WESTAMERICA BANCORPORATION
Form 10-Q
August 01, 2013
UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)
[x] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2013

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from __________ to __________.

Commission file number: 001-9383
WESTAMERICA BANCORPORATION
(Exact Name of Registrant as Specified in Its Charter)

CALIFORNIA	94-2156203
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

1108 FIFTH AVENUE, SAN RAFAEL, CALIFORNIA 94901
(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code (707) 863-6000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [x] No [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes [x] No [ ]

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

Large accelerated filer [x]	Accelerated filer [ ]	Non-accelerated filer [ ] (Do not check if a smaller reporting company)	Smaller reporting company [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [x]

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date:

Title of Class	Shares outstanding as of July 23, 2013
Common Stock, No Par Value	26,771,525

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FORWARD-LOOKING STATEMENTS

This report on Form 10-Q contains forward-looking statements about Westamerica Bancorporation for which it claims the protection of the safe harbor provisions contained in the Private Securities Litigation Reform Act of 1995. Examples of forward-looking statements include, but are not limited to: (i) projections of revenues, expenses, income or loss, earnings or loss per share, the payment or nonpayment of dividends, capital structure and other financial items; (ii) statements of plans, objectives and expectations of the Company or its management or board of directors, including those relating to products or services; (iii) statements of future economic performance; and (iv) statements of assumptions underlying such statements. Words such as "believes", "anticipates", "expects", "intends", "targeted", "projected", "continue", "remain", "will", "should", "may" and other similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

These forward-looking statements are based on Management’s current knowledge and belief and include information concerning the Company’s possible or assumed future financial condition and results of operations. A number of factors, some of which are beyond the Company’s ability to predict or control, could cause future results to differ materially from those contemplated. These factors include but are not limited to (1) the length and severity of current and potential future difficulties in the global, national and California economies and the effects of government efforts to address those difficulties; (2) liquidity levels in capital markets; (3) fluctuations in asset prices including, but not limited to stocks, bonds, real estate, and commodities; (4) the effect of acquisitions and integration of acquired businesses; (5) economic uncertainty created by terrorist threats and attacks on the United States, the actions taken in response, and the uncertain effect of these events on the national and regional economies; (6) changes in the interest rate environment; (7) changes in the regulatory environment; (8) competitive pressure in the banking industry; (9) operational risks including data processing system failures or fraud; (10) volatility of interest rate sensitive loans, deposits and investments; (11) asset/liability management risks and liquidity risks; (12) the effect of natural disasters, including earthquakes, fire, flood, drought, and other disasters, on the uninsured value of loan collateral, the financial condition of debtors and issuers of investment securities, the economic conditions affecting the Company’s market place, and commodities and asset values, and (13) changes in the securities markets. The reader is directed to the Company's annual report on Form 10-K for the year ended December 31, 2012, for further discussion of factors which could affect the Company's business and cause actual results to differ materially from those expressed in any forward-looking statement made in this report. The Company undertakes no obligation to update any forward-looking statements in this report.

PART I - FINANCIAL INFORMATION
Item 1 Financial Statements

WESTAMERICA BANCORPORATION
CONSOLIDATED BALANCE SHEETS
(unaudited)

	At June 30, 2013	At December 31, 2012
	(In thousands)	
Assets:		
Cash and due from banks	$384,276	$ 491,382
Investment securities available for sale	1,004,888	825,636
Investment securities held to maturity, with fair values of: $1,124,946 at June 30, 2013 and $1,184,557 at December 31, 2012	1,134,615	1,156,041
Purchased covered loans	324,976	372,283
Purchased non-covered loans	61,062	74,891
Originated loans	1,553,303	1,664,183
Allowance for loan losses	(30,926)	(30,234)
Total loans	1,908,415	2,081,123
Non-covered other real estate owned	8,957	12,661
Covered other real estate owned	10,480	13,691
Premises and equipment, net	38,267	38,639
Identifiable intangibles, net	20,877	23,261
Goodwill	121,673	121,673
Other assets	181,460	188,086
Total Assets	$4,813,908	$ 4,952,193
Liabilities:		
Noninterest bearing deposits	$1,644,151	$ 1,676,071
Interest bearing deposits	2,457,243	2,556,421
Total deposits	4,101,394	4,232,492
Short-term borrowed funds	66,640	53,687
Federal Home Loan Bank advances	25,687	25,799
Term repurchase agreement	10,000	10,000
Debt financing	15,000	15,000
Other liabilities	50,565	55,113
Total Liabilities	4,269,286	4,392,091
Shareholders' Equity:		
Common stock (no par value), authorized - 150,000 shares Issued and outstanding: 26,769 at June 30, 2013 and 27,213 at December 31, 2012	371,498	372,012
Deferred compensation	2,711	3,101
Accumulated other comprehensive income	4,524	14,625
Retained earnings	165,889	170,364
Total Shareholders' Equity	544,622	560,102
Total Liabilities and Shareholders' Equity	$4,813,908	$ 4,952,193

See accompanying notes to unaudited consolidated financial statements.

WESTAMERICA BANCORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(unaudited)

	For the Three Months		For the Six Months	
	Ended June 30,			
	2013	2012	2013	2012
	(In thousands, except per share data)			
Interest and Fee Income:				
Loans	$26,180	$33,745	$53,579	$69,401
Investment securities available for sale	5,532	4,938	10,868	9,726
Investment securities held to maturity	7,557	8,218	15,287	16,072
Total Interest and Fee Income	39,269	46,901	79,734	95,199
Interest Expense:				
Deposits	847	1,107	1,746	2,294
Short-term borrowed funds	26	21	37	48
Term repurchase agreement	25	24	49	49
Federal Home Loan Bank advances	120	119	238	239
Debt financing	201	201	401	401
Total Interest Expense	1,219	1,472	2,471	3,031
Net Interest Income	38,050	45,429	77,263	92,168
Provision for Loan Losses	1,800	2,800	4,600	5,600
Net Interest Income After Provision For Loan Losses	36,250	42,629	72,663	86,568
Noninterest Income:				
Service charges on deposit accounts	6,452	7,027	12,994	14,122
Merchant processing services	2,413	2,529	4,822	4,922
Debit card fees	1,478	1,345	2,836	2,508
ATM processing fees	721	932	1,426	1,865
Trust fees	585	497	1,153	986
Financial services commissions	284	194	464	365
Loss on sale of securities	-	(1,287)	-	(1,287)
Other	2,351	2,296	4,867	4,721
Total Noninterest Income	14,284	13,533	28,562	28,202
Noninterest Expense:				
Salaries and related benefits	14,064	14,494	28,467	29,540
Occupancy	3,638	3,775	7,524	7,709
Outsourced data processing services	2,140	2,078	4,297	4,161
Amortization of identifiable intangibles	1,165	1,339	2,384	2,741
Furniture and equipment	1,021	1,041	1,901	1,892
Professional fees	745	902	1,380	1,669
Courier service	737	793	1,478	1,578
Other real estate owned	278	3	612	233
Other	4,404	4,924	8,826	9,860
Total Noninterest Expense	28,192	29,349	56,869	59,383
Income Before Income Taxes	22,342	26,813	44,356	55,387
Provision for income taxes	5,230	5,849	9,973	13,418
Net Income	$17,112	$20,964	$34,383	$41,969
Average Common Shares Outstanding	26,890	27,744	27,017	27,897
Diluted Average Common Shares Outstanding	26,898	27,790	27,027	27,951
Per Common Share Data:				

Basic earnings	$0.64	$0.76	$1.27	$1.50
Diluted earnings	0.64	0.75	1.27	1.50
Dividends paid	0.37	0.37	0.74	0.74

See accompanying notes to unaudited consolidated financial statements.

WESTAMERICA BANCORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(unaudited)

	For the Three Months		For the Six Months	
	Ended June 30,			
	2013	2012	2013	2012
	(In thousands)			
Net Income	$17,112	$20,964	$34,383	$41,969
Other comprehensive (loss) income:				
(Decrease) increase in net unrealized gains on securities available for sale	(18,733)	1,451	(17,461)	2,835
Deferred tax benefit (expense)	7,876	(610)	7,342	(1,192)
(Decrease) increase in net unrealized gains on securities available for sale, net of tax	(10,857)	841	(10,119)	1,643
Post-retirement benefit transition obligation amortization	15	15	30	30
Deferred tax expense	(6)	(6)	(12)	(12)
Post-retirement benefit transition obligation amortization, net of tax	9	9	18	18
Total Other Comprehensive (Loss) Income	(10,848)	850	(10,101)	1,661
Total Comprehensive Income	$6,264	$21,814	$24,282	$43,630

See accompanying notes to unaudited consolidated financial statements.

WESTAMERICA BANCORPORATION
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(unaudited)

	Common Shares Outstanding	Common Stock	Accumulated Deferred Compensation	Accumulated Other Comprehensive Income	Retained Earnings	Total
	(In thousands)					
Balance, December 31, 2011	28,150	$ 377,775	$ 3,060	$ 11,369	$ 166,437	$558,641
Net income for the period					41,969	41,969
Other comprehensive income				1,661		1,661
Exercise of stock options	25	1,030				1,030
Tax benefit increase upon exercise of stock options		2				2
Restricted stock activity	11	482	41			523
Stock based compensation		805				805
Stock awarded to employees	1	63				63
Purchase and retirement of stock	(566)	(7,526)			(18,555)	(26,081)
Dividends					(20,687)	(20,687)
Balance, June 30, 2012	27,621	$ 372,631	$ 3,101	$ 13,030	$ 169,164	$557,926
Balance, December 31, 2012	27,213	$ 372,012	$ 3,101	$ 14,625	$ 170,364	$560,102
Net income for the period					34,383	34,383
Other comprehensive loss				(10,101)		(10,101)
Exercise of stock options	157	6,414				6,414
Tax benefit decrease upon exercise of stock options		(201)				(201)
Restricted stock activity	15	1,068	(390)			678
Stock based compensation		730				730
Stock awarded to employees	1	61				61
Purchase and retirement of stock	(617)	(8,586)			(18,807)	(27,393)
Dividends					(20,051)	(20,051)
Balance, June 30, 2013	26,769	$ 371,498	$ 2,711	$ 4,524	$ 165,889	$544,622

See accompanying notes to unaudited consolidated financial statements.

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WESTAMERICA BANCORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	For the Six Months Ended June 30, 2013	2012
	(In thousands)	
Operating Activities:		
Net income	$34,383	$41,969
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	9,032	7,037
Loan loss provision	4,600	5,600
Net amortization of deferred loan fees	(202)	(303)
Decrease in interest income receivable	88	1,004
Increase in net deferred tax asset	(2,644)	(6,275)
Decrease (increase) in other assets	8,174	(3,386)
Stock option compensation expense	730	805
Tax benefit decrease (increase) upon exercise of stock options	201	(2)
Increase (decrease) in income taxes payable	30	(1,186)
Increase (decrease) in interest expense payable	9	(129)
(Decrease) increase in other liabilities	(5,482)	2,160
Loss on sale of securities available for sale	-	1,287
Gain on sale of other assets	(548)	(256)
Net loss on sale of premises and equipment	9	1
Originations of mortgage loans for resale	(240)	(27)
Proceeds from sale of mortgage loans originated for resale	241	28
Net gain on sale of foreclosed assets	(556)	(2,041)
Writedown of foreclosed assets	1,062	1,925
Net Cash Provided by Operating Activities	48,887	48,211
Investing Activities:		
Net repayments of loans	167,500	194,740
Proceeds from FDIC1 loss-sharing indemnification	4,039	20,259
Purchases of investment securities available for sale	(275,460)	(137,378)
Proceeds from sale/maturity/calls of securities available for sale	77,558	70,249
Purchases of investment securities held to maturity	(87,643)	(405,281)
Proceeds from maturity/calls of securities held to maturity	107,428	106,080
Purchases of premises and equipment	(1,110)	(2,637)
Net change in FRB2/FHLB3 securities	1,488	895
Proceeds from sale of foreclosed assets	9,401	16,632
Net Cash Provided by (Used in) Investing Activities	3,201	(136,441)
Financing Activities:		
Net change in deposits	(130,915)	(41,048)
Net change in short-term borrowings and FHLB3 advances	12,952	(34,106)
Exercise of stock options	6,414	1,030
Tax benefit (decrease) increase upon exercise of stock options	(201)	2
Retirement of common stock including repurchases	(27,393)	(26,081)
Common stock dividends paid	(20,051)	(20,687)

Net Cash Used in Financing Activities	(159,194)	(120,890)
Net Change In Cash and Due from Banks	(107,106)	(209,120)
Cash and Due from Banks at Beginning of Period	491,382	530,045
Cash and Due from Banks at End of Period	$384,276	$320,925
Supplemental Cash Flow Disclosures:		
Supplemental disclosure of non cash activities:		
Loan collateral transferred to other real estate owned	$3,932	$4,108
Supplemental disclosure of cash flow activities:		
Interest paid for the period	2,722	3,602
Income tax payments for the period	12,779	21,631

See accompanying notes to unaudited consolidated financial statements.

1 Federal Deposit Insurance Corporation ("FDIC")

2 Federal Reserve Bank ("FRB")

3 Federal Home Loan Bank ("FHLB")

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1: Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. The results of operations reflect interim adjustments, all of which are of a normal recurring nature and which, in the opinion of Management, are necessary for a fair presentation of the results for the interim periods presented. The interim results for the three and six months ended June 30, 2013 and 2012 are not necessarily indicative of the results expected for the full year. These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes as well as other information included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012.

The Company has evaluated events and transactions subsequent to the balance sheet date. Based on this evaluation, the Company is not aware of any events or transactions that occurred subsequent to the balance sheet date but prior to filing that would require recognition or disclosure in its unaudited consolidated financial statements.

Note 2: Accounting Policies

The Company’s accounting policies are discussed in Note 1 to the audited consolidated financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012. Certain amounts in prior periods have been reclassified to conform to the current presentation.

Certain accounting policies underlying the preparation of these financial statements require Management to make estimates and judgments. These estimates and judgments may significantly affect reported amounts of assets and liabilities, revenues and expenses, and disclosures of contingent assets and liabilities. Management exercises judgment to estimate the appropriate level of the allowance for credit losses, the acquisition date fair value of purchased loans, and the evaluation of other than temporary impairment of investment securities, which are discussed in the Company’s accounting policies.

Recently Adopted Accounting Standards

FASB ASU 2012-06, Subsequent Accounting for an Indemnification Asset Recognized at the Acquisition Date as a Result of a Government-Assisted Acquisition of a Financial Institution, was issued October 2012 to provide guidance for consistently measuring an indemnification asset subsequent to acquisition. Subsequent accounting for changes in the measurement of the indemnification asset should be on the same basis as a change in the assets subject to indemnification. Any amortization of changes in value is limited to the shorter of the contractual term of the indemnification agreement or the remaining life of the indemnified assets. The Company’s historical accounting treatment is consistent with ASU 2012-06, therefore there was no effect on the Company’s financial statements at January 1, 2013, when adopted.

FASB ASU 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income, was issued February 2013 requiring an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. The adoption of the update did not have a material effect on the Company’s financial statements at January 1, 2013, the date adopted. The

Company's only item reclassified out of other comprehensive income to net income is the amortization of unrecognized post retirement benefit transition obligation, which is immaterial for purposes of disclosure.

Note 3: Investment Securities

The amortized cost, unrealized gains and losses accumulated in other comprehensive income, and fair value of investment securities available for sale follows:

	Investment Securities Available for Sale At June 30, 2013			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
U.S. Treasury securities	$3,511	$ 23	$ -	$3,534
Securities of U.S. Government sponsored entities	38,699	49	(367)	38,381
Residential mortgage-backed securities	39,532	2,089	(11)	41,610
Commercial mortgage-backed securities	3,716	73	-	3,789
Obligations of States and political subdivisions	191,367	7,338	(278)	198,427
Residential collateralized mortgage obligations	285,670	918	(8,790)	277,798
Asset-backed securities	15,328	-	(125)	15,203
FHLMC (1) and FNMA (2) stock	824	7,204	-	8,028
Corporate securities	416,108	2,279	(3,074)	415,313
Other securities	2,049	888	(132)	2,805
Total	$996,804	$ 20,861	$ (12,777)	$1,004,888

(1) Federal Home Loan Mortgage Corporation
(2) Federal National Mortgage Association

The amortized cost, unrealized gains and losses, and fair value of investment securities held to maturity follows:

	Investment Securities Held to Maturity At June 30, 2013			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
Securities of U.S. Government sponsored entities	$2,256	$ 10	$ -	$2,266
Residential mortgage-backed securities	64,404	986	(488)	64,902
Obligations of States and political subdivisions	723,096	9,146	(18,155)	714,087
Residential collateralized mortgage obligations	344,859	1,459	(2,627)	343,691
Total	$1,134,615	$ 11,601	$ (21,270)	$1,124,946

The amortized cost, unrealized gains and losses accumulated in other comprehensive income, and fair value of investment securities available for sale follows:

	Investment Securities Available for Sale At December 31, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
U.S. Treasury securities	$3,520	$ 38	$ -	$ 3,558
Securities of U.S. Government sponsored entities	49,335	207	(17)	49,525
Residential mortgage-backed securities	53,078	3,855	(1)	56,932
Commercial mortgage-backed securities	4,076	69	-	4,145
Obligations of States and political subdivisions	200,769	14,730	(252)	215,247
Residential collateralized mortgage obligations	219,613	1,786	(294)	221,105
Asset-backed securities	16,130	18	(143)	16,005
FHLMC and FNMA stock	824	2,061	(5)	2,880
Corporate securities	250,655	3,009	(826)	252,838
Other securities	2,091	1,370	(60)	3,401
Total	$800,091	$ 27,143	$ (1,598)	$ 825,636

The amortized cost, unrealized gains and losses, and fair value of investment securities held to maturity follows:

	Investment Securities Held to Maturity At December 31, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
Securities of U.S. Government sponsored entities	$3,232	$ 43	$ -	$3,275
Residential mortgage-backed securities	72,807	2,090	(10)	74,887
Obligations of States and political subdivisions	680,802	23,004	(1,235)	702,571
Residential collateralized mortgage obligations	399,200	5,185	(561)	403,824
Total	$1,156,041	$ 30,322	$ (1,806)	$1,184,557

The amortized cost and fair value of investment securities by contractual maturity are shown in the following tables at the dates indicated:

	At June 30, 2013			
	Securities Available for Sale		Securities Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)			
Maturity in years:				
1 year or less	$69,203	$69,604	$ 11,182	$ 11,441
Over 1 to 5 years	426,099	425,485	162,937	166,079
Over 5 to 10 years	71,015	72,718	282,150	281,073
Over 10 years	98,696	103,051	269,083	257,760
Subtotal	665,013	670,858	725,352	716,353
Mortgage-backed securities and residential collateralized mortgage obligations	328,918	323,197	409,263	408,593
Other securities	2,873	10,833	-	-

Total	$996,804	$1,004,888	$ 1,134,615	$ 1,124,946

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	At December 31, 2012			
	Securities Available for Sale		Securities Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)			
Maturity in years:				
1 year or less	$40,380	$ 40,686	$ 10,265	$ 10,496
Over 1 to 5 years	309,293	312,480	167,162	171,769
Over 5 to 10 years	59,817	63,540	227,603	236,608
Over 10 years	110,919	120,467	279,004	286,973
Subtotal	520,409	537,173	684,034	705,846
Mortgage-backed securities and residential collateralized mortgage obligations	276,767	282,182	472,007	478,711
Other securities	2,915	6,281	-	-
Total	$800,091	$ 825,636	$ 1,156,041	$ 1,184,557

Expected maturities of mortgage-backed securities can differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call or prepayment penalties. In addition, such factors as prepayments and interest rates may affect the yield on the carrying value of mortgage-backed securities. At June 30, 2013 and December 31, 2012, the Company had no high-risk collateralized mortgage obligations as defined by regulatory guidelines.

An analysis of gross unrealized losses of investment securities available for sale follows:

	Investment Securities Available for Sale At June 30, 2013					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)					
Securities of U.S. Government sponsored entities	$24,507	$ (367)	$-	$ -	$24,507	$ (367)
Residential mortgage-backed securities	18	-	868	(11)	886	(11)
Obligations of States and political subdivisions	9,893	(141)	5,756	(137)	15,649	(278)
Residential collateralized mortgage obligations	250,865	(8,790)	1	-	250,866	(8,790)
Asset-backed securities	10,108	(10)	5,095	(115)	15,203	(125)
Corporate securities	218,697	(2,715)	32,548	(359)	251,245	(3,074)
Other securities	-	-	1,868	(132)	1,868	(132)
Total	$514,088	$ (12,023)	$46,136	$ (754)	$560,224	$ (12,777)

An analysis of gross unrealized losses of investment securities held to maturity follows:

	Investment Securities Held to Maturity At June 30, 2013					
	Less than 12 months		12 months or longer		Total	
		Unrealized		Unrealized		Unrealized

	Fair Value	Losses	Fair Value	Losses	Fair Value	Losses
			(In thousands)			
Residential mortgage-backed securities	$33,116	$ (360)	$7,561	$ (128)	$40,677	$ (488)
Obligations of States and political subdivisions	338,807	(17,765)	9,307	(390)	348,114	(18,155)
Residential collateralized mortgage obligations	208,216	(2,360)	16,418	(267)	224,634	(2,627)
Total	$580,139	$ (20,485)	$33,286	$ (785)	$613,425	$ (21,270)

The unrealized losses on the Company's investment securities were caused by market conditions for these types of investments particularly interest rates which rose between December 31, 2012 and June 30, 2013, causing bond prices to decline. The Company evaluates securities on a quarterly basis including changes in security ratings issued by ratings agencies, changes in the financial condition of the issuer, and, for mortgage-related and asset-backed securities, delinquency and loss information with respect to the underlying collateral, changes in the levels of subordination for the Company's particular position within the repayment structure, and remaining credit enhancement as compared to expected credit losses of the security. Substantially all of these securities continue to be investment grade rated by one or more major rating agencies. In addition to monitoring credit rating agency evaluations, Management performs its own evaluations regarding the credit worthiness of the issuer or the securitized assets underlying asset backed securities.

The Company does not intend to sell any investments and has concluded that it is more likely than not that it will not be required to sell the investments prior to recovery of the amortized cost basis. Therefore, the Company does not consider these investments to be other-than-temporarily impaired as of June 30, 2013.

The fair values of the investment securities could decline in the future if the general economy deteriorates, credit ratings decline, the issuer's financial condition deteriorates, or the liquidity for securities declines. As a result, other than temporary impairments may occur in the future.

As of June 30, 2013, $815,646 thousand of investment securities were pledged to secure public deposits, short-term borrowed funds, and term repurchase agreements, compared to $850,421 thousand at December 31, 2012.

An analysis of gross unrealized losses of investment securities available for sale follows:

	Investment Securities Available for Sale 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)					
Securities of U.S. Government sponsored entities	$9,983	$ (17)	$-	$ -	$9,983	$ (17)
Residential mortgage-backed securities	103	(1)	11	-	114	(1)
Residential collateralized mortgage obligations	72,803	(294)	-	-	72,803	(294)
Obligations of States and political subdivisions	2,080	(23)	8,928	(229)	11,008	(252)
Asset-backed securities	-	-	5,828	(143)	5,828	(143)
FHLMC and FNMA stock	-	-	1	(5)	1	(5)
Corporate securities	53,570	(423)	24,597	(403)	78,167	(826)
Other securities	-	-	1,940	(60)	1,940	(60)
Total	$138,539	$ (758)	$41,305	$ (840)	$179,844	$ (1,598)

An analysis of gross unrealized losses of investment securities held to maturity follows:

	Investment Securities Held to Maturity 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)					
Residential mortgage-backed securities	$113	$ -	$664	$ (10)	$777	$ (10)
Residential collateralized mortgage obligations	26,683	(386)	9,353	(175)	36,036	(561)
Obligations of States and political subdivisions	69,839	(1,205)	4,275	(30)	74,114	(1,235)
Total	$96,635	$ (1,591)	$14,292	$ (215)	$110,927	$ (1,806)

During the second quarter 2012, the Company transferred one residential collateralized mortgage obligation with a carrying value of $9,077 thousand from the held to maturity portfolio to the available for sale portfolio. The residential collateralized mortgage obligation was subsequently sold due to a decline in the credit worthiness from increased losses on subordinate tranches resulting in proceeds of $7,790 thousand and a realized loss on sale of $1,287 thousand during the quarter.

The following table provides information about the amount of interest income from taxable and non-taxable investment securities:

	For the Three Months		For the Six Months	
	Ended June 30,			
	2013	2012	2013	2012
	(In thousands)			
Taxable:				
Mortgage related securities	$3,371	$3,713	$6,933	$7,076
Other	2,220	1,635	4,192	2,962
Total taxable	5,591	5,348	11,125	10,038
Tax-exempt	7,498	7,808	15,030	15,760
Total interest income from investment securities	$13,089	$13,156	$26,155	$25,798

Note 4: Loans and Allowance for Credit Losses

A summary of the major categories of loans outstanding is shown in the following table.

	At June 30, 2013					
	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment & Other	Total
	(In thousands)					
Originated loans	$309,621	$ 614,005	$ 8,015	$ 195,322	$ 426,340	$1,553,303
Purchased covered loans:						
Impaired	284	6,211	1,649	-	254	8,398
Non impaired	42,386	220,054	4,805	9,280	58,567	335,092
Purchase discount	(5,058)	(11,597)	(99)	(434)	(1,326)	(18,514)
Purchased non-covered loans:						
Impaired	660	2,621	-	-	198	3,479
Non impaired	8,170	34,758	1,330	1,015	15,919	61,192
Purchase discount	(876)	(1,002)	-	(262)	(1,469)	(3,609)
Total	$355,187	$ 865,050	$ 15,700	$ 204,921	$ 498,483	$1,939,341

	At December 31, 2012					
	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment & Other	Total
	(In thousands)					
Originated loans	$340,116	$ 632,927	$ 7,984	$ 222,458	$ 460,698	$1,664,183
Purchased covered loans:						
Impaired	308	7,585	1,824	-	257	9,974
Non impaired	59,135	247,534	5,462	9,374	66,932	388,437
Purchase discount	(8,459)	(15,140)	(279)	(433)	(1,817)	(26,128)
Purchased non-covered loans:						
Impaired	1,261	6,763	-	-	297	8,321
Non impaired	9,840	38,673	1,619	3,110	18,554	71,796
Purchase discount	(870)	(1,748)	(95)	(474)	(2,039)	(5,226)

Total	$401,331	$ 916,594	$ 16,515	$ 234,035	$ 542,882	$2,111,357

Changes in the carrying amount of impaired purchased covered loans were as follows:

Impaired purchased covered loans	For the Six Months Ended June 30, 2013	For the Year Ended December 31, 2012
	(In thousands)	
Carrying amount at the beginning of the period	$ 7,865	$ 18,591
Reductions during the period	(605)	(10,726)
Carrying amount at the end of the period	$ 7,260	$ 7,865

Changes in the carrying amount of impaired purchased non-covered loans were as follows:

Impaired purchased non-covered loans	For the Six Months Ended June 30, 2013	For the Year Ended December 31, 2012
	(In thousands)	
Carrying amount at the beginning of the period	$ 6,764	$ 15,572
Reductions during the period	(4,166)	(8,808)
Carrying amount at the end of the period	$ 2,598	$ 6,764

Changes in the accretable yield for purchased loans were as follows:

Accretable yield:	For the Six Months Ended June 30, 2013	For the Year Ended December 31, 2012
	(In thousands)	
Balance at the beginning of the period	$ 4,948	$ 9,990
Reclassification from nonaccretable difference	8,864	12,121
Accretion	(7,363)	(17,163)
Disposals and other	-	-
Balance at the end of the period	$ 6,449	$ 4,948
Accretion	$ (7,363)	$ (17,163)
Reduction in FDIC indemnification asset	5,759	13,207
(Increase) in interest income	$ (1,604)	$ (3,956)

The following summarizes activity in the allowance for credit losses:

Allowance for Credit Losses For the Three Months Ended June 30, 2013								
Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Purchased Non-covered Loans	Purchased Covered Loans	Unallocated	Total

	(In thousands)								
Allowance for loan losses:									
Balance at beginning of period	$5,536	$10,965	$480	$539	$2,768	$-	$738	$9,328	$30,354
Additions:									
Provision	(1,301)	660	(2)	15	225	116	46	2,041	1,800
Deductions:									
Chargeoffs	(148)	(427)	-	(22)	(896)	(116)	(517)	-	(2,126
Recoveries	297	77	-	-	506	-	18	-	898
Net loan recoveries (losses)	149	(350)	-	(22)	(390)	(116)	(499)	-	(1,228
Balance at end of period	4,384	11,275	478	532	2,603	-	285	11,369	30,926
Liability for off-balance sheet credit exposure	1,698	1	127	-	473	-	-	394	2,693
Total allowance for credit losses	$6,082	$11,276	$605	$532	$3,076	$-	$285	$11,763	$33,619

Allowance for Credit Losses
For the Six Months Ended June 30, 2013

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Purchased Non-covered Loans	Purchased Covered Loans	Unallocated	Tot
	(In thousands)								
Allowance for loan losses:									
Balance at beginning of period	$6,445	$10,063	$484	$380	$3,194	$-	$1,005	$8,663	$30,2
Additions:									
Provision	(770)	1,653	(6)	261	507	116	133	2,706	4,60
Deductions:									
Chargeoffs	(2,050)	(539)	-	(109)	(2,205)	(116)	(876)	-	(5,8
Recoveries	759	98	-	-	1,107	-	23	-	1,98
Net loan losses	(1,291)	(441)	-	(109)	(1,098)	(116)	(853)	-	(3,9
Balance at end of period	4,384	11,275	478	532	2,603	-	285	11,369	30,9
Liability for off-balance sheet credit exposure	1,698	1	127	-	473	-	-	394	2,69
Total allowance for credit losses	$6,082	$11,276	$605	$532	$3,076	$-	$285	$11,763	$33,6

Allowance for Credit Losses
For the Three Months Ended June 30, 2012

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Purchased Non-covered Loans	Purchased Covered Loans	Unallocated	Total
	(In thousands)								
Allowance for loan losses:									
Balance at beginning of period	$6,814	$11,427	$2,755	$645	$2,825	$-	$139	$7,278	$31,883
Additions:									
Provision	1,984	(1,561)	(270)	19	817	25	324	1,462	2,800
Deductions:									
Chargeoffs	(2,696)	-	-	(62)	(1,211)	(25)	(247)	-	(4,241
Recoveries	228	33	196	-	600	-	24	-	1,081
Net loan (losses) recoveries	(2,468)	33	196	(62)	(611)	(25)	(223)	-	(3,160
Balance at end of period	6,330	9,899	2,681	602	3,031	-	240	8,740	31,523
Liability for off-balance sheet credit exposure	1,644	16	12	-	384	-	-	637	2,693
Total allowance for credit losses	$7,974	$9,915	$2,693	$602	$3,415	$-	$240	$9,377	$34,216

Allowance for Credit Losses
For the Six Months Ended June 30, 2012

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Purchased Non-covered Loans	Purchased Covered Loans	Unallocated	Tota
	(In thousands)								
Allowance for loan losses:									
Balance at beginning of period	$6,012	$10,611	$2,342	$781	$3,072	$-	$-	$9,779	$32,5
Additions:									
Provision	3,259	203	141	753	1,444	25	814	(1,039)	5,60
Deductions:									

Chargeoffs	(3,558)	(948)	-	(932)	(2,864)	(25)	(612)	-	(8,9
Recoveries	617	33	198	-	1,379	-	38	-	2,26
Net loan (losses) recoveries	(2,941)	(915)	198	(932)	(1,485)	(25)	(574)	-	(6,6
Balance at end of period	6,330	9,899	2,681	602	3,031	-	240	8,740	31,5
Liability for off-balance sheet credit exposure	1,644	16	12	-	384	-	-	637	2,69
Total allowance for credit losses	$7,974	$9,915	$2,693	$602	$3,415	$-	$240	$9,377	$34,2

The recorded investment in loans evaluated for impairment follows:

	Allowance for Credit Losses and Recorded Investment in Loans Evaluated for Impa At June 30, 2013						
	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Purchased Non-covered Loans	Purcha Cove Loa
	(In thousands)						
Allowance for credit losses:							
Individually evaluated for impairment	$100	$-	$-	$-	$-	$-	$147
Collectively evaluated for impairment	5,982	11,276	605	532	3,076	-	138
Purchased loans with evidence of credit deterioration	-	-	-	-	-	-	-
Total	$6,082	$11,276	$605	$532	$3,076	$-	$285
Carrying value of loans:							
Individually evaluated for impairment	$2,496	$4,421	$-	$-	$-	$3,990	$15,1
Collectively evaluated for impairment	307,125	609,584	8,015	195,322	426,340	54,474	302,
Purchased loans with evidence of credit deterioration	-	-	-	-	-	2,598	7,26
Total	$309,621	$614,005	$8,015	$195,322	$426,340	$61,062	$324,

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Allowance for Credit Losses and
Recorded Investment in Loans Evaluated for Impai
At December 31, 2012

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Purchased Non-covered Loans	Purcha Cove Loa
					(In thousands)		
Allowance for credit losses:							
Individually evaluated for impairment	$1,865	$134	$-	$-	$-	$-	$753
Collectively evaluated for impairment	6,314	9,938	484	380	3,613	-	252
Purchased loans with evidence of credit deterioration	-	-	-	-	-	-	-
Total	$8,179	$10,072	$484	$380	$3,613	$-	$1,00
Carrying value of loans:							
Individually evaluated for impairment	$5,153	$4,161	$-	$-	$-	$3,029	$16,6
Collectively evaluated for impairment	334,963	628,766	7,984	222,458	460,698	65,098	347,
Purchased loans with evidence of credit deterioration	-	-	-	-	-	6,764	7,86
Total	$340,116	$632,927	$7,984	$222,458	$460,698	$74,891	$372,

The Bank's customers are small businesses, professionals and consumers. Given the scale of these borrowers, corporate credit rating agencies do not evaluate the borrowers' financial condition. The Bank maintains a Loan Review Department which reports directly to the Board of Directors. The Loan Review Department performs independent evaluations of loans and assigns credit risk grades to evaluated loans using grading standards employed by bank regulatory agencies. Loans judged to carry lower-risk attributes are assigned a "pass" grade, with a minimal likelihood of loss. Loans judged to carry higher-risk attributes are referred to as "classified loans," and are further disaggregated, with increasing expectations for loss recognition, as "substandard," "doubtful," and "loss." Loan Review evaluations occur every calendar quarter. If the Bank becomes aware of deterioration in a borrower's performance or financial condition between Loan Review examinations, assigned risk grades will be re-evaluated promptly. Credit risk grades assigned by the Loan Review Department are subject to review by the Bank's regulatory authority during regulatory examinations.

The following summarizes the credit risk profile by internally assigned grade:

Credit Risk Profile by Internally Assigned Grade
At June 30, 2013

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Purchased Non-covered Loans	Purchased Covered Loans (1)	Total
				(In thousands)				
Grade:								
Pass	$297,214	$ 568,854	$ 7,557	$ 192,790	$ 424,989	$ 44,635	$ 227,835	$1,763,874
Substandard	10,271	45,151	458	2,532	1,137	19,049	115,255	193,853
Doubtful	2,136	-	-	-	8	987	350	3,481
Loss	-	-	-	-	206	-	50	256
Default risk purchase discount	-	-	-	-	-	(3,609)	(18,514)	(22,123)
Total	$309,621	$ 614,005	$ 8,015	$ 195,322	$ 426,340	$ 61,062	$ 324,976	$1,939,341

(1) Credit risk profile reflects internally assigned grade of purchased covered loans without regard to FDIC indemnification.

Credit Risk Profile by Internally Assigned Grade
At December 31, 2012

	Commercial	Commercial Real Estate	Construction	Residential Real Estate	Consumer Installment and Other	Purchased Non-covered Loans	Purchased Covered Loans (1)	Total
				(In thousands)				
Grade:								
Pass	$324,452	$ 599,472	$ 7,518	$ 219,655	$ 459,076	$ 51,901	$ 274,976	$ 1,937,050
Substandard	11,413	33,455	466	2,803	1,158	27,066	122,815	199,176
Doubtful	4,251	-	-	-	46	1,145	470	5,912
Loss	-	-	-	-	418	5	150	573
Default risk purchase discount	-	-	-	-	-	(5,226)	(26,128)	(31,354)
Total	$340,116	$ 632,927	$ 7,984	$ 222,458	$ 460,698	$ 74,891	$ 372,283	$ 2,111,357

(1) Credit risk profile reflects internally assigned grade of purchased covered loans without regard to FDIC indemnification.

The following tables summarize loans by delinquency and nonaccrual status:

Summary of Loans by Delinquency and Nonaccrual Status
At June 30, 2013

	Current and Accruing	30-89 Days Past Due and Accruing	Past Due 90 days or More and Accruing	Nonaccrual	Total Loans
			(In thousands)		
Commercial	$ 304,644	$ 2,302	$ -	$ 2,675	$ 309,621
Commercial real estate	593,883	14,275	-	5,847	614,005
Construction	8,015	-	-	-	8,015
Residential real estate	194,348	560	-	414	195,322
Consumer installment & other	422,702	3,397	241	-	426,340
Total originated loans	1,523,592	20,534	241	8,936	1,553,303
Purchased non-covered loans	54,447	1,712	-	4,903	61,062
Purchased covered loans	300,332	7,747	74	16,823	324,976
Total	$ 1,878,371	$ 29,993	$ 315	$ 30,662	$ 1,939,341

Summary of Loans by Delinquency and Nonaccrual Status
At December 31, 2012

	Current and Accruing	30-89 Days Past Due and Accruing	Past Due 90 days or More and Accruing	Nonaccrual	Total Loans
			(In thousands)		
Commercial	$ 333,474	$ 1,032	$ -	$ 5,610	$ 340,116
Commercial real estate	616,276	10,750	-	5,901	632,927
Construction	7,984	-	-	-	7,984
Residential real estate	220,032	2,193	-	233	222,458
Consumer installment & other	455,007	5,205	455	31	460,698
Total originated loans	1,632,773	19,180	455	11,775	1,664,183
Purchased non-covered loans	65,567	1,821	4	7,499	74,891
Purchased covered loans	352,619	6,488	155	13,021	372,283
Total	$ 2,050,959	$ 27,489	$ 614	$ 32,295	$ 2,111,357

The following is a summary of the effect of nonaccrual loans on interest income:

	For the Three Months		For the Six Months	
	Ended June 30,			
	2013	2012	2013	2012
	(In thousands)			
Interest income that would have been recognized had the loans performed in accordance with their original terms	$634	$1,104	$1,388	$2,168
Less: Interest income recognized on nonaccrual loans	(203)	(494)	(578)	(1,336)

Total reduction of interest income	$431	$610	$810	$832

There were no commitments to lend additional funds to borrowers whose loans were on nonaccrual status at June 30, 2013 and December 31, 2012.

The following summarizes impaired loans:

	Impaired Loans At June 30, 2013		
	Recorded Investment	Unpaid Principal Balance (In thousands)	Related Allowance
Impaired loans with no related allowance recorded:			
Commercial	$ 9,717	$ 17,846	$ -
Commercial real estate	21,536	24,652	-
Construction	2,935	3,369	-
Residential real estate	414	414	-
Consumer installment and other	521	627	-
Impaired loans with an allowance recorded:			
Commercial	1,000	2,173	100
Commercial real estate	3,954	3,954	147
Total:			
Commercial	$ 10,717	$ 20,019	$ 100
Commercial real estate	25,490	28,606	147
Construction	2,935	3,369	-
Residential real estate	414	414	-
Consumer installment and other	521	627	-

	Impaired Loans At December 31, 2012		
	Recorded Investment	Unpaid Principal Balance (In thousands)	Related Allowance
Impaired loans with no related allowance recorded:			
Commercial	$ 3,100	$ 9,506	$ -
Commercial real estate	24,135	27,972	-
Construction	2,363	2,992	-
Residential real estate	668	668	-
Consumer installment and other	2,328	2,616	-
Impaired loans with an allowance recorded:			
Commercial	12,129	13,739	2,588
Commercial real estate	4,038	4,038	164
Total:			
Commercial	$ 15,229	$ 23,245	$ 2,588
Commercial real estate	28,173	32,010	164
Construction	2,363	2,992	-
Residential real estate	668	668	-
Consumer installment and other	2,328	2,616	-

Impaired loans may include troubled debt restructured loans. Impaired loans at June 30, 2013, included $8,014 thousand of restructured loans, including $7,358 thousand that were on nonaccrual status. Impaired loans at December 31, 2012, included $6,678 thousand of restructured loans, including $988 thousand that were on nonaccrual status.

	Impaired Loans							
	For the Three Months Ended June 30,				For the Six Months Ended June 30,			
	2013		2012		2013		2012	
	Average Recorded Investment	Recognized Interest Income	Average Recorded Investment	Recognized Interest Income	Average Recorded Investment	Recognized Interest Income	Average Recorded Investment	Recognized Interest Income
	(In thousands)							
Commercial	$11,473	$ 52	$9,888	$ 67	$12,601	$ 106	$9,342	$ 117
Commercial real estate	27,166	205	30,228	349	27,836	505	31,416	727
Construction	2,397	25	7,552	59	2,254	51	7,981	159
Residential real estate	558	-	1,112	-	621	-	957	-
Consumer installment and other	1,059	8	2,825	8	1,511	15	2,873	26
Total	$42,653	$ 290	$51,605	$ 483	$44,823	$ 677	$52,569	$ 1,029

The following table provides information on troubled debt restructurings:

	Troubled Debt Restructurings At June 30, 2013			
	Number of Contracts	Pre-Modification Carrying Value	Period-End Carrying Value	Period-End Individual Impairment Allowance
	(In thousands)			
Commercial	4	$ 1,991	$ 1,759	$ -
Commercial real estate	3	6,295	6,255	147
Total	7	$ 8,286	$ 8,014	$ 147

	Troubled Debt Restructurings At December 31, 2012			
	Number of Contracts	Pre-Modification Carrying Value	Period-End Carrying Value	Period-End Individual Impairment Allowance
	(In thousands)			
Commercial	3	$ 1,318	$ 1,196	$ 797
Commercial real estate	2	5,391	5,482	-
Total	5	$ 6,709	$ 6,678	$ 797

During the three and six months ended June 30, 2013, the Company modified three loans with a total carrying value of $1,010 thousand and four loans with a total carrying value of $3,019 thousand, respectively, that were considered troubled debt restructurings. During the three and six months ended June 30, 2012, the Company modified one loan with a carrying value of $429 thousand and two loans totaling $1,817 thousand, respectively, that were considered troubled debt restructurings. The concessions granted in the four restructurings completed in the first six months of 2013 consisted of modification of payment terms to lower the interest rate and extend the maturity date to allow for deferred principal repayment. The concessions granted in the restructurings completed during the first six months of 2012 largely consisted of modification of payment terms extending the maturity date to allow for deferred principal repayment. During the three and six months ended June 30, 2013, a commercial real estate loan with a carrying value of $3,954 thousand defaulted. During the three and six months ended June 30, 2012, a construction loan with a carrying value of $3,068 thousand defaulted.

The Company pledges loans to secure borrowings from the Federal Home Loan Bank (“FHLB”). The carrying value of the FHLB advances was $25,687 thousand and $25,799 thousand at June 30, 2013 and December 31, 2012, respectively. The loans restricted due to collateral requirements approximate $28,492 thousand and $32,084 thousand at June 30, 2013 and December 31, 2012, respectively. The amount of loans pledged exceeds collateral requirements. The FHLB does not have the right to sell or repledge such loans.

There were no loans held for sale at June 30, 2013 and December 31, 2012.

Note 5: Concentration of Credit Risk

The Company’s business activity is with customers in Northern and Central California. The loan portfolio is well diversified within the Company’s geographic market, although the Company has significant credit arrangements that are secured by real estate collateral. In addition to real estate loans outstanding as disclosed in Note 4, the Company had loan commitments and standby letters of credit related to real estate loans of $69,988 thousand and $69,345 thousand at June 30, 2013 and December 31, 2012, respectively. The Company requires collateral on all real estate loans with loan-to-value ratios at origination generally no greater than 75% on commercial real estate loans and no greater than 80% on residential real estate loans at origination.

Note 6: Other Assets

Other assets consisted of the following:

	At June 30, 2013	At December 31, 2012
	(In thousands)	
Cost method equity investments:		
Federal Reserve Bank stock (1)	$14,069	$ 14,069
Federal Home Loan Bank stock (2)	5,865	7,353
Other investments	376	376
Total cost method equity investments	20,310	21,798
Life insurance cash surrender value	46,056	45,579
Deferred taxes receivable	52,486	42,449
Limited partnership investments	19,219	20,631
Interest receivable	20,186	20,274
FDIC indemnification receivable	8,758	13,847
Prepaid assets	3,180	11,679
Other assets	11,265	11,829
Total other assets	$181,460	$ 188,086

(1) A bank applying for membership in the Federal Reserve System is required to subscribe to stock in the Federal Reserve Bank (FRB) in a sum equal to six percent of the bank’s paid-up capital stock and surplus. One-half of the amount of the bank's subscription shall be paid to the FRB and the remaining half will be subject to call when deemed necessary by the Board of Governors of the Federal Reserve System.

(2) Borrowings from the Federal Home Loan Bank (FHLB) must be supported by capital stock holdings. The minimum activity-based requirement is 4.7% of the outstanding advances. The requirement may be adjusted from time to time by the FHLB within limits established in the FHLB's Capital Plan.

Note 7: Goodwill and Identifiable Intangible Assets

The Company has recorded goodwill and other identifiable intangibles associated with purchase business combinations. Goodwill is not amortized, but is periodically evaluated for impairment. The Company did not recognize impairment during the six months ended June 30, 2013 and 2012. Identifiable intangibles are amortized to their estimated residual values over their expected useful lives. Such lives and residual values are also periodically reassessed to determine if any amortization period adjustments are indicated. During the six months ended June 30, 2013 and 2012, no such adjustments were recorded.

The carrying values of goodwill were (in thousands):

June 30, 2013	$121,673
December 31, 2012	$121,673

The gross carrying amount of identifiable intangible assets and accumulated amortization was:

	At June 30, 2013		At December 31, 2012	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	(In thousands)			
Core Deposit Intangibles	$56,808	$ (37,114)	$ 56,808	$ (34,938)
Merchant Draft Processing Intangible	10,300	(9,117)	10,300	(8,909)
Total Identifiable Intangible Assets	$67,108	$ (46,231)	$ 67,108	$ (43,847)

As of June 30, 2013, the current year and estimated future amortization expense for identifiable intangible assets was:

	Core Deposit Intangibles	Merchant Draft Processing Intangible	Total
	(In thousands)		
Six months ended June 30, 2013 (actual)	$ 2,176	$ 208	$ 2,384
Estimate for year ended December 31, 2013	4,304	400	4,704
2014	3,946	324	4,270
2015	3,594	262	3,856
2016	3,292	212	3,504
2017	2,913	164	3,077
2018	1,892	29	1,921

Note 8: Deposits and Borrowed Funds

Deposits totaled $4,101,394 thousand at June 30, 2013, compared with $4,232,492 thousand at December 31, 2012. The following table provides additional detail regarding deposits.

	Deposits	
	At June 30, 2013	At December 31, 2012
	(In thousands)	
Noninterest-bearing	$1,644,151	$ 1,676,071
Interest-bearing:		
Transaction	725,852	748,818
Savings	1,139,110	1,165,032
Time	592,281	642,571
Total deposits	$4,101,394	$ 4,232,492

Demand deposit overdrafts of $3,033 thousand and $6,307 thousand were included as loan balances at June 30, 2013 and December 31, 2012, respectively. Interest expense for aggregate time deposits with individual account balances in excess of $100 thousand was $283 thousand and $587 thousand in the second quarter and first six months of 2013, respectively and $414 thousand and $836 thousand in the second quarter and first six months of 2012, respectively.

Short-term borrowed funds of $66,640 thousand at June 30, 2013 represent securities sold under agreements to repurchase the securities. As the Company is obligated to repurchase the securities, the transfer of the securities is accounted for as a secured borrowing rather than a sale. Securities sold under repurchase agreements are held in the custody of independent securities brokers. The amount of the securities approximates $108,872 thousand at June 30, 2013. The short-term borrowed funds mature on an overnight basis.

FHLB advances with carrying value of $25,687 thousand at June 30, 2013 are secured by $28,492 thousand of residential real estate loans and $9,320 thousand of securities at June 30, 2013. The FHLB advances are due in full upon their maturity dates: $5,000 thousand mature in December 2013 and $20,000 thousand mature in January 2015. The FHLB advances may be paid off prior to such maturity dates subject to prepayment fees.

A term repurchase agreement of $10,000 thousand at June 30, 2013 represents securities sold under an agreement to repurchase the securities. As the Company is obligated to repurchase the securities, the transfer of the securities is accounted for as a secured borrowing rather than a sale. Securities sold under repurchase agreements are held in the custody of independent securities brokers. The carrying amount of the related securities is approximately $14,243 thousand at June 30, 2013. The term repurchase agreement matures in full in August 2014.

The Company has a $35,000 thousand unsecured line of credit which had no outstanding balance at June 30, 2013, and a variable interest rate of 2.0% per annum with interest payable monthly on outstanding advances. Advances may be made up to the unused credit limit under the line of credit through March 19, 2014.

Debt financing of $15,000 thousand is a note issued by Westamerica Bancorporation on October 31, 2003 which matures October 31, 2013. Interest of 5.31% per annum is payable semiannually on April 30 and October 31, with principal due at maturity. The note is subject to financial covenants requiring the Company to maintain, at all times, certain minimum levels of consolidated tangible net worth and maximum levels of capital debt. The Company believes it is in compliance with all of the covenants required by the note as of June 30, 2013.

Note 9: Fair Value Measurements

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Available for sale investment securities are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as certain loans held for investment, investment securities held to maturity, and other assets. These nonrecurring fair value adjustments typically involve the lower-of-cost-or-fair value accounting of individual assets.

In accordance with the Fair Value Measurement and Disclosure topic of the Codification, the Company bases its fair values on the price that would be received to sell an asset or paid to transfer a liability in the principal market or most advantageous market for an asset or liability in an orderly transaction between market participants on the measurement date under current market conditions. A fair value measurement reflects all of the assumptions that market participants would use in pricing the asset or liability, including assumptions about the risk inherent in a particular valuation technique, the effect of a restriction on the sale or use of an asset, and the risk of nonperformance.

The Company groups its assets and liabilities measured at fair value into a three-level hierarchy, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. When the valuation assumptions used to measure the fair value of the asset or liability are categorized within different levels of the fair value hierarchy, the asset or liability is categorized in its entirety within the lowest level of the hierarchy. These levels are:

Level 1 – Valuation is based upon quoted prices for identical instruments traded in active exchange markets, such as the New York Stock Exchange. Level 1 includes U.S. Treasury, equity securities and federal agency securities, which are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market. Level 2 includes mortgage-backed securities, corporate securities, asset-backed securities, municipal bonds and residential collateralized mortgage obligations.

Level 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company’s estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

The Company relies on independent vendor pricing services to measure fair value for investment securities available for sale and investment securities held to maturity. The Company employs three pricing services. To validate the pricing of these vendors, the Company routinely randomly selects securities for pricing by two or more of the vendors; significant pricing differences, if any, are evaluated using all available independent quotes with the lowest quote generally used as the fair value estimate. In addition, the Company conducts "other than temporary impairment (OTTI)" analysis on a quarterly basis; securities selected for OTTI analysis include all securities with fair value pricing of less than 95 percent of amortized cost. As with any valuation technique used to estimate fair value, changes in underlying assumptions used could significantly affect the results of current and future values. Accordingly, these fair values estimates may not be realized in an actual sale of the securities.

When the Company changes its valuation assumptions for measuring financial assets and financial liabilities at fair value, either due to changes in current market conditions or other factors, it may need to transfer those assets or liabilities to another level in the hierarchy based on the new assumptions used. The Company recognizes these transfers at the end of the reporting period that the transfers occur. For the six months ended June 30, 2013 and 2012, there were no transfers in or out of levels 1, 2 or 3.

Assets Recorded at Fair Value on a Recurring Basis

The table below presents assets measured at fair value on a recurring basis.

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(In thousands)		
Investment securities available for sale:				
At June 30, 2013	$1,004,888	$ 50,880	$ 954,008	$ -
At December 31, 2012	$825,636	$ 57,424	$ 768,212	$ -

Assets Recorded at Fair Value on a Nonrecurring Basis

The Company may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with GAAP. These adjustments to fair value usually result from application of lower-of-cost-or-market accounting of individual assets. For assets measured at fair value on a nonrecurring basis that were recorded in the balance sheet at June 30, 2013 and December 31, 2012, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related assets at period end.

	At June 30, 2013				
	Fair Value	Level 1	Level 2	Level 3	Total Losses
			(In thousands)		
Non-covered other real estate owned	$4,909	$-	$4,909	$-	$ (822)
Covered other real estate owned	6,035	-	6,035	-	(133)
Originated impaired loans	4,278	-	2,537	1,741	(2,093)
Purchased covered impaired loans	8,911	-	3,421	5,490	(517)
Total assets measured at fair value on a nonrecurring basis	$24,133	$-	$16,902	$7,231	$ (3,565)

	At December 31, 2012				
	Fair Value	Level 1	Level 2	Level 3	Total Losses
			(In thousands)		
Non-covered other real estate owned	$6,618	$-	$6,618	$-	$ (1,360)
Covered other real estate owned	7,929	-	7,929	-	(371)
Originated impaired loans	5,197	-	3,097	2,100	(3,158)
Purchased covered impaired loans	6,684	-	2,224	4,460	(83)
	$26,428	$-	$19,868	$6,560	$ (4,972)

Total assets measured at fair value on a nonrecurring basis	

Level 2 – Valuation is based upon independent market prices or appraised value of the collateral, less 10% for selling costs, generally. Level 2 includes other real estate owned that has been measured at fair value subsequent to its initial classification as foreclosed assets and impaired loans collateralized by real property where a specific reserve has been established or a charge-off has been recorded.

Level 3 – Valuation is based upon estimated liquidation values of loan collateral. The value of level 3 assets can also include a component of real estate, which is valued as described for level 2 inputs, when collateral for the impaired loan includes both business assets and real estate. Level 3 includes impaired loans where a specific reserve has been established or a charge-off has been recorded.

Disclosures about Fair Value of Financial Instruments

The following section describes the valuation methodologies used by the Company for estimating fair value of financial instruments not recorded at fair value in the balance sheet.

Cash and Due from Banks Cash and due from banks represent U.S. dollar denominated coin and currency, deposits at the Federal Reserve Bank and correspondent banks, and amounts being settled with other banks to complete the processing of customers' daily transactions. Collectively, the Federal Reserve Bank and financial institutions operate a market in which cash and due from banks transactions are processed continuously in significant daily volumes honoring the face value of the U.S. dollar.

Investment Securities Held to Maturity The fair values of investment securities were estimated using quoted prices as described above for Level 1 and Level 2 valuation.

Loans Loans were separated into two groups for valuation. Variable rate loans, except for those described below, which reprice frequently with changes in market rates were valued using historical cost. Fixed rate loans and variable rate loans that have reached their minimum contractual interest rates were valued by discounting the future cash flows expected to be received from the loans using current interest rates charged on loans with similar characteristics. Additionally, the allowance for loan losses of $30,926 thousand at June 30, 2013 and $30,234 thousand at December 31, 2012 and the fair value discount due to credit default risk associated with purchased covered and purchased non-covered loans of $18,514 thousand and $3,609 thousand, respectively at June 30, 2013 and purchased covered and purchased non-covered loans of $26,128 thousand and $5,226 thousand, respectively at December 31, 2012 were applied against the estimated fair values to recognize estimated future defaults of contractual cash flows. The Company does not consider these values to be a liquidation price for the loans.

FDIC Indemnification Receivable The fair value of the FDIC indemnification receivable recorded in Other Assets was estimated by discounting estimated future cash flows using current market rates for financial instruments with similar characteristics.

Deposit Liabilities Deposits with no stated maturity such as checking accounts, savings accounts and money market accounts can be readily converted to cash or used to settle transactions at face value through the broad financial system operated by the Federal Reserve Bank and financial institutions. The fair value of deposits with no stated maturity is equal to the amount payable on demand. The fair values of time deposits were estimated by discounting estimated future contractual cash flows using current market rates for financial instruments with similar characteristics.

Short-Term Borrowed Funds The carrying amount of securities sold under agreement to repurchase and other short-term borrowed funds approximate fair value due to the relatively short period of time between their origination and their expected realization.

Federal Home Loan Bank Advances The fair values of FHLB advances were estimated by using redemption amounts quoted by the Federal Home Loan Bank of San Francisco.

Term Repurchase Agreement The fair value of the term repurchase agreement was estimated by using interpolated yields for financial instruments with similar characteristics.

Debt Financing The fair value of debt financing was estimated by using interpolated yields for financial instruments with similar characteristics.

The table below is a summary of fair value estimates for financial instruments and the level of the fair value hierarchy within which the fair value measurements are categorized, excluding financial instruments recorded at fair value on a recurring basis. The values assigned do not necessarily represent amounts which ultimately may be realized. In addition, these values do not give effect to discounts to fair value which may occur when financial instruments are sold in larger quantities. The carrying amounts in the following table are recorded in the balance sheet under the indicated captions.

The Company has not included assets and liabilities that are not financial instruments, such as goodwill, long-term relationships with deposit, merchant processing and trust customers, other purchased intangibles, premises and equipment, deferred taxes and other assets and liabilities. The total estimated fair values do not represent, and should not be construed to represent, the underlying value of the Company.

	At June 30, 2013				
	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets:			(In thousands)		
Cash and due from banks	$384,276	$ 384,276	$ 384,276	$-	$ -
Investment securities held to maturity	1,134,615	1,124,946	2,266	1,122,680	-
Loans	1,908,415	1,922,777	-	-	1,922,777
Other assets - FDIC indemnification receivable	8,758	8,756	-	-	8,756
Financial Liabilities:					
Deposits	$4,101,394	$ 4,100,948	$ -	$3,509,113	$ 591,835
Short-term borrowed funds	66,640	66,640	-	66,640	-
Federal Home Loan Bank advances	25,687	25,834	25,834	-	-
Term repurchase agreement	10,000	10,096	-	10,096	-
Debt financing	15,000	15,201	-	15,201	-

	At December 31, 2012				
	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets:			(In thousands)		
Cash and due from banks	$491,382	$ 491,382	$ 491,382	$-	$ -
Investment securities held to maturity	1,156,041	1,184,557	3,275	1,181,282	-
Loans	2,081,123	2,090,712	-	-	2,090,712
Other assets - FDIC indemnification receivable	13,847	13,834	-	-	13,834
Financial Liabilities:					
Deposits	$4,232,492	$ 4,232,239	$ -	$3,589,921	$ 642,318
Short-term borrowed funds	53,687	53,687	-	53,687	-
Federal Home Loan Bank advances	25,799	26,150	26,150	-	-
Term repurchase agreement	10,000	10,135	-	10,135	-
Debt financing	15,000	15,645	-	15,645	-

The majority of the Company's standby letters of credit and other commitments to extend credit carry current market interest rates if converted to loans. No premium or discount was ascribed to these commitments because virtually all funding would be at current market rates.

Note 10: Commitments and Contingent Liabilities

Loan commitments are agreements to lend to a customer provided there is no violation of any condition established in the agreement. Commitments generally have fixed expiration dates or other termination clauses. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future funding requirements. Loan commitments are subject to the Company's normal credit policies and collateral requirements. Unfunded loan commitments were $334,136 thousand and $339,651 thousand at June 30, 2013 and December 31, 2012, respectively. Standby letters of credit commit the Company to make payments on behalf of customers when certain specified future events occur. Standby letters of credit are primarily issued to support customers' short-term financing requirements and must meet the Company's normal credit policies and collateral requirements. Standby letters of credit outstanding totaled $32,293 thousand and $32,347 thousand at June 30, 2013 and December 31, 2012, respectively. The Company also had commitments for commercial and similar letters of credit of $344 thousand and $344 thousand at June 30, 2013 and December 31, 2012, respectively.

Due to the nature of its business, the Company is subject to various threatened or filed legal cases. Based on the advice of legal counsel, the Company does not expect such cases will have a material, adverse effect on its financial position or results of operations. Legal liabilities are accrued when obligations become probable and the amount is reasonably estimable. Legal costs related to covered assets are eighty percent indemnified under loss-sharing agreements with the FDIC if certain conditions are met.

Note 11: Earnings Per Common Share

The table below shows earnings per common share and diluted earnings per common share. Basic earnings per common share are computed by dividing net income applicable to common equity by the average number of common shares outstanding during the period. Diluted earnings per common share are computed by dividing net income applicable to common equity by the average number of common shares outstanding during the period plus the impact of common stock equivalents.

	For the Three Months		For the Six Months	
	Ended June 30,			
	2013	2012	2013	2012
	(In thousands, except per share data)			
Net income applicable to common equity (numerator)	$17,112	$20,964	$34,383	$41,969
Basic earnings per common share				
Weighted average number of common shares outstanding - basic (denominator)	26,890	27,744	27,017	27,897
Basic earnings per common share	$0.64	$0.76	$1.27	$1.50
Diluted earnings per common share				
Weighted average number of common shares outstanding - basic	26,890	27,744	27,017	27,897
Add exercise of options reduced by the number of shares that could have been purchased with the proceeds of such exercise	8	46	10	54
Weighted average number of common shares outstanding - diluted (denominator)	26,898	27,790	27,027	27,951
Diluted earnings per common share	$0.64	$0.75	$1.27	$1.50

For the three and six months ended June 30, 2013, options to purchase 2,264 thousand and 2,290 thousand shares of common stock, respectively, were outstanding but not included in the computation of diluted net income per share because the option exercise price exceeded the fair value of the stock such that their inclusion would have had an anti-dilutive effect.

For the three and six months ended June 30, 2012, options to purchase 2,072 thousand and 2,035 thousand shares of common stock, respectively, were outstanding but not included in the computation of diluted net income per share because their inclusion would have had an anti-dilutive effect.

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WESTAMERICA BANCORPORATION
FINANCIAL SUMMARY

	For the Three Months		For the Six Months	
	Ended June 30,			
	2013	2012	2013	2012
	(In thousands, except per share data)			
Net Interest and Fee Income (FTE)1	$42,628	$50,333	$86,463	$102,032
Provision for Loan Losses	1,800	2,800	4,600	5,600
Noninterest Income				
Loss on Sale of Securities	-	(1,287)	-	(1,287)
Other	14,284	14,820	28,562	29,489
Total Noninterest Income	14,284	13,533	28,562	28,202
Noninterest Expense	28,192	29,349	56,869	59,383
Income Before Income Taxes (FTE)1	26,920	31,717	53,556	65,251
Income Tax Provision (FTE)1	9,808	10,753	19,173	23,282
Net Income	$17,112	$20,964	$34,383	$41,969
Average Common Shares Outstanding	26,890	27,744	27,017	27,897
Diluted Average Common Shares Outstanding	26,898	27,790	27,027	27,951
Common Shares Outstanding at Period End	26,769	27,621	26,769	27,621
Per Common Share:				
Basic Earnings	$0.64	$0.76	$1.27	$1.50
Diluted Earnings	0.64	0.75	1.27	1.50
Book Value Per Common Share	$20.34	$20.20		
Financial Ratios:				
Return on Assets	1.42 %	1.69 %	1.42 %	1.69 %
Return on Common Equity	12.74 %	15.55 %	12.84 %	15.50 %
Net Interest Margin (FTE)1	4.12 %	4.89 %	4.19 %	5.00 %
Net Loan Losses to Average Loans:				
Originated Loans	0.15 %	0.65 %	0.37 %	0.67 %
Purchased Covered Loans	0.59 %	0.19 %	0.49 %	0.23 %
Purchased Non-covered Loans	0.71 %	0.09 %	0.34 %	0.04 %
Efficiency Ratio2	49.5 %	46.0 %	49.4 %	45.6 %
Average Balances:				
Assets	$4,840,319	$4,974,619	$4,874,212	$5,002,777
Earning Assets	4,147,096	4,127,699	4,141,510	4,093,985
Originated Loans	1,586,435	1,789,221	1,613,769	1,812,296
Purchased Covered Loans	341,896	478,965	352,802	495,965
Purchased Non-covered Loans	66,030	107,483	69,373	113,493
Deposits	4,132,509	4,227,752	4,165,685	4,240,758
Shareholders' Equity	538,529	542,192	540,192	544,434
Period End Balances:				
Assets	$4,813,908	$4,953,130		
Earning Assets	4,078,844	4,232,582		
Originated Loans	1,553,303	1,751,578		

Purchased Covered Loans	324,976	463,251		
Purchased Non-covered Loans	61,062	102,390		
Deposits	4,101,394	4,208,499		
Shareholders' Equity	544,622	557,926		
Capital Ratios at Period End:				
Total Risk Based Capital	15.98 %	15.74 %		
Tangible Equity to Tangible Assets	8.61 %	8.54 %		
Dividends Paid Per Common Share	$0.37	$0.37	$0.74	$0.74
Common Dividend Payout Ratio	58 %	49 %	58 %	49 %

The above financial summary has been derived from the Company's unaudited consolidated financial statements. This information should be read in conjunction with those statements, notes and the other information included elsewhere herein. Percentages under the heading "Financial Ratios" are annualized with the exception of the efficiency ratio.

1 Yields on securities and certain loans have been adjusted upward to a "fully taxable equivalent" ("FTE") basis, which is a non-GAAP financial measure, in order to reflect the effect of income which is exempt from federal income taxation at the current statutory tax rate.

2 The efficiency ratio is defined as noninterest expense divided by total revenue (net interest income on an FTE basis, which is a non-GAAP financial measure, and noninterest income).

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

In order to provide stimulus to the economy following the “financial crisis” recession, the Federal Reserve’s Federal Open Market Committee has maintained highly accommodative monetary policies to influence interest rates to low levels. The Company’s principal source of revenue is net interest and fee income, which represents interest earned on loans and investment securities (“earning assets”) reduced by interest paid on deposits and other borrowings (“interest bearing liabilities”). The decline in market interest rates following the recession has reduced the spread between interest rates on earning assets and interest bearing liabilities. As a result, the Company’s net interest margin and net interest income have declined. The Company also earns revenue from service charges on deposit accounts, merchant processing services, debit card fees, and other fees (“noninterest income”). Service charges on deposit accounts are subject to laws and regulations; recent regulations and customer activity have caused service charges on deposit accounts to decline in 2012 and the three and six months ended June 30, 2013; however, debit card fees, trust fees and financial services commissions have increased due to higher transaction volumes and the Company’s sales efforts. The Company incurs noninterest expenses to deliver products and services to our customers. Management is focused on controlling noninterest expense levels, particularly due to the recent market interest rate pressure on net interest income.

Westamerica Bancorporation and subsidiaries (the “Company”) reported net income of $17.1 million or $0.64 diluted earnings per common share for the second quarter 2013 and net income of $34.4 million or $1.27 diluted earnings per common share for the six months ended June 30, 2013. These results compare to net income of $21.0 million or $0.75 diluted earnings per common share for the second quarter 2012 and net income of $42.0 million or $1.50 diluted earnings per common share for the six months ended June 30, 2012. The second quarter of 2012 included a $1.3 million loss realized from the sale of a collateralized mortgage obligation bond which decreased net income by $750 thousand and a tax refund from an amended tax return which increased net income by $950 thousand.

Net Income

Following is a summary of the components of net income for the periods indicated:

	For the Three Months		For the Six Months	
	Ended June 30,			
	2013	2012	2013	2012
	(In thousands, except per share data)			
Net interest income (FTE)	$42,628	$50,333	$86,463	$102,032
Provision for loan losses	(1,800)	(2,800)	(4,600)	(5,600)
Noninterest income	14,284	13,533	28,562	28,202
Noninterest expense	(28,192)	(29,349)	(56,869)	(59,383)
Income before taxes (FTE)	26,920	31,717	53,556	65,251
Income tax provision (FTE)	(9,808)	(10,753)	(19,173)	(23,282)
Net income	$17,112	$20,964	$34,383	$41,969
Average diluted common shares	26,898	27,790	27,027	27,951
Diluted earnings per common share	$0.64	$0.75	$1.27	$1.50
Average total assets	$4,840,319	$4,974,619	$4,874,212	$5,002,777
Net income to average total assets (annualized)	1.42%	1.69%	1.42%	1.69%
Net income to average common stockholders' equity (annualized)	12.74%	15.55%	12.84%	15.50%

Net income for the second quarter of 2013 was $3.9 million less than the same quarter of 2012, the net result of lower net interest and fee income (fully taxable equivalent or “FTE”), partially offset by higher noninterest income and decreases in loan loss provision, noninterest expense and income tax provision (FTE). A decrease in net interest and fee income (FTE) was mostly attributed to lower average balances of loans and lower yields on interest-earning assets, partially offset by higher average balances of investments, lower average balances of interest-bearing deposits and lower rates paid on interest-bearing deposits. The provision for loan losses was reduced, reflecting Management's evaluation of losses inherent in the loan portfolio; net loan losses and nonperforming loan volumes have declined relative to earlier periods. Noninterest expense decreased $1.2 million primarily due to reduced personnel costs, occupancy expense, professional fees and intangible asset amortization.

Comparing the first half of 2013 to the first half of 2012, net income decreased $7.6 million primarily due to lower net interest and fee income (FTE), partially offset by higher noninterest income and decreases in loan loss provision, noninterest expense and income tax provision (FTE). The lower net interest and fee income (FTE) was primarily caused by a lower average volume of loans and lower yields on interest-earning assets, partially offset by higher average balances of investments, lower average balances of interest-bearing deposits and lower rates paid on interest-bearing deposits. The provision for loan losses was reduced $1.0 million, reflecting Management's evaluation of losses inherent in the loan portfolio; net loan losses and nonperforming loan volumes have declined relative to earlier periods. Noninterest expense decreased $2.5 million primarily due to reduced personnel costs, occupancy expense, professional fees and intangible asset amortization.

Net Interest and Fee Income (FTE)

Following is a summary of the components of net interest and fee income (FTE) for the periods indicated:

	For the Three Months		For the Six Months	
	Ended June 30,			
	2013	2012	2013	2012
	(In thousands)			
Interest and fee income	$39,269	$46,901	$79,734	$95,199
Interest expense	(1,219)	(1,472)	(2,471)	(3,031)
FTE adjustment	4,578	4,904	9,200	9,864
Net interest income (FTE)	$42,628	$50,333	$86,463	$102,032
Average earning assets	$4,147,096	$4,127,699	$4,141,510	$4,093,985
Net interest margin (FTE) (annualized)	4.12%	4.89%	4.19%	5.00%

Net interest and fee income (FTE) for the second quarter 2013 decreased $7.7 million compared with the same period in 2012 to $42.6 million, mainly due to lower average balances of loans (down $381 million) and lower yields on interest-earning assets (down 0.80%), partially offset by higher average balances of investments (up $401 million), lower average balances of interest-bearing deposits (down $146 million) and lower rates paid on interest-bearing deposits (down 0.03%).

Comparing the first half of 2013 with the first half of 2012, net interest and fee income (FTE) decreased $15.6 million primarily due to a lower average volume of loans (down $386 million) and lower yields on interest earning assets (down 0.84%), partially offset by higher average balances of investments (up $433 million) and lower average balances of interest-bearing deposits (down $134 million) and lower rates paid on interest-bearing deposits (down 0.03%).

Loan volumes have declined due to problem loan workout activities, particularly with purchased loans, and reduced volumes of loan originations. In Management’s opinion, competitive loan pricing does not currently provide adequate forward earnings potential. As a result, the Company has not currently taken an aggressive posture relative to loan portfolio growth. Management has maintained relatively stable interest-earning asset volumes by increasing investment securities as loan volumes have declined.

Yields on interest-earning assets have declined due to relatively low interest rates prevailing in the market. Management’s response to prevailing economic conditions and competitive loan pricing has been to reduce loan volumes, placing greater reliance on lower-yielding investment securities. Rates on interest-bearing deposits have declined to offset some of the decline in asset yields.

At June 30, 2013, purchased FDIC covered loans represented 17 percent of the Company’s loan portfolio. Under the terms of the FDIC loss-sharing agreements, the FDIC is obligated to reimburse the Bank 80 percent of loan interest income foregone on covered loans. Such reimbursements are limited to the lesser of 90 days contractual interest or actual unpaid contractual interest at the time a principal loss is recognized in respect to the underlying loan. FDIC loss indemnification of covered non-residential assets expires February 6, 2014. For further information, see the Loan Portfolio Credit Risk section of this report.

Interest and Fee Income (FTE)

Interest and fee income (FTE) for the second quarter of 2013 decreased $8.0 million or 15.4% from the same period in 2012. The decrease was caused by lower average balances of loans and lower yields on interest-earning assets, partially offset by higher average balances of investments. The total average balances of loans declined due to decreases in the average balances of commercial real estate loans (down $166 million), taxable commercial loans (down $73 million), consumer loans (down $53 million), residential real estate loans (down $52 million), tax-exempt commercial loans (down $24 million) and construction loans (down $13 million). The average investment portfolio increased largely due to higher average balances of corporate securities (up $228 million), collateralized mortgage obligations and mortgage backed securities (up $201 million) and municipal securities (up $42 million), partially offset by a $67 million decrease in average balances of securities of U.S. government sponsored entities. The average yield on the Company's earning assets decreased from 5.04% in the second quarter 2012 to 4.24% in the corresponding period of 2013. The composite yield on loans declined 0.46% to 5.38% mostly due to lower yields on commercial real estate loans (down 0.49%), consumer loans (down 0.52%), taxable commercial loans (down 0.71%), residential real estate loans (down 0.18%) and tax-exempt loans (down 0.34%), partially offset by higher yields on construction loans (up 4.47%). Nonperforming loans are included in average loan volumes used to compute loan yields; fluctuations in nonaccrual loan volumes impact loan yields. Yields on construction loans increased primarily due to higher delinquent interest received on nonaccrual loans. The investment yields in general declined due to market rates. The investment portfolio yield decreased 0.77% to 3.18% primarily due to lower yields on collateralized mortgage obligations and mortgage backed securities (down 0.90%), municipal securities (down 0.46%) and corporate securities (down 0.45%).

Comparing the first half of 2013 with the first half of 2012, interest and fee income (FTE) was down $16.1 million. The decrease resulted from a lower average volume of loans and lower yields on interest earning assets, partially offset by higher average balances of investments. The total average balances of loans declined due to decreases in the average balances of commercial real estate loans (down $176 million), taxable commercial loans (down $75 million), consumer loans (down $44 million), residential real estate loans (down $52 million), tax-exempt commercial loans (down $24 million) and construction loans (down $15 million). The average investment portfolio increased largely due to higher average balances of collateralized mortgage obligations and mortgage backed securities (up $255 million), corporate securities (up $208 million) and municipal securities (up $36 million), partially offset by a $65 million decrease in average balances of securities of U.S. government sponsored entities. The average yield on the Company's earning assets decreased from 5.15% in the first half of 2012 to 4.31% in the corresponding period of 2013. The composite yield on loans declined 0.46% to 5.42% mostly due to lower yields on commercial real estate loans (down 0.44%), consumer loans (down 0.67%), taxable commercial loans (down 0.49%), residential real estate loans (down 0.15%) and tax-exempt loans (down 0.16%), partially offset by higher yields on construction loans (up 2.34%). Nonperforming loans are included in average loan volumes used to compute loan yields; fluctuations in nonaccrual loan volumes impact loan yields. The yield on construction loans in the first half of 2013 was elevated due to delinquent interest received on nonaccrual loans. The investment yields in general declined due to market rates. The investment portfolio yield for the first half of 2013 decreased 0.84% to 3.25% compared with the same period in 2012 primarily due to lower yields on collateralized mortgage obligations and mortgage backed securities (down 0.98%), municipal securities (down 0.46%) and corporate securities (down 0.37%).

Interest Expense

Interest expense has been reduced by lowering rates paid on interest-bearing deposits and by reducing the volume of higher-cost funding sources. Lower-cost checking and savings deposits accounted for 85.5% of total average deposits in the second quarter 2013 compared with 81.7% in the second quarter 2012. Interest expense in the second quarter of 2013 decreased $253 thousand or 17.2% compared with the same period in 2012 due to lower rates paid on interest-bearing deposits and a shift from higher costing deposits to lower costing deposits. Interest-bearing liabilities declined due to lower average balances of time deposits $100 thousand or more (down $132 million), time deposits less than $100 thousand (down $39 million), preferred money market savings (down $20 million) and customer sweep accounts (down $33 million), partially offset by higher average balances of regular savings (up $29 million) and money market savings (up $13 million). The average rate paid on interest-bearing liabilities was 0.19% in the second quarter of 2013 compared with 0.21% in the second quarter of 2012. Rates on interest-bearing deposits for the second quarter 2013 decreased 0.03% to 0.14% compared with second quarter 2012 primarily due to decreases in rates paid on time deposits less than $100 thousand (down 0.10%) and time deposits $100 thousand or more (down 0.02%).

Comparing the first half of 2013 with the first half of 2012, interest expense declined $559 thousand due to lower average balances of interest-bearing deposits and short-term borrowings, and lower rates paid on interest-bearing deposits. Lower-cost checking and savings deposits accounted for 85.2% of total average deposits in the first half 2013 compared with 81.6% in the first half of 2012. Average interest-bearing liabilities during the first half of 2013 fell $179 million compared with the first half of 2012 primarily due to declines in the average balances of time deposits $100 thousand or more (down $127 million) and time deposits less than $100 thousand (down $40 million), preferred money market accounts (down $24 million) and customer sweep accounts (down $45 million), partially offset by increases in the average balances of regular savings (up $30 million) and money market savings (up $17 million). Rates paid on interest-bearing deposits averaged 0.14% during the first half of 2013 compared with 0.17% for the first half of 2012 as a result of decreases in rates paid on time deposits less than $100 thousand (down 0.11%) and time deposits $100 thousand or more (down 0.02%).

Net Interest Margin (FTE)

The following summarizes the components of the Company's net interest margin for the periods indicated:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2013	2012	2013	2012
Yield on earning assets (FTE)	4.24 %	5.04 %	4.31 %	5.15 %
Rate paid on interest-bearing liabilities	0.19 %	0.21 %	0.19 %	0.22 %
Net interest spread (FTE)	4.05 %	4.83 %	4.12 %	4.93 %
Impact of noninterest bearing demand deposits	0.07 %	0.06 %	0.07 %	0.07 %
Net interest margin (FTE)	4.12 %	4.89 %	4.19 %	5.00 %

During the second quarter of 2013, the net interest margin (FTE) decreased 0.77% compared with the same period in 2012. Lower yields on earning assets were partially offset by lower rates paid on interest-bearing liabilities and resulted in a 0.78% decrease in net interest spread (FTE). The 0.07% net interest margin contribution of noninterest-bearing demand deposits resulted in the net interest margin (FTE) of 4.12%. During the first half of 2013, the net interest margin (FTE) decreased 0.81% compared with the first half of 2012. The net interest spread (FTE) in the first half of 2013 was 4.12% compared with 4.93% in the first half of 2012, the net result of a 0.84% decrease in earning asset yields, partially offset by lower cost of interest-bearing liabilities (down 0.03%).

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Summary of Average Balances, Yields/Rates and Interest Differential

The following tables present, for the periods indicated, information regarding the consolidated average assets, liabilities and shareholders' equity, the amounts of interest income earned from average interest earning assets and the resulting yields, and the amounts of interest expense incurred on average interest-bearing liabilities and the resulting rates. Average loan balances include nonperforming loans. Interest income includes proceeds from loans on nonaccrual status only to the extent cash payments have been received and applied as interest income and accretion of purchased loan premiums and discounts. Yields on tax-exempt securities and loans have been adjusted upward to reflect the effect of income exempt from federal income taxation at the current statutory tax rate (FTE).

Distribution of Assets, Liabilities & Shareholders' Equity and Yields, Rates & Interest Margin

For the Three Months Ended June 30, 2013		
	Interest	
Average	Income/	Yields/