804
(562) 621-1400

Fullerton
315 N. Harbor Blvd.
Fullerton, CA 92832
(714) 578-1945

Garden Grove
10422 Garden Grove Blvd.
Garden Grove, CA 92843
(714) 590-3880

Huntington Beach
7125 Yorktown Ave.
Huntington Beach, CA 92648
(714) 465-3131

Laguna Hills
24300 Paseo de Valencia
Laguna Hills, CA 92653
(949) 340-3150

Lake Forest
23772 Rockfield Blvd.
Lake Forest, CA 92630
(949) 460-7900

Lakewood
5101 Lakewood Blvd.
Lakewood, CA 90712
(562) 602-8378

Los Altos
2302 Bellflower Blvd.
Long Beach, CA 90815
(562) 799-7271

Memorial Hospital
2801 Atlantic Ave.
Long Beach, CA 90806
(562) 989-7862

Newport Beach
4695 MacArthur Ct., Ste. 130
Newport Beach, CA 92660
(949) 241-8280

Orange
1220 E. Katella Ave.
Orange, CA 92867
(714) 288-8450

Rolling Hills Estates
27525 Indian Peak Rd.
Rolling Hills Estates, CA 90274
(310) 491-1711

Rossmoor
12535 Seal Beach Blvd.
Seal Beach, CA 90740
(562) 799-2002

San Clemente
621 N. El Camino Real
San Clemente, CA 92672
(949) 373-2470

San Juan Capistrano
31873 Del Obispo St.
San Juan Capistrano, CA 92675
(949) 488-8550

Santa Ana
1750 E. Seventeenth St.
Santa Ana, CA 92705
(714) 564-1750

Torrance
22400 Hawthorne Blvd.
Torrance, CA 90505
(310) 265-3200

Tustin
2691 Park Ave.
Tustin, CA 92782
(714) 824-3070

Farmers & Merchants Bank®

fmb.com

MEMBER FDIC

EQUAL HOUSING OPPORTUNITY

Farmers & Merchants Bank®

Together, we're keeping our communities healthy.

Financials

2012 ANNUAL REPORT

FARMERS & MERCHANTS BANK OF LONG BEACH
2012 ANNUAL REPORT

Contents

KPMG LLP
Suite 700
20 Pacifica
Irvine, CA 92618-3391

Independent Auditors' Report

The Board of Directors
Farmers & Merchants Bank of Long Beach:

Report on the Financial Statements

We have audited the accompanying financial statements of Farmers & Merchants Bank of Long Beach (the Bank), which comprise the balance sheets as of December 31, 2012 and 2011, and the related statements of income, comprehensive income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Farmers & Merchants Bank of Long Beach as of December 31, 2012 and 2011, and the results of its operations and its cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

Report on Other Legal and Regulatory Requirements

We also have examined in accordance with attestation standards established by the American Institute of Certified Public Accountants, the Bank's internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated April 19, 2013 expressed an unqualified opinion on the effectiveness of the Bank's internal control over financial reporting.

KPMG LLP

Irvine, California
April 19, 2013

FARMERS & MERCHANTS BANK OF LONG BEACH
BALANCE SHEETS

	December 31, 2012	December 31, 2011
	(In thousands, except share and per share data)	
Assets		
Cash and due from banks:		
Non-interest-bearing balances	$ 60,914	$ 57,394
Interest-bearing balances	253,087	278,525
Total cash and due from banks	314,001	335,919
Securities available-for-sale (amortized cost of $617,239 and $533,026)	630,055	548,289
Securities held-to-maturity (fair value of $2,015,916 and $1,633,061)	1,942,085	1,564,841
Loans, net	1,933,082	2,028,507
Other real estate owned, net	17,696	23,036
Public welfare investments	35,804	43,566
Bank premises and equipment, net	60,504	55,155
Net deferred tax assets	26,060	28,583
Other assets	29,674	31,449
Total assets	**$ 4,988,961**	**$ 4,659,345**
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits:		
Non-interest bearing deposits	$ 1,474,215	$ 1,263,162
Interest bearing deposits	2,211,651	2,130,316
Total deposits	3,685,866	3,393,478
Securities sold under repurchase agreements	551,293	555,992
Other liabilities	34,543	39,659
Total liabilities	4,271,702	3,989,129
Commitments and contingencies		
Stockholders' equity:		
Common stock, par value $20; authorized 250,000 shares; issued and outstanding 130,928 shares	2,619	2,619
Additional paid-in capital	12,044	12,044
Retained earnings	695,169	646,708
Accumulated other comprehensive income	7,427	8,845
Total stockholders' equity	717,259	670,216
Total liabilities and stockholders' equity	**$ 4,988,961**	**$ 4,659,345**

See accompanying notes to financial statements.

FARMERS & MERCHANTS BANK OF LONG BEACH
STATEMENTS OF INCOME

	Years Ended December 31, 2012	2011
	(In thousands, except per share data)	
Interest income:		
Loans	$ 112,157	$ 115,395
Securities available-for-sale	10,794	13,980
Securities held-to-maturity	47,112	48,734
Deposits with banks	1,051	497
Total interest income	171,114	178,606
Interest expense:		
Deposits	5,840	7,920
Securities sold under repurchase agreements	1,147	1,535
Total interest expense	6,987	9,455
Net interest income	164,127	169,151
Provision for loan losses	-	14,200
Net interest income after provision for loan losses	164,127	154,951
Non-interest income:		
Service charges on deposit accounts	4,598	5,114
Gain on sale of securities	345	174
Merchant bankcard income	8,822	6,657
Other income	9,224	7,360
Total non-interest income	22,989	19,305
Non-interest expense:		
Salaries and employee benefits	48,271	41,814
FDIC and other insurance expense	6,479	4,671
Occupancy expense	5,487	5,501
Equipment expense	5,800	5,435
Other real estate owned expense, net	1,679	3,441
Amortization of public welfare investments	7,762	3,894
Merchant bankcard expense	7,112	5,400
Legal and professional services	2,882	3,896
Marketing expense	3,674	3,934
Other expense	5,727	5,842
Total non-interest expense	94,873	83,828
Income before income tax expense	92,243	90,428
Income tax expense	28,856	31,310
Net income	**$ 63,387**	**$ 59,118**
Basic and diluted earnings per common share	$ 484.14	$ 451.53

See accompanying notes to financial statements.

FARMERS & MERCHANTS BANK OF LONG BEACH
STATEMENTS OF COMPREHENSIVE INCOME

	Years Ended December 31, 2012	2011
	(In thousands)	
Net income	$ 63,387	$ 59,118
Other comprehensive income, net of tax:		
Unrealized losses on securities:		
Unrealized holding (losses) gains arising during period	(1,180)	2,258
Reclassification adjustment for net (gains) losses included in net income	(238)	31
Other comprehensive (loss) income	(1,418)	2,289
Comprehensive income	**$ 61,969**	**$ 61,407**

See accompanying notes to financial statements.

FARMERS & MERCHANTS BANK OF LONG BEACH
STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(IN THOUSANDS)

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Stockholders' Equity
Balance, December 31, 2010	**$ 2,619**	**$ 12,044**	**$ 601,861**	**$ 6,556**	**$ 623,080**
Net income	-	-	59,118	-	59,118
Cash dividends	-	-	(14,271)	-	(14,271)
Other comprehensive income, net of tax	-	-	-	2,289	2,289
Balance, December 31, 2011	**$ 2,619**	**$ 12,044**	**$ 646,708**	**$ 8,845**	**$ 670,216**
Net income	-	-	63,387	-	63,387
Cash dividends	-	-	(14,926)	-	(14,926)
Other comprehensive loss, net of tax	-	-	-	(1,418)	(1,418)
Balance, December 31, 2012	**$ 2,619**	**$ 12,044**	**$ 695,169**	**$ 7,427**	**$ 717,259**

See accompanying notes to financial statements.

FARMERS & MERCHANTS BANK OF LONG BEACH
STATEMENTS OF CASH FLOWS

	Years Ended December 31, 2012	2011
	(In thousands)	
Cash flows from operating activities:		
Net income	$ 63,387	$ 59,118
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,191	4,117
Net amortization on securities	28,655	22,953
Provision for loan losses	-	14,200
Addition (reduction) of reserve for losses on unfunded loan Commitments	100	(221)
Gain on sale of securities available-for-sale	(345)	(174)
Gain on sale of other real estate owned	(2,195)	(3,360)
Provision for other real estate owned	938	3,676
Amortization of public welfare investments	7,762	3,893
Deferred income tax expense (benefit)	3,553	(3,213)
Decrease in other assets	1,774	13,707
(Decrease) increase in other liabilities	(4,932)	1,327
Total adjustments	39,501	56,905
Net cash provided by operating activities	102,888	116,023
Cash flows from investing activities:		
Securities available-for-sale:		
Proceeds from maturities and paydowns	344,782	255,935
Proceeds from sales	7,642	6,049
Purchases	(444,242)	(333,168)
Securities held-to-maturity:		
Proceeds from maturities and paydowns	445,401	462,880
Purchases	(843,350)	(546,311)
Net decrease (increase) in loans	83,471	(45,932)
Purchases of bank premises and equipment	(9,540)	(5,353)
Proceeds from sale of other real estate owned	18,267	30,059
Capitalized expenditures on other real estate owned	-	(258)
Payments of senior lien on other real estate owned	-	(173)
Increase in public welfare investments	-	(4,983)
Net cash used in investing activities	(397,569)	(181,255)
Cash flows from financing activities:		
Net increase in deposits	292,388	389,485
Net decrease in securities sold under repurchase agreements	(4,699)	(72,200)
Cash dividends paid	(14,926)	(14,271)
Net cash provided by financing activities	272,763	303,014
Net (decrease) increase in cash and due from banks	(21,918)	237,782
Cash and cash equivalents at beginning of year	335,919	98,137
Cash and cash equivalents at end of year	**$ 314,001**	**$ 335,919**

See accompanying notes to financial statements.

FARMERS & MERCHANTS BANK OF LONG BEACH
STATEMENTS OF CASH FLOWS, CONTINUED

	Years Ended December 31,	
	2012	2011
	(In thousands)	
Supplemental disclosures of cash flow information		
Cash paid during the year for:		
Interest	$ 6,911	$ 9,535
Income taxes	31,369	30,673
Non-cash investing and financing activities:		
Transfers to other real estate owned from loans	$ 11,954	$ 17,665
Loans to facilitate the sale of other real estate owned	1,753	1,850
Transfers to bank premises from other real estate owned	-	2,270

See accompanying notes to financial statements.

NOTE 1 – NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Farmers & Merchants Bank of Long Beach (the "Bank" or "FMB") was founded in 1907 as a California state-chartered community bank that offers a broad range of banking products and services to individuals, professionals and small to medium-sized businesses. The Bank operates 21 branches in California's South Los Angeles County and Orange County as of December 31, 2012.

As a full-service commercial bank, FMB offers a broad range of banking products and services including: accepting demand, money market, and time deposits; originating loans and leases, including commercial real estate loans and commercial business loans; and providing other business-oriented banking products. The Bank also provides financing for residential loans including single-family and multifamily loans. To a lesser extent, the Bank also makes real estate construction and consumer loans.

The Bank's operations, like those of other financial institutions operating in Southern California, are significantly influenced by economic conditions in Southern California, including local economies, the strength of the real estate market, and the fiscal and regulatory policies of the federal and state government and the regulatory authorities that govern financial institutions.

Basis of Financial Statement Presentation

The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") and conform to general practices within the banking industry. The policies that materially affect the determination of financial position, results of operations and cash flow are summarized below.

Use of Estimates

In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and income statement for the year. Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan losses, the carrying value of securities available-for-sale, the valuation of other real estate owned and fair value disclosures. Actual results could differ from those estimates.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year's presentation.

Cash and due from banks

For purposes of reporting cash flows, cash and cash equivalents consist of cash and due from banks.

Securities Available-for-sale and Securities Held-to-maturity

The Bank classifies its securities into one of two categories: available-for-sale and held-to-maturity.

All securities not identified as held-to-maturity are classified as available-for-sale. These securities available-for-sale are carried at fair value. Unrealized holding gains and losses, net of the related tax effect, on securities available-for-sale are excluded from income and reported as a separate component of stockholders' equity identified as accumulated other comprehensive income until realized.

NOTE 1 – Nature of Operations and Summary of Significant Accounting Policies, continued

Securities Available-for-sale and Securities Held-to-maturity, continued

Securities held-to-maturity are those for which the Bank has the ability and positive intent to hold until maturity. These securities are recorded at cost, adjusted for the amortization of premiums and accretion of discounts on a level-yield basis.

Transfers of securities between categories, if any, are recorded at fair value at the date of the transfer. Unrealized holding gains or losses included in the separate component of equity for securities transferred from available-for-sale to held-to-maturity would be maintained and amortized into income over the remaining life of the security as an adjustment to the yield in a manner consistent with the amortization of premium or accretion of discount on the associated security.

If a decline in market value of any held-to-maturity or available-for-sale security below cost is deemed other-than-temporary, the security is written down to its fair value which becomes the new cost basis and an impairment loss is recognized. In estimating other-than-temporary impairment losses, management considers, among other things, (i) the length of time and the extent of which the fair value has been less than cost, (ii) the financial condition and near-term prospects of the issuer, and (iii) the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Any impairment on securities the Bank intends, or is more likely than not required to sell, is recognized in earnings as the entire difference between the amortized cost and its fair value. Any impairment on securities the Bank does not intend, or it is not more likely than not required to sell before recovery, is separated into an amount representing the credit loss, which is recognized in earnings and the amount related to all other factors, which is recognized in other comprehensive income. The new cost basis is not changed for subsequent recoveries in fair value.

Premiums and discounts are amortized and accreted over the life of the related investment security as an adjustment to yield using the interest method. Unamortized premiums and unaccreted discounts are recognized as a component of gain or loss on sale upon disposition of the related security. Interest income is recognized when earned. Realized gains and losses on the sale of securities available-for-sale are included in non-interest income as gain (loss) on sale of securities using the specific-identification method.

Loans

Loans are reported at the principal amounts outstanding, net of the allowance for loan losses, unamortized non-refundable loan fees and related direct loan origination costs. Deferred net fees and costs are recognized in interest income on an effective yield basis over the contractual loan term. Interest on loans is accrued as earned.

Nonaccrual Loans

It is the Bank's general practice for interest accrual on loans to be discontinued whenever the payment of interest or principal is 90 days past due. Whenever the accrual of interest is discontinued, previously accrued but uncollected interest income is reversed. Accrual of interest is resumed only when principal and interest are brought fully current and when in management's judgment such loans are deemed fully collectible as to both principal and interest. The accrual of interest on loans that are more than 90 days past due may continue if the loans are well secured, in the process of collection, and management deems it appropriate.

NOTE 1 – Nature of Operations and Summary of Significant Accounting Policies, continued

Impaired Loans

The Bank considers a loan impaired when it is probable that the Bank will be unable to collect all amounts due according to its contractual terms. The amount of impairment is measured either based on the present value of expected future cash flows discounted at the loan's effective interest rate, or measured against the value of the loan's underlying collateral if the loan is collateral dependent. Impairment losses are included in the allowance for loan losses through the provision for loan losses. Cash receipts on impaired loans receivable are applied to reduce the principal amount of such loans until the principal has been recovered and are recognized as income thereafter.

Troubled Debt Restructured Loans

A loan is classified as a troubled debt restructuring ("TDR") when a borrower is experiencing financial difficulties that lead to a restructuring of the loan, and the Bank grants concessions to the borrower in the restructuring that it would not otherwise consider. These concessions may include interest rate reductions, principal forgiveness, extension of maturity date and other actions intended to minimize potential losses. TDR loans may be excluded from restructured loan disclosures in years subsequent to the restructuring if the loans are in compliance with their modified terms. Generally, a nonaccrual loan that is restructured remains on nonaccrual for a period of six months to demonstrate that the borrower can meet the restructured terms. However, the borrower's performance prior to restructuring, or other significant events at the time of restructuring may be considered in assessing whether the borrower can meet the new terms and may result in the loan being returned to accrual status after a shorter performance period. If the borrower's performance under the new terms is not reasonably assured, the loan remains classified as a nonaccrual loan. Loans classified as TDRs are reported as impaired loans.

Allowance for Loan Losses

The allowance for loan losses is maintained at a level deemed appropriate by the Bank to adequately provide for known and inherent risks in the loan portfolio at the balance sheet date. The allowance is based upon a continuing review of the portfolio, past loan loss experience, current economic conditions which may affect the borrowers' ability to pay, and the underlying collateral value of the loans. Loans which are deemed to be uncollectible are charged off and deducted from the allowance. The provision for loan losses and recoveries on loans previously charged off are added to the allowance.

The allowance for loan losses consists of two components: specific allowances and general allowances. To determine the adequacy of the allowance in each of these two components, two primary methodologies are employed, the individual loan review analysis methodology and the classification migration methodology. These methodologies support the basis for determining allocations between the various loan segments and the overall adequacy of our allowance to provide for probable losses inherent in the loan portfolio. These methodologies are further supported by additional analysis of relevant factors such as the historical losses in the portfolio during the past 16 quarters, and environmental factors which include trends in delinquency and non-accrual, and other significant factors, such as the national and local economy, the volume and composition of the portfolio, strength of management and loan staff, underwriting standards, and the concentration of credit.

NOTE 1 – Nature of Operations and Summary of Significant Accounting Policies, continued

Allowance for Loan Losses, continued

The Bank's management allocates a specific allowance for "Impaired Loans", in accordance with Accounting Standard Codification ("ASC") Section 310-10-35. For non-impaired loans, a general allowance is established for those loans internally classified and risk graded Pass, Special Mention, Substandard, or Doubtful based on historical losses in the specific loan portfolio and a reserve based on environmental factors determined for that loan group. The level of the general allowance is established to provide coverage for management's estimate of the credit risk in the loan portfolio by various loan segments not covered by the specific allowance.

The Bank's loan portfolio, excluding impaired loans which are evaluated individually, is categorized into several segments for purposes of determining allowance amounts by loan segment. The loan segments management currently evaluates are: commercial real estate, real estate construction, single-family residence, multi-family residence, equity lines, credit cards, commercial, consumer and farmland. Within these segments, management then evaluates loans not criticized, which are referred to as "pass" loans, separately from criticized loans. The criticized loans are further grouped into three credit risk rating categories: "special mention," "substandard" and "doubtful," which management defines as follows.

Special Mention: Loans classified as special mention have a potential weakness that requires management's attention. If not addressed, these potential weaknesses may result in further deterioration in the borrower's ability to repay the loan.

Substandard: Loans classified as substandard have a well-defined weakness or weaknesses that jeopardize the collection of the debt. They are characterized by the possibility that the Bank will sustain some loss if the weaknesses are not corrected.

Doubtful: Loans classified as doubtful have all the weaknesses as those classifies as substandard, with the additional trait that the weaknesses make collection or repayment in full highly questionable and improbable.

In addition, management may refer to the loans classified as "substandard" and "doubtful" together as "classified loans." For additional information on classified loans, see Note 6, *Loans and Allowances for Loan Losses.*

Bank Premises and Equipment

Bank premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation is computed on a straight-line method based on the estimated useful lives of the assets:

Type	Estimated Useful Life
Buildings	20 to 30 years
Building improvements	20 to 30 years
Furniture, fixtures, and equipment	3 to 7 years
Leasehold improvements	Shorter of useful lives or the terms of the lease

Construction in process is carried at cost and includes land acquisition, architectural fees, general contractor fees, capitalized interest and other costs related directly to the construction of a property. Maintenance and repairs are charged to expense. Gains or losses on sale or retirement of assets are reported in equipment expense.

NOTE 1 – Nature of Operations and Summary of Significant Accounting Policies, continued

Bank Premises and Equipment, continued

The Bank reviews its long-lived assets for impairment annually or when events or circumstances indicate that the carrying amount of these assets may not be recoverable. When impairment is indicated for an asset, the amount of impairment loss is the excess of the net book value over its fair value.

Other Real Estate Owned

Other real estate owned (OREO) represents the collateral acquired through foreclosure in full or partial satisfaction of the related loan and is recorded at the fair value as established by a current appraisal, adjusted for estimated selling costs. The excess of the carrying amount of a loan over the fair value of real estate acquired less cost to sell is charged to the allowance for loan losses at the date of transfer. OREO values are reviewed on an ongoing basis and any decline in value is charged against OREO expense and included in the allowance for OREO in the period in which they are identified. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in OREO expense.

Public Welfare Investments

The Bank invests in limited liability companies and partnerships that make investments in commercial enterprises and affordable housing projects located in low income communities, which qualify for Federal or State income tax credits. The Bank's interests are accounted for utilizing the cost method of accounting and are being amortized over the life of the related tax credits. The investments are reviewed for impairment on an annual basis or on an interim basis if an event occurs that would trigger potential impairment.

Securities Sold Under Repurchase Agreements

The Bank sells certain securities under agreements to repurchase. The agreements are treated as collateralized financing transactions and the obligations to repurchase securities sold are reflected as a liability in the accompanying balance sheets. The securities underlying the agreements remain in the applicable asset accounts.

Operating Leases

The Bank enters into a variety of lease contracts generally for premises and equipment. Lease contracts that do not transfer substantially all of the benefits and risks of ownership and do not meet the accounting requirements for capital lease classification are treated as operating leases. The Bank accounts for the payments of rent on these contracts on a straight-line basis over the lease term. At inception of the lease term, any periods for which no rents are paid and/or escalation clauses are stipulated in the lease contract are included in the determination of the rent expense and recognized ratably over the lease term.

NOTE 1 – Nature of Operations and Summary of Significant Accounting Policies, continued

Reserve for Losses on Unfunded Loan Commitments

The Bank maintains a reserve for losses on unfunded loan commitments to absorb losses inherent in those commitments upon funding. The commitments include unfunded loan commitments, standby letters of credit and commercial lines of credit. The Bank's methodology for assessing the appropriateness of this allowance is the same as that used for the allowance for loan losses and incorporates an assumption based upon historical information of likely utilization. See accounting policy "Loans and Allowance for Loan Losses." The reserve for losses on unfunded loan commitments is classified as other liabilities and the change in this reserve is recognized in noninterest expense.

Income Taxes

Income taxes are accounted for under the asset and liability method. Under this method, the deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

The Bank has adopted the provisions of ASC 740-10, *Accounting for Uncertainty in Income Taxes,* which prescribes a recognition threshold and measurement standard for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. ASC 740-10 requires that the Bank recognize in the financial statements the impact of a tax position, if that position is more likely than not to be sustained, based on the technical merits of the position.

On an ongoing basis, management evaluates the deferred tax assets to determine if the tax benefits are expected to be realized in future periods. To the extent the benefit of a deferred tax asset is no longer expected to be realized, a valuation allowance is established with a corresponding charge through the provision for income taxes.

The Bank may, from time to time, be assessed interest or penalties by taxing authorities. In the event a reserve for interest and penalties is established pursuant to ASC 740-10, or, if any such interest and penalties are assessed by a tax authority, such amounts will be classified in the financial statements as income tax expense.

Comprehensive Income

Other comprehensive income refers to revenues, expenses, and gains and losses that are included in comprehensive income but are excluded from net income because they have been recorded directly in equity. The Bank’s comprehensive income consists of net income and net unrealized gains (losses) on securities available-for-sale, arising during the period and is presented in the statements of comprehensive income.

Earnings Per Share (EPS) Data

Basic EPS is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period.

NOTE 1 – Nature of Operations and Summary of Significant Accounting Policies, continued

Recent Accounting Standards

In April 2011, the FASB issued ASU 2011-03, *Transfers and Servicing (Topic 860): Reconsideration of Effective Control for Repurchase Agreements*. ASU 2011-03 removes the transferor's ability criterion from the consideration of effective control for repos and other agreements that both entitle and obligate the transferor to repurchase or redeem financial assets before their maturity. The amendments in ASU 2011-03 remove from the assessment of effective control (1) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee, and (2) the collateral maintenance implementation guidance related to that criterion. The FASB indicates that eliminating the transferor's ability criterion and related implementation guidance from an entity's assessment of effective control should improve the accounting for repos and other similar transactions. The amendments in ASU 2011-03 are effective for the first interim or annual period beginning on or after December 15, 2011 and are to be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted. The adoption of this guidance did not have a material effect on the Bank's financial statements.

In May 2011, the FASB issued ASU 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. ASU 2011-04 addresses convergence between GAAP and International Financial Reporting Standards ("IFRS") requirements for measurement of and disclosures about fair value. The amendments are not expected to have a significant impact on companies applying GAAP. Key provisions of the amendment include: a prohibition on grouping financial instruments for purposes of determining fair value, except when an entity manages market and credit risks on the basis of the entity's net exposure to the group; an extension of the prohibition against the use of a blockage factor to all fair value measurements (that prohibition currently applies only to financial instruments with quoted prices in active markets); and a requirement that for recurring Level 3 fair value measurements, entities disclose quantitative information about unobservable inputs, a description of the valuation process used and qualitative details about the sensitivity of the measurements. In addition, for items not carried at fair value but for which fair value is disclosed, entities will be required to disclose the level within the fair value hierarchy that applies to the fair value measurement disclosed. The amendments in ASU 2011-04 are effective during interim and annual periods beginning after December 15, 2011. The adoption of this guidance did not have a material effect on the Bank's financial statements.

In June 2011, The FASB issued ASU 2011-05, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income*. ASU 2011-05 will require companies to present the components of net income and other comprehensive income either as one continuous statement or as two consecutive statements. It eliminates the option to present components of other comprehensive income as part of the statement of changes in stockholders' equity. The standard does not change the items which must be reported in other comprehensive income, how such items are measured, or when they must be reclassified to net income. The FASB amended ASU 2011-05 in December 2011, with the issuance of ASU 2011-12, *Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05.* ASU 2011-12 defers only changes in ASU 2011-05 that relate to the presentation of reclassification adjustments. Both standards are effective for interim and annual periods beginning after December 15, 2011. The adoption of these standards only affected the presentation of the Bank's financial statements and did not have an impact on the financial amounts presented in the statements.

NOTE 1 – Nature of Operations and Summary of Significant Accounting Policies, continued

Recent Accounting Standards, continued

In December 2011, the FASB issued ASU 2011-11, *Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities*. ASU 2011-11 affects all entities that have financial instruments and derivative instruments that are either (1) offset in accordance with either Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement. The requirements amend the disclosure requirements on offsetting in Section 210-20-50. This information is intended to enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments in the scope of this ASU. The amended guidance is effective for interim and annual periods beginning after January 1, 2013 and should be applied retrospectively to all periods presented. The Bank does not expect the adoption of the disclosure requirements to have a material effect on its financial statements.

NOTE 2 – SECURITIES AVAILABLE-FOR-SALE

The following table presents an analysis of the securities available-for-sale portfolio:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
At December 31, 2012				
US Treasury	$ 100	$ -	$ -	$ 100
Federal agency - Debt	143,847	187	4	144,030
Federal agency - MBS	123,987	8,104	-	132,091
CMOs - Federal agency	17,995	296	-	18,291
State and municipal securities	326,280	4,458	233	330,505
Corporate debt securities	5,030	8	-	5,038
Total securities available-for-sale	$ 617,239	$ 13,053	$ 237	$ 630,055
At December 31, 2011				
Federal agency - Debt	$ 153,114	$ 262	$ 37	$ 153,339
Federal agency - MBS	181,325	9,952	-	191,277
CMOs - Federal agency	31,861	611	-	32,472
State and municipal securities	163,903	4,510	39	168,374
Corporate debt securities	2,823	12	8	2,827
Total securities available-for-sale	$ 533,026	$ 15,347	$ 84	$ 548,289

NOTE 2 – Securities Available-for-Sale, continued

The following table presents a summary of the estimated maturities of securities available-for-sale as of December 31, 2012:

	Amortized Cost	Fair Value
	(In thousands)	
Due in 1 year or less	$ 95,767	$ 95,936
Due after 1 year through 5 years	175,770	177,420
Due after 5 years through 10 years	99,893	102,012
Due after 10 years	103,827	104,305
Federal agency - MBS	123,987	132,091
CMOs - Federal agency	17,995	18,291
	$ 617,239	$ 630,055

Proceeds from sales of securities available-for-sale were $7.64 million during 2012 and $6.05 million during 2011. Gross realized gains on sale of securities available-for-sale were $345,000 in 2012 and $174,000 in 2011.

The following table shows the gross unrealized losses on available-for-sale securities and the fair value of the related available-for-sale securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2012:

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)					
Federal agency - Debt	$ 11,084	$ 4	$ -	$ -	$ 11,084	$ 4
State and municipal securities	65,947	226	700	7	66,647	233
Total temporarily impaired securities	$ 77,031	$ 230	$ 700	$ 7	$ 77,731	$ 237

The unrealized losses on State and municipal securities are primarily attributable to declining market prices caused by lower interest rate environment. At December 31, 2012, there were 304 and 2 available-for-sale securities with unrealized losses less than 12 months and 12 months or longer, respectively. Whenever the cost of an investment security exceeds its fair value, management evaluates, among other factors, general market conditions, the duration and extent to which cost is more than fair value.

At December 31, 2012, management believes that available-for-sale securities in an unrealized loss position had a loss position that was temporary in nature, therefore no impairment losses were recognized in the income statement. Because the Bank has the ability and intent to hold these investments until a market price recovery or maturity, these available-for-sale securities are not considered other-than-temporarily impaired.

NOTE 2 – Securities Available-for-Sale, continued

The following represents the related tax effect allocated to each component of other comprehensive income for the year ended December 31, 2012 and December 31, 2011:

	Before-Tax Amount	Tax (Expense) Benefit	Net-of-Tax Amount
		(In thousands)	
Year ended December 31, 2012			
Unrealized losses on securities:			
Unrealized holding (losses) gains arising during period	$ (2,036)	$ 856	$ (1,180)
Reclassification adjustment for net (gains) losses included in net income	(411)	173	(238)
Other comprehensive (loss) income	$ (2,447)	$ 1,029	$ (1,418)
Year ended December 31, 2011			
Unrealized losses on securities:			
Unrealized holding gains (losses) arising during Period	$ 3,897	$ (1,639)	$ 2,258
Reclassification adjustment for net losses (gains) included in net income	54	$ (23)	$ 31
Other comprehensive income (loss)	$ 3,951	$ (1,662)	$ 2,289

NOTE 3 – SECURITIES HELD-TO-MATURITY

The following table presents an analysis of the securities held-to-maturity portfolio:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(In thousands)		
At December 31, 2012				
Federal agency - Debt	$ 16,247	$ 59	$ 7	$ 16,299
Federal agency - MBS	1,452,426	48,771	111	1,501,086
CMOs - Federal agency	71,010	846	55	71,801
State and municipal securities	396,935	24,591	389	421,137
Corporate debt securities	5,467	126	-	5,593
Total securities held-to-maturity	$ 1,942,085	$ 74,393	$ 562	$ 2,015,916
At December 31, 2011				
Federal agency - Debt	$ 4,141	$ 82	$ -	$ 4,223
Federal agency - MBS	1,114,111	44,423	-	1,158,534
CMOs - Federal agency	114,495	1,984	117	116,362
State and municipal securities	326,339	21,676	59	347,956
Corporate debt securities	5,755	231	-	5,986
Total securities held-to-maturity	$ 1,564,841	$ 68,396	$ 176	$ 1,633,061

NOTE 3 – Securities Held-to-Maturity, continued

The following table is a summary of the estimated maturities of securities held-to-maturity as of December 31, 2012:

	Amortized Cost	Fair Value
	(In thousands)	
Due in 1 year or less	$ 13,793	$ 14,029
Due after 1 year through 5 years	67,868	71,568
Due after 5 years through 10 years	234,600	252,295
Due after 10 years	102,388	105,137
Federal agency - MBS	1,452,426	1,501,086
CMOs - Federal agency	71,010	71,801
	$ 1,942,085	$ 2,015,916

There were no sales of securities held-to-maturity in 2012 or 2011.

The following table shows the gross unrealized losses on held-to-maturity securities and the fair value of the related held-to-maturity securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2012:

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
			(In thousands)			
Federal agency - Debt	$ 3,735	$ 7	$ -	$ -	$ 3,735	$ 7
Federal agency - MBS	52,728	111	-	-	52,728	111
CMOs - Federal agency	13,209	55	-	-	13,209	55
State and municipal securities	34,406	389	-	-	34,406	389
Total temporarily impaired securities	$ 104,078	$ 562	$ -	$ -	$ 104,078	$ 562

The Bank's held-to-maturity portfolio is primarily comprised of mortgage-backed securities issued or guaranteed by FNMA (Fannie Mae) or GNMA (Ginnie Mae). The unrealized losses are primarily attributable to declining market prices caused by accelerated prepayments on the mortgages resulting from a lower interest rate environment. At December 31, 2012, there were 132 and 0 held-to-maturity securities with unrealized losses less than 12 months and 12 months or longer, respectively.

At December 31, 2012, management believes that held-to-maturity securities in an unrealized loss position had a loss position that was temporary in nature, and therefore no impairment losses were recognized in the statement of income. Because the Bank has the ability and intent to hold these investments until maturity, these held-to-maturity securities are not considered other-than-temporarily impaired.

Total securities with a carrying value of approximately $1.03 billion and $1.04 billion at December 31, 2012 and December 31, 2011, respectively, were pledged to secure securities sold under agreement to repurchase, public deposits and for other purposes required by law.

Interest income on tax-exempt securities was $11.7 million for the year ended December 31, 2012, and $10.1 million for the year ended December 31, 2011.

NOTE 4 – LOANS AND ALLOWANCE FOR LOAN LOSSES

The loan portfolio is composed mainly of credit extended to borrowers in Southern California with the majority of loans secured by real estate, even though a substantial amount of the Bank's loans are intended for business purposes. There is no concentration of loans to borrowers in a specific industry within the loan portfolio. Loans are generally expected to be paid off from the operating cash flow of the borrowers, refinancing by another lender, or through sale by the borrowers of the secured collateral.

The following is the presentation of the loan portfolio by loan segment:

	December 31, 2012	December 31, 2011
	(In thousands)	
Commercial loans	$ 154,477	$ 178,030
Real estate construction loans	36,535	81,278
Loans secured by real estate	1,652,436	1,680,287
Equity lines	123,972	127,251
Installment and other loans	17,020	20,542
Gross Loans	1,984,440	2,087,388
Less: Allowance for loan losses	(50,994)	(58,463)
Unamortized deferred loan fees, net	(364)	(418)
Loans, net	$ 1,933,082	$ 2,028,507
Loans held for sale	$ 2,364	$ 4,713

Nonaccrual and Past Due

Loans are tracked by the numbers of days borrower payments are past due. The following table presents an aging analysis of nonaccrual and past due loans, segregated by loan segment as of December 31, 2012 and as of December 31, 2011:

	As of December 31, 2012					
	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days & Over Still Accruing	Non-accrual	Current	Total
	(In thousands)					
Loan Segment						
Commercial loans	6,070	521	-	2,428	145,458	154,477
Real estate construction loans	-	-	-	6,607	29,928	36,535
Loans secured by real estate	8,230	231	440	38,564	1,604,971	1,652,436
Equity lines	-	-	-	1,526	122,446	123,972
Installment and other loans	9	191	70	-	16,750	17,020
Total loans	**$ 14,309**	**$ 943**	**$ 510**	**$ 49,125**	**$ 1,919,553**	**$ 1,984,440**

NOTE 4 – Loans and Allowance for Loan Losses, continued

Nonaccrual and Past Due, continued

	As of December 31, 2011					
	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days & Over Still Accruing	Non-accrual	Current	Total
	(In thousands)					
Loan Segment						
Commercial loans	$ -	$ -	$ 141	$ 4,134	$ 173,755	$ 178,030
Real estate construction loans	2,766	-	-	14,594	63,918	81,278
Loans secured by real estate	5,036	428	144	106,521	1,568,158	1,680,287
Equity lines	96	-	-	803	126,352	127,251
Installment and other loans	720	343	108	-	19,371	20,542
Total loans	**$ 8,618**	**$ 771**	**$ 393**	**$ 126,052**	**$ 1,951,554**	**$ 2,087,388**

The following is a summary of non-accrual loans as of December 31, 2012 and 2011 and the related contractual interest income foregone for the years then ended:

	2012	2011
	(In thousands)	
Nonaccrual loans		
Outstanding balance	$ 49,125	$ 126,052
Average balance	79,801	113,841
Interest income recorded	217	1,134
Interest income foregone	3,144	5,029

Credit Quality

Loans are risk rated based on analysis of the current state of the borrower's credit quality. The analysis of credit quality includes review of all sources of repayment, the borrower's current payment performance/delinquency, the borrower's current financial and liquidity status, and all other relevant information.

The following tables present the credit risk rating categories for each loan segment as of the dates indicated. Nonclassified loans are those with a credit risk rating of either pass or special mention, while classified loans are those with a credit risk rating of either substandard or doubtful.

	December 31, 2012			December 31, 2011		
	Nonclassified	Classified	Total	Nonclassified	Classified	Total
	(In thousands)					
Year Ended December 31, 2010						
Commercial loans	$ 151,088	$ 3,389	$ 154,477	$ 174,719	$ 3,311	$ 178,030
Real estate construction loans	29,457	7,078	36,535	64,567	16,711	81,278
Loans secured by real estate	1,554,072	98,364	1,652,436	1,488,381	191,906	1,680,287
Equity lines	116,826	7,146	123,972	120,139	7,112	127,251
Installment and other loans	17,020	-	17,020	20,433	109	20,542
Total	**$ 1,868,463**	**$ 115,977**	**$ 1,984,440**	**$ 1,868,239**	**$ 219,149**	**$ 2,087,388**

NOTE 4 – Loans and Allowance for Loan Losses, continued

Loan Impairment

Nonaccrual loans and performing restructured loans are considered impaired for reporting purposes. The following table segregates the major loan categories between those loans that were individually evaluated for impairment and those loans that were collectively evaluated for impairment.

	December 31, 2012			December 31, 2011		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
	(In thousands)					
Loan Segment						
Commercial loans	$ 2,598	$ 151,879	$ 154,477	$ 4,324	$ 173,706	$ 178,030
Real estate construction loans	6,839	29,696	36,535	14,594	66,683	81,277
Loans secured by real estate	55,031	1,597,405	1,652,436	121,853	1,558,434	1,680,287
Equity lines	1,526	122,446	123,972	803	126,448	127,251
Installment and other loans	-	17,020	17,020	-	20,543	20,543
Total	**$ 65,994**	**$ 1,918,446**	**$ 1,984,440**	**$ 141,574**	**$ 1,945,814**	**$ 2,087,388**

For the indicated periods, the following table contains an analysis of impaired loans by segment:

	As of December 31, 2012						
	Unpaid Principal Balance	Recorded Investment With No ALLL	Recorded Investment With Allowance	Related ALLL	Total	Average Recorded Investment	Interest Income Recognized
	(In thousands)						
Loan Segment							
Commercial loans	$ 8,486	$ 2,395	$ 203	$ 36	$ 2,562	$ 6,913	$ 179
Real estate construction loans	7,460	6,839	-	-	6,839	11,455	14
Loans secured by real estate	64,131	51,668	3,363	804	54,227	83,075	1,183
Equity lines	1,760	1,526	-	-	1,526	1,555	34
Installment and other loans	-	-	-	-	-	-	-
Total	**$ 81,837**	**$ 62,428**	**$ 3,566**	**$ 840**	**$ 65,154**	**$ 102,998**	**$ 1,410**

	As of December 31, 2011						
	Unpaid Principal Balance	Recorded Investment With No ALLL	Recorded Investment With Allowance	Related ALLL	Total	Average Recorded Investment	Interest Income Recognized
	(In thousands)						
Loan Segment							
Commercial loans	$ 4,822	$ 3,999	$ 325	$ (109)	$ 4,215	$ 3,811	$ 25
Real estate construction loans	21,028	12,773	1,821	(213)	14,381	16,556	367
Loans secured by real estate	146,187	105,805	16,048	(345)	121,508	113,853	1,639
Equity lines	934	803	-	-	803	783	2
Installment and other loans	-	-	-	-	-	-	-
Total	**$ 172,971**	**$ 123,380**	**$ 18,194**	**$ (667)**	**$ 140,907**	**$ 135,003**	**$ 2,033**

NOTE 4 – Loans and Allowance for Loan Losses, continued

Troubled Debt Restructured Loans

Included in the Bank's loan portfolio are troubled debt restructured loans (TDR) which are modified because of deterioration in the financial condition of the borrower. The total amount of TDR was $57.0 million at December 31, 2012 and $88.9 million at December 31, 2011.

The following tables present TDRs as of each year end that were modified as TDRs during the year.

	For The Year Ended December 31, 2012						
		Pre-modification	Post-modification			TDRs that Subsequently Defaulted	
	No. of Contracts	Outstanding Recorded Investment	Outstanding Recorded Investment	Charge-offs During modification	Allocated Reserve	No. of Contracts	Recorded Investment
	(In thousands)						
Loan Segment							
Commercial loans	4	$ 472	$ 472	$ -	$ 33	-	$ -
Real estate construction loans	3	6,996	6,996	-	-	1	1,494
Loans secured by real estate	12	18,236	18,221	15	776	1	1,355
Equity lines	-	-	-	-	-	-	-
Installment and other loans	-	-	-	-	-	-	-
Total	**19**	**$ 25,704**	**$ 25,689**	**$ 15**	**$ 809**	**2**	**$ 2,849**

	For The Year Ended December 31, 2011						
		Pre-modification	Post-modification			TDRs that Subsequently Defaulted	
	No. of Contracts	Outstanding Recorded Investment	Outstanding Recorded Investment	Charge-offs During modification	Allocated Reserve	No. of Contracts	Recorded Investment
	(In thousands)						
Loan Segment							
Commercial loans	4	$ 436	$ 436	$ -	$ 8	-	$ -
Real estate construction loans	3	11,878	11,878	-	1	2	3,726
Loans secured by real estate	33	78,270	78,270	-	345	8	15,721
Equity lines	1	442	442	-	-	-	-
Installment and other loans	-	-	-	-	-	-	-
Total	**41**	**$ 91,026**	**$ 91,026**	**$ -**	**$ 354**	**10**	**$ 19,447**

NOTE 4 – Loans and Allowance for Loan Losses, continued

Accruing TDRs

A summary of accruing TDRs by concession type and by loan segment is shown below for each year end.

	As of December 31, 2012			
	Principal Deferral	Rate Reduction	Combination of such Concession	Total
	(In thousands)			
Loan Segment				
Commercial loans	$ 170	$ -	$ -	$ 170
Real estate construction loans	-	-	231	231
Loans secured by real estate	7,208	-	9,260	16,468
Total loans	**$ 7,378**	**$ -**	**$ 9,491**	**$ 16,869**

	As of December 31, 2011			
	Principal Deferral	Rate Reduction	Combination of such Concession	Total
	(In thousands)			
Loan Segment				
Commercial loans	$ 190	$ -	$ -	$ 190
Real estate construction loans	-	-	-	-
Loans secured by real estate	3,716	3,270	8,347	15,333
Total loans	**$ 3,906**	**$ 3,270**	**$ 8,347**	**$ 15,523**

Non-Accruing TDRs

A summary of non-accruing TDRs by concession type and by loan segment is shown below for each year end.

	As of December 31, 2012			
	Principal Deferral	Rate Reduction	Combination of such Concession	Total
	(In thousands)			
Loan Segment				
Commercial loans	$ 222	$ -	$ -	$ 222
Real estate construction loans	6,382	-	-	6,382
Loans secured by real estate	21,109	-	12,017	33,126
Equity lines	416	-	-	416
Total loans	**$ 28,129**	**$ -**	**$ 12,017**	**$ 40,146**

NOTE 4 – Loans and Allowance for Loan Losses, continued

Non-Accruing TDRs, continued

	As of December 31, 2011			
	Principal Deferral	Rate Reduction	Combination of such Concession	Total
	(In thousands)			
Loan Segment				
Commercial loans	$ 203	$ -	$ 16	$ 219
Real estate construction loans	6,768	-	4,811	11,579
Loans secured by real estate	29,139	1,107	30,862	61,108
Equity lines	431	-	-	431
Total loans	**$ 36,541**	**$ 1,107**	**$ 35,689**	**$ 73,337**

Allowance for Loan Losses

The following tables present summaries of the activity in the allowance for loan losses by loan segment for the years ended December 31, 2012 and 2011:

	Commercial Loans	Real Estate Construction Loans	Loans Secured by Real Estate	Equity Lines	Installment and Other Loans	Total
	(In thousands)					
December 31, 2010	**$ 2,504**	**$ 10,960**	**$ 33,208**	**$ 2,129**	**$ 6,826**	**$ 55,627**
Provision	4,994	(3,169)	15,646	(1,842)	(1,429)	14,200
Charge-Offs	(1,398)	(400)	(10,473)	(150)	(1,736)	(14,157)
Recoveries	768	949	210	515	351	2,793
December 31, 2011	**$ 6,868**	**$ 8,340**	**$ 38,591**	**$ 652**	**$ 4,012**	**$ 58,463**
Provision	348	(6,520)	3,965	544	1,663	-
Charge-Offs	(6,028)	(1,274)	(1,899)	(125)	(892)	(10,218)
Recoveries	902	879	531	2	435	2,749
December 31, 2012	**$ 2,090**	**$ 1,425**	**$ 41,188**	**$ 1,073**	**$ 5,218**	**$ 50,994**
The ending balance of the allowance is composed of amounts applicable to loans:						
Individually evaluated for impairment	$ 36	$ -	$ 804	$ -	$ -	$ 840
Collectively evaluated for impairment	$ 2,054	$ 1,425	$ 40,384	$ 1,073	$ 5,218	$ 50,154

NOTE 4 – Loans and Allowance for Loan Losses, continued

Reserve for Unfunded Loan Commitments

Activities in the reserve for unfunded loan commitments included in other liabilities in the accompanying balance sheet for the years ended December 31, 2012 and 2011 were as follows:

	December 31, 2012	December 31, 2011
	(In thousands)	
Balance, beginning of year	$ 2,052	$ 2,272
Addition (reduction) of reserve for losses on unfunded loan commitments	100	(220)
Balance, end of year	$ 2,152	$ 2,052

NOTE 5 – BANK PREMISES AND EQUIPMENT

The following is a summary of bank premises and equipment as of the dates indicated:

	December 31, 2012	December 31, 2011
	(In thousands)	
Land	$ 24,725	$ 21,806
Buildings and building improvements	43,014	40,093
Furniture, fixtures and equipment	25,567	26,541
Leasehold improvements	3,780	3,594
Construction in progress	2,444	1,453
	$ 99,530	$ 93,487
Less accumulated depreciation and amortization	(39,026)	(38,332)
	$ 60,504	$ 55,155

Depreciation and amortization expense was $4.2 million in 2012 and $4.1 million in 2011.

The Bank is committed under operating leases on certain premises and equipment. Certain leases require the Bank to pay property taxes and insurance. Rental expense was $518,000 in 2012 and $994,000 in 2011, net of rental income of $1,012,700 and $590,000, respectively. Annual minimum lease commitments at December 31, 2012 were:

Year Ending December 31,	Commitments (In thousands)
2013	$ 1,244
2014	968
2015	862
2016	604
2017	446
Thereafter	$ 1,087

NOTE 5 – Bank Premises and Equipment, continued

The following table shows future rental payments to be received under operating leases with terms in excess of one year as of December 31, 2012:

Year Ending December 31,	Commitments
	(In thousands)
2013	$ 913
2014	807
2015	670
Thereafter	$ 1,261

Management expects that in the normal course of business, leases that expire will be renewed or replaced by other leases.

NOTE 6 – OTHER REAL ESTATE OWNED

At December 31, 2012 and 2011, other real estate owned was $17.7 million, net of reserve for OREO of $11.7 million and $23.0 million, net of reserve for OREO of $13.4 million, respectively. The following table summarizes OREO by property type at the dates indicated:

	December 31,	
	2012	2011
	(In thousands)	
Commercial real estate	$ 1,900	$ 4,010
Construction and land development	13,746	18,585
Farmland	1,065	-
Single family residence	985	441
Total OREO, net	$ 17,696	$ 23,036

The components of OREO expense, net are as follows:

	2012	2011
	(In thousands)	
Operating and maintenance expense	$ 3,538	$ 4,996
Provision for losses	938	3,676
Rental income	(602)	(1,871)
Net gain on sale	(2,195)	(3,360)
	$ 1,679	$ 3,441

NOTE 7 – PUBLIC WELFARE INVESTMENTS

The Bank has invested in certain limited liability companies and partnerships that make investments in commercial enterprises and affordable housing projects located in low income communities. The Bank evaluates the investment in the fund to determine whether it meets the definition of variable interest entity (VIE) and whether the Bank is required to consolidate the fund. The Bank is not the primary beneficiary and, therefore not required to consolidate these entities.

NOTE 7 – Public Welfare Investments, continued

The Bank's investments totaled $35.8 and $43.6 million at December 31, 2012 and December 31, 2011, respectively. Unfunded commitments related to these investments totaled $23.0 million and $31.1 million at December 31, 2012 and December 31, 2011, respectively, which were recorded under accrued interest payable and other liabilities.

The remaining Federal tax credits to be utilized over a multiple-year period are $39.6 million at December 31, 2012. The Bank's usage of tax credits approximated $8.9 million for 2012 and $3.7 million for 2011.

NOTE 8 – DEPOSITS

The following table presents the components of deposits as of the dates indicated:

	December 31,	
	2012	2011
	(In thousands)	
Non-interest bearing checking	$ 1,474,215	$ 1,263,162
Interest bearing checking	346,991	300,984
Money market accounts	468,650	405,473
Savings deposits	542,379	504,321
Total core deposits	$ 2,832,235	$ 2,473,940
Time deposits:		
Less than $100,000	$ 227,521	$ 245,620
$100,000 or greater	626,110	673,918
Total time deposits	853,631	919,538
Total deposits	$ 3,685,866	$ 3,393,478

Interest expense on time deposits of $100,000 and over totaled $3.6 million and $4.8 million for the years ended December 31, 2012, and 2011, respectively.

At December 31, 2012, the maturity distribution of the Bank's time deposits was as follows:

Year of Maturity	$100,000 or Greater	Less Than $100,000	Total
		(In thousands)	
2013	$ 491,297	$ 195,457	$ 686,754
2014	90,217	20,833	111,050
2015	26,020	6,553	32,573
2016	10,272	2,117	12,389
2017	8,304	2,561	10,865
	$ 626,110	$ 227,521	$ 853,631

NOTE 9 – SECURITIES SOLD UNDER REPURCHASE AGREEMENTS

At December 31, 2012 and 2011, securities sold under repurchase agreements totaled $551.3 million and $556.0 million and carried weighted average interest rates of 0.19% and 0.20%, respectively. The securities underlying these agreements were U.S. Government agency obligations, state and municipal securities, and mortgage-backed securities with carrying values of $630.7 million and $665.6 million and fair values of $656.4 million and $692.6 million, at December 31, 2012 and 2011, respectively. The securities underlying these agreements are held by a custodian bank until the maturity of the agreement. The identical securities will be repurchased by the Bank.

The following summarizes the activity within the securities sold under repurchase agreements during the periods 2012 and 2011, respectively:

	2012	2011
Average outstanding	$ 563,144	$ 622,266
Weighted average interest rate	0.20%	0.25%
Maximum amounts outstanding	$ 644,975	$ 699,547

Substantially, all of the repurchase agreements have open-ended maturity, but either the customer or the Bank may terminate this repurchase agreement at any time upon written notice. All outstanding balances and pledged securities will be rebalanced and interest rates will reset daily to reflect market movement.

NOTE 10 – INCOME TAXES

The provision for income taxes for the years ended December 31, 2012 and 2011 is comprised of the following:

	2012	2011
	(In thousands)	
Current income taxes:		
Federal	$ 17,120	$ 26,608
State	8,183	7,915
Total current income tax expense	25,303	34,523
Deferred income taxes:		
Federal	2,709	(2,132)
State	844	(1,081)
Total deferred income tax expense (benefit)	3,553	(3,213)
Total income tax expense	$ 28,856	$ 31,310

NOTE 10 – Income Taxes, continued

Significant temporary differences that give rise to the deferred tax assets and liabilities as of December 31, 2012 and December 31, 2011 are as follows:

	2012	2011
	(In thousands)	
Deferred tax assets		
Allowance for loan losses	$ 24,362	$ 27,740
Depreciation and amortization	1,445	1,232
Gain/loss on sale of OREO	5,480	6,336
Other, net	885	-
Subtotal deferred tax assets	$ 32,172	$ 35,308
Valuation allowance	(658)	-
Total deferred tax assets	31,514	35,308
Deferred tax liabilities		
Discount accretion income	(35)	(35)
State income taxes	(31)	(262)
Fair value adjustments on securities available-for-sale	(5,388)	(6,418)
Other, net	-	(10)
Total deferred tax liabilities	$ (5,454)	$ (6,725)
Net deferred tax assets	$ 26,060	$ 28,583

The Federal tax rate was 35% for 2012 and 2011. A reconciliation of income tax expense and the amount computed by applying the statutory Federal income tax rate to income before income taxes follows:

	2012	2011
Federal income tax rate	35.0%	35.0%
State income taxes, net of Federal benefit	5.6%	5.2%
Tax exempt income	(4.3%)	(3.9%)
Tax credit	(5.5%)	(1.6%)
Other	0.4%	(0.1%)
	31.2%	34.6%

In assessing the realization of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent on the generation of future taxable income during the periods in which those temporary differences become deductible.

Based upon our taxpaying history and estimates of taxable income over the years in which the items giving rise to the deferred tax assets are deductible, management believes it is more likely than not that the Bank will realize the benefits of these deductible differences (except to the extent of the recorded valuation allowance). A valuation allowance has been provided for expected capital losses in California since management believes that these losses may not be utilized.

NOTE 10 – Income Taxes, continued

The Bank has adopted the provisions of ASC 740-10, *Accounting for Uncertainty in Income Taxes*, which prescribes the requirements for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The ASC 740-10 standard requires that all tax positions be assessed and to the extent the position is more likely than not to be sustained on its technical merits, a benefit be recognized based on the greatest amount that is more likely than not to be sustained.

Management's evaluation of tax positions was performed for those tax years which remain open to audit. As of December 31, 2012, all the federal and state returns filed since 2009 are subject to adjustment upon audit. The Bank may, from time to time, be assessed interest or penalties by taxing authorities, although any such assessments historically have been minimal and immaterial to our financial results. The Bank has concluded that there are no significant uncertain tax positions as of December 31, 2012.

NOTE 11 – EARNINGS PER SHARE

As of December 31, 2012 and 2011, there were no securities or other contracts to issue common stock. The table below is a reconciliation of the numerators and denominators used in the calculation of basic and diluted EPS for the years ended December 31, 2012 and 2011.

	2012	2011
	(In thousands, except share and per share data)	
Basic and diluted earnings per share:		
Net income available to common stockholders	$ 63,387	$ 59,118
Weighted average number of common shares outstanding	130,928	130,928
Weighted basic and diluted earnings per common share	$ 484.14	$ 451.53

NOTE 12 – COMMITMENTS AND CONTINGENCIES

Commitments to Extend Credit

In the normal course of business, the Bank has various outstanding commitments to extend credit that are not reflected in the accompanying financial statements. While the Bank does not anticipate material losses as a result of these transactions, commitments to extend credit are included in determining the appropriate level of the reserve for unfunded loan commitments.

Commitments to extend credit are agreements to lend to a customer, provided there is no violation of any condition established in the agreement. Substantially all of the Bank's commitments to extend credit are on a variable rate basis. Standby letters of credit are conditional commitments issued by the Bank to make payment on behalf of customers when certain specified future events occur. The customer is obligated to reimburse the Bank for any such payment. Most letters of credit expire within 1 year.

The Bank uses the same credit policies in making commitments to extend credit and in issuing standby letters of credit. Each customer's creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained is based on management's credit evaluation of the customer.

NOTE 12 – Commitments and Contingencies, continued

Commitments to Extend Credit, continued

The following table presents a summary of the Bank's commitments to extend credit as of the dates indicated:

	December 31,	
	2012	2011
	(In thousands)	
Commitments to extend credit	$ 463,074	$ 462,755
Financial standby letters of credit	8,201	19,685
Performance standby letters of credit	7,871	6,638
	$ 479,146	$ 489,078

Legal Matters

From time to time, the Bank is a defendant or plaintiff in various legal proceedings, including litigation arising in the ordinary course of its business. In the opinion of management, the ultimate disposition of these matters will not have a material effect on the Bank's financial position or results of operations and, as of December 31, 2012, the Bank is not a party to any material litigation.

NOTE 13 – FAIR VALUE MEASUREMENTS

FASB ASC 820, *Fair Value Measurements and Disclosures*, defines fair value, establishes a framework for measuring fair value including a three-level valuation hierarchy, and expands disclosures about fair value measurements. Fair value is defined as the exchange price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date reflecting assumptions that a market participant would use when pricing an asset or liability. The three-level inputs to measure the fair value of assets and liabilities are as follows:

Level 1 - Quoted prices for identical instruments that are highly liquid, observable and actively traded in over-the-counter markets. Level 1 financial instrument typically includes U.S. Treasury securities.

Level 2 - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable and can be corroborated by market data. Level 2 financial instruments typically include U.S. Government debt and agency mortgage-backed securities, municipal securities, corporate debt securities, impaired loans and other real estate owned ("OREO").

Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. This category typically includes impaired loans and OREO.

NOTE 13 – Fair Value Measurements, continued

The Bank uses the following methodologies to measure the fair value of its financial assets on a recurring and non-recurring basis:

Securities available-for-sale – Other than US Treasury which is a Level 1 measurement, the Bank measures all other securities by using quoted market prices for similar securities or dealer quotes, a Level 2 measurement.

Impaired loans - The Bank does not record loans at fair value on a recurring basis. However, from time to time, nonrecurring fair value adjustments to collateral-dependent impaired loans are recorded based on either current appraised value of the collateral, a Level 2 measurement, or management's judgment and estimation of value reported on appraisals which are adjusted based on recent market trends, a Level 3 measurement. The impaired loans categorized as Level 3 also include loans whose fair values are based on unobservable inputs such as cash flows discounted at the effective loan rate, management’s judgment or in the event when current appraised value was higher than the Bank’s book balance.

Other real estate owned - The fair value of OREO is generally based on third-party appraisals, which are reviewed and approved by the Bank's Credit Administration Department. OREO measured at fair value based on third-party appraisals or accepted written offers is classified in Level 2 in the fair value hierarchy. In certain circumstances, fair value may be determined using a combination of inputs including appraised values, broker price opinions and recent market activity. The weighing of each input in the calculation of fair value is based on management's assumptions regarding market conditions. These assumptions cannot be observed in the market. OREO measured at fair value using non-observable inputs is classified in Level 3 of the fair value hierarchy.

The following table presents the Bank’s hierarchy for its assets and liabilities measured at fair value on a recurring and non-recurring basis. These assets and liabilities are reported on the balance sheets at their fair values as of December 31, 2012 and December 31, 2011, respectively:

	As of December 31, 2012			
	Fair Value Measurements Using			Total at
	Level 1	Level 2	Level 3	Fair Value
	(In thousands)			
Assets				
On a recurring basis:				
Securities available-for-sale	$ 100	$ 629,955	$ -	$ 630,055
On a non-recurring basis:				
Impaired loans	-	9,183	2,559	11,742
Other real estate owned	-	8,012	1,049	9,061
Total assets	$ 100	$ 647,150	$ 3,608	$ 650,858

NOTE 13 – Fair Value Measurements, continued

	As of December 31, 2011			
	Fair Value Measurements Using			Total at
	Level 1	Level 2	Level 3	Fair Value
	(In thousands)			
Assets				
On a recurring basis:				
Securities available-for-sale	$ -	$ 548,289	$ -	$ 548,289
On a non-recurring basis:				
Impaired loans	-	25,555	20,691	46,246
Other real estate owned	-	6,977	4,814	11,791
Total assets	$ -	$ 580,821	$ 25,505	$ 606,326

NOTE 14 – FAIR VALUE OF FINANCIAL INSTRUMENTS

Financial instruments are defined under FASB ASC 825-50, *Financial Instruments-Disclosures,* as cash, evidence of an ownership in an entity, or a contract that conveys or imposes on an entity the contractual right or obligation to either receive or deliver cash or another financial instrument. A significant portion of the Bank's assets and liabilities are financial instruments as defined under FASB ASC 825-50.

The following presents a description of the Bank's financial instruments and the methodologies and assumptions used to estimate their fair value. Much of the information used to determine fair value is highly subjective. When applicable, readily available market information has been utilized. However, for a significant portion of the Bank's financial instruments, active markets do not exist. Therefore, considerable judgments were required in estimating fair value of certain items. The subjective factors include, among other things, the estimated timing and amount of cash flows, risk characteristics, credit quality and interest rates, all of which are subject to change. Since the fair value is estimated as of December 31, 2012 and 2011, the amounts that will actually be realized could be significantly different.

Cash and due from banks

The carrying value of cash and due from banks approximates the fair value because of the short maturity of such assets.

Securities Available-for-sale and Securities Held-to-maturity

The Bank used market quotes for similar or identical securities in an actively traded market to determine the fair values of securities available-for-sale and securities held-to-maturity as disclosed in Notes 2 and 3, respectively.

NOTE 14 – Fair Value of Financial Instruments, continued

Loans

Fair values were estimated for portfolios of loans with similar financial characteristics. Each loan category was further segmented into fixed and adjustable rate interest terms and by performing and nonperforming categories. The fair value of performing loans was calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest rate risk inherent in the loan. The entire allowance for loan losses was applied to classified loans including nonaccruals. Accordingly, they are considered to be carried at fair value as the allowance for loan losses represents the estimated discount for credit risk for the applicable loans.

Deposits

The fair value of demand deposits, savings and money market saving accounts represents the amount payable on demand at the reporting date. For fixed maturity time deposits, the fair value was estimated by discounting expected cash flows by the current offering rates of term deposits with similar maturities; However, since the bank's current interest rate is approximately at market, fixed maturity time deposits was determined to approximate the carrying value. In accordance with FASB ASC 825-10, *Financial Instruments-Overall* no value has been assigned to the Bank's long-term relationship with its deposit customers (core deposit intangibles) since it is not a financial instrument as defined under FASB ASC 825-10.

Securities Sold Under Repurchase Agreements

The fair value of securities sold under agreements to repurchase approximates carrying value due to the terms and nature of the obligations, where the interest rate will reset daily according to the market movement.

Off-Balance Sheet Financial Instruments

As the standby letters of credit and commitments to lend have terms that are consistent with current market terms, the Bank estimates that the fair value of the fees charged to enter into such agreements to be nominal.

NOTE 14 – Fair Value of Financial Instruments, continued

Off-Balance Sheet Financial Instruments, continued

The following table presents estimated fair value information for the Bank's financial instruments at December 31:

	2012		2011	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
	(In thousands)			
Financial Assets:				
Cash and due from banks	$ 314,001	$ 314,001	$ 335,919	$ 335,919
Securities available-for-sale	617,239	630,055	533,026	548,289
Securities held-to-maturity	1,942,085	2,015,916	1,564,841	1,633,061
Loans, net of allowance for loan losses	1,933,082	1,944,257	2,028,507	2,052,436
Financial Liabilities:				
Deposits:				
Non-interest bearing checking	$ 1,474,215	$ 1,474,215	$ 1,263,162	$ 1,263,162
Interest bearing checking	346,991	346,991	300,984	300,984
Savings and money market deposits	1,011,029	1,011,029	909,794	909,794
Time deposit	853,631	853,631	919,538	919,538
Securities sold under repurchase agreements	551,293	551,293	555,992	555,992

NOTE 15 – RELATED PARTY TRANSACTIONS

The Bank and Queen City Investments, Inc. ("Queen City"), which is the parent company of the Farmers & Merchants Trust Company of Long Beach (the "Trust Company."), may be considered affiliated parties as significant percentages of the outstanding shares of the Bank and Queen City are held by common shareholders, including by certain directors and/or executive officers of the Bank. In addition, certain executive and other officers of the Bank serve as officers and/or directors of Queen City Investments and/or its subsidiaries, including the Trust Company.

The Bank and the Trust Company have entered into an Employee Leasing Agreement whereby the Bank provides the Trust Company with the services of various Bank employees and in return the Trust Company pays fees to the Bank for such employee services. In 2012 and 2011, the Trust Company paid the Bank $559,000 and $435,000, respectively, under this arrangement. In addition, the Bank and the Trust Company have entered into an Exchange of Services Agreement for the exchange of various other services, which agreement provides for the periodic settlement between the parties of the differences in the values of respective services provided by one party to the other. Under this arrangement, the Bank provides administrative, accounting and data processing services as well as office space to the Trust Company and the Trust Company provides trustee and financial management services to the Bank and maintains deposits with the Bank. In 2012 the Trust Company paid the Bank $160,000 for the difference between the values of services exchanged between the parties in 2011, and in 2011 the Trust Company paid the Bank $143,000 for the difference between the values of services exchanged between the parties in 2010.

NOTE 15 – Related Party Transactions, continued

The Bank also leases a branch location from Queen City and pursuant to this lease, the Bank paid $388,000 and $294,000, respectively, in rent for each of the years ended December 31, 2012 and 2011.

At December 31, 2012 and December 31, 2011, no loans were outstanding with any affiliated party.

NOTE 16 – PROFIT-SHARING PLAN

The Bank has a noncontributory profit-sharing plan in which employees are eligible to participate at year-end if they have been employed for at least 1,000 hours during the year. The Bank contributed $3.9 million and $3.3 million to the profit-sharing plan in 2012 and 2011, respectively. At December 31, 2012 and December 31, 2011, no shares of the Bank's stock are held by the trust created by the plan.

NOTE 17 – REGULATORY MATTERS

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2012, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2012, the most recent notification from the Federal Reserve Bank categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized the Bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the following table. There are no conditions or events since that notification that management believes have changed the institution's category.

NOTE 17 – Regulatory Matters, continued

The Bank's actual regulatory capital amounts and ratios are also presented in the table.

	Actual		For Capital Adequacy Purposes:		To Be Well Capitalized Under Prompt Corrective Action Provisions:	
	Amount	Rate	Amount	Rate	Amount	Rate
			(Dollars in thousands)			
As of December 31, 2012:						
Total Capital (to Risk-Weighted Assets)	$ 741,402	29.61%	≥ $ 200,323	≥ 8.0%	≥ $ 250,404	≥ 10.0%
Tier 1 Capital (to Risk-Weighted Assets)	$ 709,832	28.35%	≥ $ 100,162	≥ 4.0%	≥ $ 150,242	≥ 6.0%
Tier 1 Capital (to Average Assets)	$ 709,832	14.24%	≥ $ 199,429	≥ 4.0%	≥ $ 249,286	≥ 5.0%

	Actual		For Capital Adequacy Purposes:		To Be Well Capitalized Under Prompt Corrective Action Provisions:	
	Amount	Rate	Amount	Rate	Amount	Rate
			(Dollars in thousands)			
As of December 31, 2011:						
Total Capital (to Risk-Weighted Assets)	$ 692,729	27.94%	≥ $ 198,365	≥ 8.0%	≥ $ 247,956	≥ 10.0%
Tier 1 Capital (to Risk-Weighted Assets)	$ 661,370	26.67%	≥ $ 99,182	≥ 4.0%	≥ $ 148,774	≥ 6.0%
Tier 1 Capital (to Average Assets)	$ 661,370	14.26%	≥ $ 185,476	≥ 4.0%	≥ $ 231,845	≥ 5.0%

NOTE 18 – SUBSEQUENT EVENTS

The Bank has evaluated events that have occurred subsequent to December 31, 2012, and through April 19, 2013, the date that these financial statements were issued. There have been no subsequent events that have occurred during the period that would require recognition in the consolidated financial statements or its disclosure in 2012.

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