CENTRAL VALLEY COMMUNITY BANCORP
Form 10-Q
August 16, 2010
Table of Contents

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, 2010

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NUMBER: 000 31977

CENTRAL VALLEY COMMUNITY BANCORP

(Exact name of registrant as specified in its charter)

California	**77-0539125**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
7100 N. Financial Dr, Suite 101, Fresno, California	**93720**
(Address of principal executive offices)	(Zip code)

Registrant s telephone number **(559) 298-1775**

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 past 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 o

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 o No o

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

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

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

As of August 12, 2010 there were 9,364,016 shares of the registrant s common stock outstanding.

Table of Contents

CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY

2010 QUARTERLY REPORT ON FORM 10-Q

TABLE OF CONTENTS

PART 1: FINANCIAL INFORMATION	**3**
ITEM 1: FINANCIAL STATEMENTS	**3**
ITEM 2: MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	**17**
ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	**40**
ITEM 4: CONTROLS AND PROCEDURES	**41**
PART II: OTHER INFORMATION	**42**
ITEM 1: LEGAL PROCEEDINGS	**42**
ITEM 1A: RISK FACTORS	**42**
ITEM 2: CHANGES IN SECURITIES AND USE OF PROCEEDS	**42**
ITEM 3: DEFAULTS UPON SENIOR SECURITIES	**42**
ITEM 4: REMOVED AND RESERVED	**42**
ITEM 5: OTHER INFORMATION	**42**
ITEM 6: EXHIBITS	**42**
SIGNATURES	**43**

Table of Contents

PART 1: FINANCIAL INFORMATION

ITEM 1: FINANCIAL STATEMENTS

CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

(In thousands, except share amounts)	June 30, 2010 (Unaudited)	December 31, 2009
ASSETS		
Cash and due from banks	$ 16,171	$ 13,857
Interest-earning deposits in other banks	27,243	34,544
Federal funds sold	750	279
Total cash and cash equivalents	44,164	48,680
Available-for-sale investment securities (Amortized cost of $185,618 at June 30, 2010 and $199,744 at December 31, 2009)	186,436	197,319
Loans, less allowance for credit losses of $11,468 at June 30, 2010 and $10,200 at December 31, 2009	457,184	449,007
Bank premises and equipment, net	6,038	6,525
Other real estate owned	3,502	2,832
Bank owned life insurance	11,193	10,998
Federal Home Loan Bank stock	3,050	3,140
Goodwill	23,577	23,577
Core deposit intangibles	1,405	1,612
Accrued interest receivable and other assets	19,440	21,798
Total assets	$ 755,989	$ 765,488
LIABILITIES AND SHAREHOLDERS EQUITY		
Deposits:		
Non-interest bearing	$ 143,556	$ 159,630
Interest bearing	487,753	480,537
Total deposits	631,309	640,167
Short-term borrowings	10,000	5,000
Long-term debt	4,000	14,000
Junior subordinated deferrable interest debentures	5,155	5,155
Accrued interest payable and other liabilities	10,074	9,943
Total liabilities	660,538	674,265
Commitments and contingencies (Note 8)		
Shareholders equity:		
Preferred stock, no par value, $1,000 per share liquidation preference; 10,000,000 shares authorized;		
Series A, no par value, 7,000 issued and outstanding	6,841	6,819
Series B, no par value, issued and outstanding none at June 30, 2010 and 1,359 at December 31, 2009		1,317
Common stock, no par value; 80,000,000 authorized; issued and outstanding 9,362,016 at June 30, 2010 and 8,949,754 at December 31, 2009	39,590	37,611
Retained earnings	48,530	46,931
Accumulated other comprehensive income (loss), net of tax	490	(1,455)

Total shareholders equity		95,451		91,223
Total liabilities and shareholders equity	$	755,989	$	765,488

See notes to unaudited consolidated financial statements.

Table of Contents

CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(In thousands, except earnings per share amounts)	For the Three Months Ended June 30, 2010	For the Three Months Ended June 30, 2009	For the Six Months Ended June 30, 2010	For the Six Months Ended June 30, 2009
INTEREST INCOME:				
Interest and fees on loans	$ 6,927	$ 7,515	$ 13,705	$ 15,055
Interest on Federal funds sold	1	3	1	14
Interest and dividends on investment securities:				
Taxable	1,364	2,128	3,017	4,339
Exempt from Federal income taxes	759	806	1,516	1,513
Total interest income	9,051	10,452	18,239	20,921
INTEREST EXPENSE:				
Interest on deposits	983	1,499	2,036	3,281
Interest on junior subordinated deferrable interest debentures	25	36	48	77
Other	113	169	239	330
Total interest expense	1,121	1,704	2,323	3,688
Net interest income before provision for credit losses	7,930	8,748	15,916	17,233
PROVISION FOR CREDIT LOSSES	1,000	2,500	1,600	4,417
Net interest income after provision for credit losses	6,930	6,248	14,316	12,816
NON-INTEREST INCOME:				
Service charges	863	858	1,724	1,678
Appreciation in cash surrender value of bank owned life insurance	98	97	195	195
Loan placement fees	76	75	104	121
Net realized gains on sales and calls of investment securities	30	62	51	511
Total other-than-temporary impairment on available-for-sale-investment securities	(571)		18	
Change in fair value recognized in other comprehensive income	(129)		(718)	
Net other-than-temporary impairment loss on available-for-sale investment securities	(700)		(700)	
Federal Home Loan Bank dividends	2		4	
Gain on sale and disposal of equipment			5	
Other income	378	309	698	634
Total non-interest income	747	1,401	2,081	3,139
NON-INTEREST EXPENSES:				
Salaries and employee benefits	3,837	3,642	7,584	7,330
Occupancy and equipment	988	944	1,914	1,889
Regulatory assessments	306	642	606	1,010
Data processing expense	282	374	568	646
Advertising	183	184	375	369
Audit and accounting fees	114	111	228	228
Legal fees	167	72	289	164
Other real estate owned	127	16	441	16
Amortization of core deposit intangibles	103	103	207	207
Loss on sale of assets				

Other expense	1,035	1,041	2,134	2,110
Total non-interest expenses	7,142	7,129	14,346	13,969
Income before provision for income taxes	535	520	2,051	1,986
PROVISION FOR INCOME TAXES	31	56	255	263
Net income	$ 504	$ 464	$ 1,796	$ 1,723
Net income	$ 504	$ 464	$ 1,796	$ 1,723
Preferred stock dividends and accretion	99	135	198	184
Net income available to common shareholders	$ 405	$ 329	$ 1,598	$ 1,539
Net income per common share:				
Basic earnings per share	$ 0.04	$ 0.04	$ 0.18	$ 0.20
Weighted average common shares used in basic computation	9,131,753	7,651,918	9,051,168	7,647,128
Diluted earnings per share	$ 0.04	$ 0.04	$ 0.17	$ 0.20
Weighted average common shares used in diluted computation	9,210,838	7,760,014	9,148,724	7,765,519

See notes to unaudited consolidated financial statements

Table of Contents

CENTRAL VALLEY COMMUNITY BANCORP AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX MONTHS ENDED JUNE 30, 2010 AND 2009

(Unaudited)

(In thousands)	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 1,796	$ 1,723
Adjustments to reconcile net income to net cash provided by operating activities:		
Net increase in deferred loan fees	184	110
Depreciation	638	694
Accretion	947	395
Amortization	(559)	(1,401)
Stock-based compensation	113	149
Tax benefit from exercise of stock options	(25)	(8)
Provision for credit losses	1,600	4,417
Net other than temporary impairment losses on investment securities	700	
Net realized gains on sales and calls of available-for-sale investment securities	(51)	(511)
Net gain on sale and disposal of equipment	(5)	
Increase in bank owned life insurance, net of expenses	(195)	(190)
Write down of other real estate owned	283	
Net decrease (increase) in accrued interest receivable and other assets	1,612	(143)
Net decrease in prepaid FDIC Assessments	501	
Net increase (decrease) in accrued interest payable and other liabilities	131	(1,204)
Provision for deferred income taxes	(1,028)	(8)
Net cash provided by operating activities	6,642	4,023
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of available-for-sale investment securities	(15,758)	(25,490)
Purchases of held-to-maturity investment securities		(3)
Proceeds from sales or calls of available-for-sale investment securities	15,698	23,620
Proceeds from maturity of available-for-sale investment securities	156	2,885
Proceeds from principal repayments of available-for-sale investment securities	13,200	16,872
Proceeds from principal repayments of held-to-maturity investment securities		1,500
Net decrease (increase) in interest bearing deposits in other banks	7,301	(100)
Net increase in loans	(13,095)	(13,266)
Proceeds from sale of other real estate owned	2,181	
Purchases of premises and equipment	(151)	(359)
FHLB stock redeemed	90	
Proceeds from bank owned life insurance		430
Proceeds from sale of premises and equipment	5	
Net cash provided by investing activities	9,627	6,089
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase (decrease) in demand, interest bearing and savings deposits	10,262	(19,997)
Net (decrease) increase in time deposits	(19,120)	6,658
Proceeds from issuance of Series A Preferred Stock and warrants		7,000
Proceeds from short-term borrowings from Federal Home Loan Bank		10,000
Repayments of short-term borrowings to Federal Home Loan Bank	(5,000)	
Repayments of borrowings from other financial institutions		(6,368)

Proceeds from exercise of stock options		524		97
Tax benefit from exercise of stock options		25		8
Cash paid for preferred stock dividends		(175)		(102)
Net cash used in financing activities		(13,484)		(2,704)
Increase in cash and cash equivalents		2,785		7,408
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		14,136		19,518
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$	16,921	$	26,926
SUPPLEMENTAL DISCLOSURE OF CASH FLOWS INFORMATION:				
Cash paid during the year for:				
Interest	$	2,518	$	3,930
Income taxes	$	301	$	450
Non-Cash Investing Activities:				
Net pre-tax change in unrealized gain (losses) on available-for-sale investment securities	$	3,243	$	(3,453)
Non-Cash Financing Activities:				
Transfer of loans to other real estate owned	$	3,134	$	2,550
Accrued preferred stock dividends	$	44	$	44

See notes to unaudited consolidated financial statements

Table of Contents

CENTRAL VALLEY COMMUNITY BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Basis of Presentation

The interim unaudited consolidated financial statements of Central Valley Community Bancorp and subsidiary have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC). These interim consolidated financial statements include the accounts of Central Valley Community Bancorp and its wholly owned subsidiary Central Valley Community Bank (the Bank) (collectively, the Company). All significant intercompany accounts and transactions have been eliminated in consolidation. Certain information and footnote disclosures normally included in the annual consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted. The Company believes that the disclosures are adequate to make the information presented not misleading. These interim consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company s 2009 Annual Report to Shareholders on Form 10-K. In the opinion of management, all adjustments, consisting of only normal recurring adjustments, necessary to present fairly the Company s financial position and shareholders equity at June 30, 2010 and December 31, 2009, and the results of its operations for the three and six month interim periods ended June 30, 2010 and June 30, 2009 and its cash flows for the six month interim periods ended June 30, 2010 and June 30, 2009 have been included. Certain reclassifications have been made to prior year amounts to conform to the 2010 presentation. The results of operations for interim periods are not necessarily indicative of results for the full year.

The preparation of these consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Management has determined that since all of the banking products and services offered by the Company are available in each branch of the Bank, all branches are located within the same economic environment and management does not allocate resources based on the performance of different lending or transaction activities, it is appropriate to aggregate the Bank branches and report them as a single operating segment. No customer accounts for more than 10 percent of revenues for the Company or the Bank.

Recent Accounting Pronouncements

Fair Value Measurements and Disclosures

In January 2010, the FASB issued ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements (ASU 10-06). ASU 10-06 revises two disclosure requirements concerning fair value measurements and clarifies two others. It requires separate presentation of significant transfers into and out of Levels 1 and 2 of the fair value hierarchy and disclosure of the reasons for such transfers. It will also require the presentation of purchases, sales, issuances and settlements within Level 3 on a gross basis rather than a net basis. The amendments also clarify that disclosures should be disaggregated by class of asset or liability and that disclosures

about inputs and valuation techniques should be provided for both recurring and non-recurring fair value measurements. The Company s disclosures about fair value measurements are presented in Note 5: Fair Value Measurements. These new disclosure requirements were adopted by the Company in the first quarter of 2010, with the exception of the requirement concerning gross presentation of Level 3 activity, which is effective for fiscal years beginning after December 15, 2010 and they did not have a material impact on its financial condition or results of operations. Management does not believe that the adoption of the remaining portion of this ASU will have a material impact on the Company s financial position, results of operations, cash flows, or disclosures.

Table of Contents

Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses

In July 2010, the FASB issued Accounting Standards Update No. 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses.* This standard expands disclosures about credit quality of financing receivables and the allowance for loan losses. The standard will require the Company to expand disclosures about the credit quality of our loans and the related reserves against them. The extra disclosures will include disaggregated matters related to our past due loans, credit quality indicators, and modifications of loans. The Company will adopt the standard beginning with our December 31, 2010 financial statements. This standard will not have an impact on the Company s financial position or results of operations.

Impact of New Financial Accounting Standards

Accounting for Transfers of Financial Assets

In June 2009, the FASB issued ASC Topic 860 (previously SFAS No. 166), *Accounting for Transfers of Financial Assets, an amendment of SFAS No. 140.* This standard amends the derecognition accounting and disclosure guidance included in previously issued standards. This standard eliminates the exemption from consolidation for qualifying special-purpose entities (SPEs) and also requires a transferor to evaluate all existing qualifying SPEs to determine whether they must be consolidated in accordance with ASC Topic 810. This standard also provides more stringent requirements for derecognition of a portion of a financial asset and establishes new conditions for reporting the transfer of a portion of a financial asset as a sale. This standard is effective as of the beginning of the first annual reporting period that begins after November 15, 2009. The Company adopted the provisions of this standard January 1, 2010 and they did not have a material impact on its financial condition or results of operations.

Transfers and Servicing

In December 2009, the FASB issued Accounting Standards Update (ASU) 2009-16, *Transfers and Servicing (ASC Topic 860): Accounting for Transfers of Financial Assets,* which updates the derecognition guidance in ASC Topic 860 for previously issued SFAS No. 166. This update reflects the Board s response to issues entities have encountered when applying ASC 860, including: (1) requires that all arrangements made in connection with a transfer of financial assets be considered in the derecognition analysis, (2) clarifies when a transferred asset is considered legally isolated from the transferor, (3) modifies the requirements related to a transferee s ability to freely pledge or exchange transferred financial assets, and (4) provides guidance on when a portion of a financial asset can be derecognized. This update is effective for financial asset transfers occurring after the beginning of an entity s first fiscal year that begins after November 15, 2009. Early adoption is prohibited. The Company adopted the provisions of this standard January 1, 2010 and they did not have a material impact on its financial condition or results of operations.

Improvements to Financial Reporting of Interests in Variable Interest Entities

In June 2009, the FASB issued ASC Topic 810 (previously SFAS No. 167), *Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities.* This standard amends the consolidation guidance applicable to variable interest entities. The amendments to the consolidation guidance affect all entities currently within the scope of ASC Topic 810, as well as qualifying special-purpose entities that are currently excluded from the scope of ASC Topic 810. This standard is effective as of the beginning of the first annual reporting period that begins after November 15, 2009. The Company adopted the provisions of this standard January 1, 2010 and they did not have a material impact on its financial condition or results of operations.

Note 2. Share-Based Compensation

On June 30, 2010, the Company has three stock-based compensation plans which are described below.

During 1992, the Bank established a Stock Option Plan for which shares are reserved for issuance to employees and directors under incentive and nonstatutory agreements. The Company assumed all obligations under this plan as of November 15, 2000, and options to purchase shares of the Company s common stock were substituted for options to purchase shares of common stock of the Bank. Outstanding options under this plan are exercisable until their expiration, however, no new options will be granted under this plan.

On November 15, 2000, the Company adopted, and subsequently amended on December 20, 2000, the Central Valley Community Bancorp 2000 Stock Option Plan for which 593,804 shares remain reserved for issuance for options already granted to employees and directors under incentive and nonstatutory agreements and 15,091 remain reserved for future grants as of June 30, 2010. The plan requires that the option price may not be less than the fair market value of the stock at the date the option is granted, and that the option price must be paid in full at the time it is exercised. The options under the plan expire on dates determined by the Board of Directors, but not later than ten years from the date of grant. The vesting period is determined by the Board of Directors and is generally over five years.

In May 2005, the Company adopted the Central Valley Community Bancorp 2005 Omnibus Incentive Plan (2005 Plan). The plan provides for awards in the form of incentive stock options, non-statutory stock options, stock appreciation rights, and restricted stock. The plan also allows for performance awards that may be in the form of cash or shares of the Company, including restricted stock. The maximum number of shares that can be issued with respect to all awards under the plan is 476,000. Currently under the 2005 Plan, there are 43,000 shares reserved for issuance for options already granted to employees and 433,000 remain reserved for future grants as of June 30, 2010. The plan requires that the exercise price may not be less than 100% of the market value of the stock at the date the option is granted, and that the option price must be paid in full at the time it is exercised. The options and awards under the plan expire on dates determined by the Board of Directors, but not later than 10 years from the date of grant. The vesting period for the options and option related stock appreciation rights is determined by the Board of Directors and is generally over five years.

Table of Contents

For the six month periods ended June 30, 2010 and 2009, the compensation cost recognized for stock option compensation was $113,000 and $149,000, respectively. For the quarter ended June 30, 2010 and 2009, compensation cost recognized was $57,000 and $72,000, respectively. The recognized tax benefit for stock option compensation expense was $26,000 and $19,000, for the six month periods ended June 30, 2010 and 2009, respectively. For the three month periods ended June 30, 2010 and 2009, recognized tax benefits were $13,000.

The Company bases the fair value of the options granted on the date of grant using a Black-Scholes Merton option pricing model that uses assumptions based on expected option life and the level of estimated forfeitures, expected stock volatility, risk free interest rate, and dividend yield. The expected term of the Company s options was determined under the applicable guidance for estimating expected term of options. Stock volatility is based on the historical volatility of the Company s stock. The risk-free rate is based on the U. S. Treasury yield curve for the periods within the contractual life of the options in effect at the time of grant. The compensation cost for options granted is based on the weighted average grant date fair value per share.

Options to purchase 1,000 shares of the Company s common stock were issued in the first half of 2010 and in the same period of 2009, options to purchase 13,500 shares of the Company s common stock were issued from the 2005 Plan at an exercise price equal to the fair market value at the grant date

A summary of the combined activity of the Plans for the six month period ended June 30, 2010 follows:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Options outstanding at January 1, 2010	789,934			
Options granted	1,000	$ 5.30		
Options exercised	(153,400)	$ 3.42		
Options canceled	(730)	$ 9.49		
Options outstanding at June 30, 2010	636,804	$ 7.49	3.51	$ 518
Options vested or expected to vest at June 30, 2010	578,054	$ 7.37	4.36	$ 476
Options exercisable June 30, 2010	546,316	$ 7.32	3.00	$ 507

The weighted-average grant-date fair value of options granted in the six month period ended June 30, 2010 and 2009 was $2.34 and $1.33 respectively.

The total intrinsic value of 153,400 options exercised in the six months ended June 30, 2010 was $340,000. The intrinsic value of 22,522 options exercised in the six months ended June 30, 2009 was $18,000.

Cash received from options exercised for the six months ended June 30, 2010 was $524,000. The actual tax benefit realized for the tax deductions from options exercised totaled $25,000 for six months ended June 30, 2010.

As of June 30, 2010, there was $341,000 of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under all plans. The cost is expected to be recognized over a weighted average period of two years.

Note 3. Earnings per share

Basic earnings per share (EPS), which excludes dilution, is computed by dividing income available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock, such as stock options or warrants, stock appreciation rights settled in stock or restricted stock awards, result in the issuance of common stock which shares in the earnings of the Company. There was no difference in the net income used in the calculation of basic earnings per share and diluted earnings per share for the Six month periods ended June 30, 2010 and 2009.

Table of Contents

A reconciliation of the numerators and denominators of the basic and diluted EPS computations is as follows:

Basic Earnings Per share In thousands (except share and per share amounts)	**Three Months Ended June 30,**		**For the Six Months Ended June 30,**	
	2010	**2009**	**2010**	**2009**
Net Income	$ 504	$ 464	$ 1,796	$ 1,723
Less: Preferred stock dividends and accretion	99	135	198	184
Income available to common shareholders	$ 405	$ 329	$ 1,598	$ 1,539
Weighted average shares outstanding	9,131,753	7,651,918	9,051,168	7,647,128
Net income per share	$ 0.04	$ 0.04	$ 0.18	$ 0.20

Diluted Earnings Per share In thousands (except share and per share amounts)	**Three Months Ended June 30,**		**For the Six Months Ended June 30,**	
	2010	**2009**	**2010**	**2009**
Net Income	$ 504	$ 464	$ 1,796	$ 1,723
Less: Preferred stock dividends and accretion	99	135	198	184
Income available to common shareholders	$ 405	$ 329	$ 1,598	1,539
Weighted average shares outstanding	9,131,753	7,651,918	9,051,168	7,647,128
Effect of dilutive stock options	79,085	108,096	97,556	118,391
Weighted average shares of common stock and common stock equivalents	9,210,838	7,760,014	9,148,724	7,765,519
Net income per diluted share	$ 0.04	$ 0.04	$ 0.17	$ 0.20

Note 4. Investments

The investment portfolio consists primarily of agency securities, mortgage backed securities, and municipal securities and are classified available-for-sale. As of June 30, 2010, $126,295,000 was held as collateral for borrowing arrangements, public funds, and for other purposes. Total investments were $186,436,000 at June 30, 2010 compared to $197,319,000 at December 31, 2009, a decrease of $10,883,000, or 5.5%.

The fair value of the available-for-sale investment portfolio reflected an unrealized gain of $818,000 at June 30, 2010 compared to an unrealized loss of $2,425,000 at December 31, 2009.

The following table sets forth the carrying values and estimated fair values of our investment securities portfolio at the dates indicated:

Available-for-Sale Securities	**June 30, 2010**
	Amortized Cost

		Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt Securities:				
U.S. Government agencies	$ 223	$ 8	$	$ 231
Obligations of states and political subdivisions	69,083	3,640	(556)	72,167
U.S. Government agencies collateralized by mortgage obligations	82,452	1,622	(148)	83,926
Other collateralized mortgage obligations	25,714	268	(4,215)	21,767
Corporate debt securities	500	16		516
Other equity securities	7,646	183		7,829
	$ 185,618	$ 5,737	$ (4,919)	$ 186,436

Table of Contents

Available-for-Sale Securities	December 31, 2009 Amortized Cost		Gross Unrealized Gains		Gross Unrealized Losses		Estimated Fair Value
Debt Securities:							
U.S. Government agencies	$	353	$	10	$		$ 363
Obligations of states and political subdivisions		68,708		3,050		(946)	70,812
U.S. Government agencies collateralized by mortgage obligations		85,530		1,283		(858)	85,955
Other collateralized mortgage obligations		36,280		403		(5,413)	31,270
Corporate debt securities		1,228		86			1,314
Other equity securities		7,645				(40)	7,605
	$	199,744	$	4,832	$	(7,257)	$ 197,319

Investment securities with unrealized losses as of the dates indicated are summarized and classified according to the duration of the loss period as follows:

	June 30, 2010					
	Less than 12 Months		12 Months or More		Total	
Available-for-Sale Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Debt Securities:						
Obligations of states and political subdivisions	$ 5,717	$ (111)	$ 4,487	$ (445)	$ 10,204	$ (556)
U.S. Government agencies collateralized by mortgage obligations	19,807	(148)	226		20,033	(148)
Other collateralized mortgage obligations	1,103	(9)	16,081	(4,206)	17,184	(4,215)
	$ 26,627	$ (268)	$ 20,794	$ (4,651)	$ 47,421	$ (4,919)

	December 31, 2009					
	Less than 12 Months		12 Months or More		Total	
Available-for-Sale Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Debt Securities:						
Obligations of states and political subdivisions	$ 9,001	$ (295)	$ 4,911	$ (651)	$ 13,912	$ (946)
U.S. Government agencies collateralized by mortgage obligations	40,691	(856)	331	(2)	41,022	(858)
Other collateralized mortgage obligations	3,474	(446)	19,878	(4,967)	23,352	(5,413)
Other securities	7,605	(40)			7,605	(40)
	$ 60,771	$ (1,637)	$ 25,120	$ (5,620)	$ 85,891	$ (7,257)

As of June 30, 2010, the Company performed an analysis of the investment portfolio to determine whether any of the investments held in the portfolio had an other-than-temporary impairment (OTTI). Management evaluated all available-for-sale investment securities with an unrealized loss at June 30, 2010 and identified those that had an unrealized loss for at least a consecutive 12 month period, which had an unrealized loss at June 30, 2010 greater than 10% of the recorded book value on that date, or which had an unrealized loss of more than $10,000. In addition, management reviewed all private label residential mortgage backed securities (PLRMBS) at June 30, 2010.

Table of Contents

For those bonds that met the evaluation criteria management obtained and reviewed the most recently published national credit ratings for those bonds. For those bonds that were municipal debt securities with an investment grade rating by the rating agencies, management also evaluated the financial condition of the municipality and any applicable municipal bond insurance provider and concluded that no credit related impairment existed based on the rating. The evaluation for PLRMBS also includes estimating projected cash flows that the Company is likely to collect based on an assessment of all available information about the applicable security on an individual basis, the structure of the security, and certain assumptions, such as the remaining payment terms for the security, prepayment speeds, default rates, loss severity on the collateral supporting the security based on underlying loan-level borrower and loan characteristics, expected housing price changes, and interest rate assumptions, to determine whether the Company will recover the entire amortized cost basis of the security. In performing a detailed cash flow analysis, the Company identified the best estimate of the cash flows expected to be collected. If this estimate results in a present value of expected cash flows (discounted at the security s effective yield) that is less than the amortized cost basis of the security, an OTTI is considered to have occurred.

To assess whether it expects to recover the entire amortized cost basis of its PLRMBS, the Company performed a cash flow analysis for all of its PLRMBS as of June 30, 2010. In performing the cash flow analysis for each security, the Company uses a third-party model. The model considers borrower characteristics and the particular attributes of the loans underlying the Company s securities, in conjunction with assumptions about future changes in home prices and other assumptions, to project prepayments, default rates, and loss severities. In addition for those PLRMBS that were rated below investment grade, management contracted with a third party evaluation specialist to determine if a credit loss existed.

The month-by-month projections of future loan performance are allocated to the various security classes in each securitization structure in accordance with the structure s prescribed cash flow and loss allocation rules. When the credit enhancement for the senior securities in a securitization is derived from the presence of subordinated securities, losses are allocated first to the subordinated securities until their principal balance is reduced to zero. The projected cash flows are based on a number of assumptions and expectations, and the results of these models can vary significantly with changes in assumptions and expectations. The scenario of cash flows determined based on the model approach described above reflects a best-estimate scenario.

At each quarter end, the Company compares the present value of the cash flows expected to be collected on its PLRMBS to the amortized cost basis of the securities to determine whether a credit loss exists.

The unrealized losses associated with private residential PLRMBS are primarily driven by higher projected collateral losses, wider credit spreads, and changes in interest rates. The Company assesses for credit impairment using a discounted cash flow model. The key assumptions include home price depreciation, default rates, severities, discount rates and prepayment rates. Losses are estimated to a security by forecasting the underlying mortgage loans in each transaction. The forecasted loan performance is used to project cash flows to the various tranches in the structure. Based upon management s assessment of the expected credit losses of the security given the performance of the underlying collateral compared with our credit enhancement (which occurs as a result of credit loss protection provided by subordinated tranches), the Company expects to recover the entire amortized cost basis of these securities, with the exception of certain securities for which OTTI was recorded.

At June 30, 2010, the Company had a total of 42 PLRMBS with a remaining principal balance of $21,767,000 and a net unrealized loss of approximately $3,947,000. 15 of these securities account for $4,215,000 of the unrealized loss at June 30, 2010 offset by 27 of these securities with gains totaling $268,000. 12 of these PLRMBS with a remaining principal balance of $17, 328,000 had credit ratings below investment grade. The Company continues to perform extensive analyses on these securities as well as all whole loan CMOs. Several of these investment securities continue to demonstrate cash flows and credit support as expected and the expected cash flows of the security discounted at the security s effective yield are greater than the book value of the security, therefore management does not consider these securities to be other than temporarily impaired. Based on the analyses performed, eight PLRMBS with a remaining principal balance of $17,044,000 were considered to

be other than temporarily impaired at June 30, 2010 for which we recorded an OTTI charge of $700,000 was recorded against earnings. This charge was taken to reflect ongoing and increasing deterioration of credit quality and increasing loss severities of the underlying mortgages. However, the cumulative unrealized loss on these securities decreased during the three and six months ended June 30, 2010 primarily due to a declining interest rate environment. This unrealized gain was recognized in other comprehensive income and is also presented in the income statement as a component of non-interest income in the presentation of other-than-temporary impairment losses.

Table of Contents

Investment securities as of June 30, 2010 with credit ratings below investment grade are summarized in the table below (dollars in thousands):

Description	Book Value	Market Value	Unrealized (Loss) or Gain	Rating	Agency	12 Month Historical Prepayment Rates %	Projected Default Rates %	Projected Severity Rates %	Original Purchase Price %	Current Credit Enhancement %
PHHAM	$ 3,322	$ 2,682	$ (640)	CC	Fitch	13.61	23.69	50.00	97.25	5.53
RAST	2,913	2,144	(769)	C	Fitch	12.59	24.63	56.78	98.50	1.55
CWALT 1	1,092	826	(266)	CC	Fitch	12.90	26.60	58.35	100.73	7.81
CWALT 2	465	406	(59)	CC	Fitch	12.01	26.66	55.13	101.38	7.03
CWALT 3	2,494	2,173	(321)	CCC	S&P	10.39	22.07	46.08	100.25	10.16
FHAMS	2,714	2,265	(449)	CC	Fitch	14.17	18.89	50.00	95.00	3.37
CHASE	322	320	(2)	CC	Fitch	19.05	17.88	43.87	93.25	4.94
CWHL	192	194	2	BB-	S&P	15.58	10.06	22.01	97.42	7.24
GSR	2,712	2,371	(341)	CC	Fitch	14.05	19.04	47.23	96.25	4.34
CONHE	98	94	(4)	BB+	S&P	2.90	16.3	40.00	86.39	0.006
BOAA 2	214	172	(42)	BB	Fitch	7.93	9.38	51.75	97.25	5.70
RAMP	790	782	(8)	BB	S&P	17.95	2.14	29.49	105.69	17.63
TOTALS	$ 17,328	$ 14,429	$ (2,899)							

The following table provides a roll forward as of June 30, 2010 of investment securities credit losses recorded in earnings. The beginning balance represents the credit loss component for which OTTI occurred on debt securities in prior periods. Additions represent the first time a debt security was credit impaired or when subsequent credit impairments have occurred on securities for which OTTI credit losses have been previously recognized.

(Dollars in thousands)	OTTI Related to Credit Loss	OTTI Related to All Other Factors	Total OTTI
Balance, December 31, 2009	$ 300	$	$ 300
Charges on Securities for which OTTI was not previously recognized	700	3,068	3,768
Realized losses for securities sold	(300)		(300)
Balance, June 30, 2010	$ 700	$ 3,068	$ 3,768

Note 5. Fair Value Measurements

The estimated carrying and fair values of the Company s financial instruments are as follows (in thousands):

	June 30, 2010		December 31, 2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and due from banks	$ 16,171	$ 16,171	$ 13,857	$ 13,857
Interest-earning deposits in other banks	27,243	27,243	34,544	34,544
Federal funds sold	750	750	279	279

Available-for-sale investment securities	186,436	186,436	197,319	197,319
Loans, net	457,184	456,095	449,007	460,238
Bank owned life insurance	11,193	11,193	10,998	10,998
FHLB stock	3,050	3,050	3,140	3,140
Accrued interest receivable	3,286	3,286	3,608	3,608

Financial liabilities:								
Deposits	$	631,309	$	632,739	$	640,167	$	641,279
Short-term borrowings		10,000		10,000		5,000		5,000
Long-term debt		4,000		4,408		14,000		14,487
Junior subordinated defer-rable interest debentures		5,155		5,155		5,155		5,155
Accrued interest payable		458		458		416		416

These estimates do not reflect any premium or discount that could result from offering the Company s entire holdings of a particular financial instrument for sale at one time, nor do they attempt to estimate the value of anticipated future business related to the instruments. In addition, the tax ramifications related to the realization of unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of these estimates.

These estimates are made at a specific point in time based on relevant market data and information about the financial instruments. Because no market exists for a significant portion of the Company s financial instruments, fair value estimates are based on judgments regarding current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the fair values presented.

The following methods and assumptions were used to estimate the fair value of financial instruments. For cash and due from banks, interest-earning deposits in other banks, Federal funds sold, variable-rate loans, bank owned life insurance, accrued interest receivable and payable, FHLB stock, demand deposits and short-term borrowings, the carrying amount is estimated to be fair value. For investment securities, fair values are based on quoted market prices, quoted market prices for similar securities and indications of value provided by brokers. The fair values for fixed-rate loans are estimated using discounted cash flow analyses, using interest rates currently being offered at each reporting date for loans with similar terms to borrowers of comparable creditworthiness. Fair values for fixed-rate certificates of deposit are estimated using discounted cash flow analyses using interest rates offered at each reporting date by the Company for certificates with similar remaining maturities. The fair value of long-term debt and subordinated debentures was determined based on the current market for like-kind instruments of a similar maturity and structure. The fair values of commitments are estimated using the fees currently charged to enter into similar agreements and are not significant and, therefore, not included in the above table.

Fair Value Hierarchy

In accordance with applicable guidance, the Company groups its assets and liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. Valuations within these levels are based upon:

Level 1 Quoted market prices for identical instruments traded in active exchange markets.

Level 2 Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable or can be corroborated by observable market data.

Level 3 Model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect the Company s estimates of assumptions that market participants would use on pricing the asset or liability. Valuation techniques include management judgment and estimation which may be significant.

Assets Recorded at Fair Value

The following tables present information about the Company s assets and liabilities measured at fair value on a recurring and nonrecurring basis as of June 30, 2010:

Recurring Basis

The Company is required or permitted to record the following assets at fair value on a recurring basis under other accounting pronouncements (in thousands).

Description	**Fair Value**	**Level 1**	**Level 2**	**Level 3**
Available-for-sale investment securities	$ 186,436	$ 18	$ 178,607	$ 7,811

Table of Contents

Fair values for available-for-sale investment securities, which include debt securities of U.S. Governmental agencies and obligations of states and political subdivisions, are based on quoted market prices for similar securities. The securities in Level 3 are not actively traded therefore the pricing is internally calculated using matrix pricing.

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows.

(In thousands)	**Available-for-sale Investment Securities Three Months Ended June 30, 2010**	**Available-for-sale Investment Securities Six Months Ended June 30, 2010**
Beginning balance	$ 8,437	$ 14,097
Total gains or losses (realized/unrealized)		
Included in earnings (or changes in net assets)	235	248
Included in other comprehensive income	24	316
Purchases, sales and principal payments	(885)	(3,772)
Transfers in and/or out of Level 3		(3,078)
Ending balance	$ 7,811	$ 7,811

Gains and losses (realized and unrealized) included in earnings (or changes in net assets) for the three month period ended June 30, 2010 totaled $30,000 and were included in other revenue.

Non-recurring Basis

The Company may be required, from time to time, to measure certain assets at fair value on a non-recurring basis. These include assets that are measured at the lower of cost or fair value that were recognized at fair value which was below cost at June 30, 2010 (in thousands).

Description	**Fair Value**	**Level 1**	**Level 2**	**Level 3**	**Total Losses**
Impaired loans	$ 10,130	$	$	$ 10,130	$ (1,611)
Other real estate owned	3,502			3,502	
Total assets and liabilities measured at fair value on a non-recurring basis	$ 13,632	$	$	$ 13,632	$ (1,611)

The fair value of impaired loans and other real estate owned is based on the fair value of the collateral for all collateral dependent loans and for other impaired loans is estimated using a discounted cash flow model. Impaired loans and other real estate owned were determined to be collateral dependent and categorized as Level 3 due to ongoing real estate market conditions resulting in inactive market data, which in turn required the use of unobservable inputs and assumptions in fair value measurements. There were no changes in valuation techniques used during the three months ended June 30, 2010 or the year ended December 31, 2009.

Impaired loans had a principal balance of $12,428,000 with a related valuation allowance of $2,298,000 at June 30, 2010. The valuation allowance is reflected specific allocations of the allowance for credit losses for impaired loans.

The fair value of real estate is based on property appraisals at the time of transfer and as appropriate thereafter, less estimated costs to sell. Other real estate owned is periodically reviewed to determine whether the property continues to be carried at the lower of its recorded book value or estimated fair value, net of estimated selling costs. Fair value of other real estate properties was $3,502,000 at June 30, 2010.

The following tables present information about the Company s assets and liabilities measured at fair value on a recurring and non-recurring basis as of December 31, 2009:

Recurring Basis

The Company is required or permitted to record the following assets at fair value on a recurring basis under other accounting pronouncements (in thousands).

Description	**Fair Value**	**Level 1**	**Level 2**	**Level 3**
Available-for-sale investment securities	$ 197,319	$ 17	$ 183,205	$ 14,097

Table of Contents

Fair values for available-for-sale investment securities, which include debt securities of U.S. Governmental agencies and obligations of states and political subdivisions, are based on quoted market prices for similar securities. The securities in Level 3 are not actively traded and therefore the pricing is internally calculated using matrix pricing.

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows for the year ended December 31, 2009 (in thousands).

		Available-for-Sale Investment Securities
Beginning balance	$	16,164
Total gains or losses (realized/unrealized)		
Included in earnings (or changes in net assets)		283
Included in other comprehensive income		809
Purchases, sales and principal payments		(884)
Transfers in and/or out of Level 3		(2,275)
Ending balance	$	14,097

Gains and losses (realized and unrealized) included in earnings (or changes in net assets) for the year ended December 31, 2009 totaled $283,000 and were included in other revenues.

Non-recurring Basis

The Company may be required, from time to time, to measure certain assets at fair value on a non-recurring basis. These include assets that are measured at the lower of cost or fair value that were recognized at fair value which was below cost at December 31, 2009 (in thousands).

Description		Fair Value		Level 1		Level 2		Level 3		Total Losses
Impaired loans	$	4,751	$		$		$	4,751	$	(3,253)
Other real estate owned		2,832						2,832		(356)
Other		47						47		(50)
Total assets and liabilities measured at fair value on a non-recurring basis	$	7,630	$		$		$	7,630	$	(3,659)

The fair value of impaired loans and other real estate owned is based on the fair value of the collateral for all collateral dependent loans and for other impaired loans is estimated using a discounted cash flow model. Impaired loans and other real estate owned were determined to be collateral dependent and categorized as Level 3 due to ongoing real estate market conditions resulting in inactive market data, which in turn required the use of unobservable inputs and assumptions in fair value measurements.

In accordance with the provisions of ASC 360-10, impaired loans with a carrying value of $9,112,000 were written down to their fair value of $4,751,000, resulting in an impairment charge of $3,253,000, which included $2,501,000 in charge offs and specific reserve of $752,000 for the period ended December 31, 2009. Other real estate properties with carrying amounts totaling $3,189,000 at foreclosure were subsequently written down to their fair values of $2,832,000, resulting in a loss of $356,000 which was included in other expense for the period. Other repossessed assets with carrying amounts totaling $97,000 were written down to their fair values of $47,000, resulting in a loss of $50,000 which was included in other expense for the period ended December 31, 2009.

Note 6. Goodwill and Intangible Assets

Business combinations involving the Company s acquisition of the equity interests or net assets of another enterprise give rise to goodwill. Total goodwill at June 30, 2010 was $23,577,000 consisting of $14,643,000 and $8,934,000 representing the excess of the cost of Service 1st Bank and Bank of Madera County, respectively, over the net amounts assigned to assets acquired and liabilities assumed in the transactions accounted for under the purchase method of accounting. The value of goodwill is ultimately derived from the Bank s ability to generate net earnings after the acquisitions and is not deductible for tax purposes. A decline in net earnings could be indicative of a decline in the fair value of goodwill and result in impairment. For that reason, goodwill is assessed at least annually for impairment. Management engaged an independent valuation specialist to perform our annual impairment test in the third quarter of 2009 and no impairment was recorded.

Goodwill is also tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of the Company below its carrying amount. No such events or circumstances arose during the second quarter of 2010, so goodwill was not required to be retested.

Table of Contents

The intangible assets at June 30, 2010 represent the estimated fair value of the core deposit relationships acquired in the acquisition of Service 1st Bank in 2008 of $1,400,000 and the 2005 acquisition of Bank of Madera County of $1,500,000. Core deposit intangibles are being amortized by the straight-line method over an estimated life of seven years from the date of acquisition. The carrying value of intangible assets at June 30, 2010 was $1,405,000 net of $1,495,000 in accumulated amortization expense. Management evaluates the remaining useful lives quarterly to determine whether events or circumstances warrant a revision to the remaining periods of amortization. Based on the evaluation, no changes to the remaining useful lives was required in the second quarter of 2010. Management engaged an independent valuation specialist to perform our annual impairment test on core deposit intangibles in the third quarter of 2009 and determined no impairment was necessary. Amortization expense recognized was $103,000 for the three month periods ended June 30, 2010 and 2009 and $207,000 for the six months period ended June 30, 2010 and 2009.

Note 7. Comprehensive Income

Total comprehensive income (loss) for the six months ended June 30, 2010 and 2009 totaled $3,741,000 and ($1,750,000) respectively. Comprehensive income (loss) is comprised of unrealized gains (losses), net of taxes, on available-for-sale investment securities, which were $1,218,000 and ($1,359,000) for the three months ended June 30, 2010 and 2009, respectively, together with net income.

At June 30, 2010 and December 31, 2009, accumulated other comprehensive loss totaled $490,000 and ($1,455,000), respectively, and is reflected, net of taxes, as a component of shareholders equity.

Note 8. Commitments and Contingencies

In the normal course of business, the Company is a party to financial instruments with off-balance sheet risk. These financial instruments include commitments to extend credit and standby letters of credit**.** These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheets. The contract or notional amounts of these instruments reflect the extent of involvement the Company has in particular classes of financial instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for loans.

Commitments to extend credit amounting to $120,147,000 and $131,139,000 were outstanding at June 30, 2010 and December 31, 2009, respectively. Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract unless waived by the bank. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee.

Included in commitments to extend credit are undisbursed lines of credit totaling $68,352,000 and $81,125,000 at June 30, 2010 and December 31, 2009, respectively. Undisbursed lines of credit are revolving lines of credit whereby customers can repay principal and request principal advances during the term of the loan at their discretion and most expire between one and 12 months.

The Company has undisbursed portions of construction loans totaling $6,067,000 and $6,661,000 as of June 30, 2010 and December 31, 2009, respectively. These commitments are agreements to lend to a customer, subject to meeting certain construction progress requirements established in the contract. The underlying construction loans have fixed expiration dates.

Standby letters of credit and financial guarantees amounting to $265,000 and $240,000 were outstanding at June 30, 2010 and December 31, 2009, respectively. Standby letters of credit and financial guarantees are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support private borrowing arrangements. Most standby letters of credit and guarantees carry a one year term or less. The fair value of the liability related to these standby letters of credit, which represents the fees received for their issuance, was not significant at June 30, 2010 and December 31, 2009. The Company recognizes these fees as revenue over the term of the commitment or when the commitment is used.

The Company generally requires collateral or other security to support financial instruments with credit risk. Management does not anticipate any material loss will result from the outstanding commitments to extend credit, standby letters of credit and financial guarantees.

The Company is subject to legal proceedings and claims which arise in the ordinary course of business. In the opinion of management, the amount of ultimate liability with respect to such actions will not materially affect the consolidated financial position or consolidated results of operations of the Company.

Note 9. Income Taxes

The Company files its income taxes on a consolidated basis with its subsidiaries. The allocation of income tax expense (benefit) represents each entity s proportionate share of the consolidated provision for income taxes. Deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. On the consolidated balance sheets, net deferred tax assets are included in accrued interest receivable and other assets. The Company establishes a tax valuation allowance when it is more likely than not that a recorded tax benefit is not expected to be fully realized. The expense to create the tax valuation is recorded as an additional income tax expense in the period the tax valuation allowance is created. Based on management s analysis as of June 30, 2010, no valuation allowance was deemed necessary.

Table of Contents

Accounting for uncertainty in income taxes - The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more likely than not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination. The Company recognizes accrued interest and penalties related to unrecognized tax benefits as a component of tax expense in the consolidated statements of income. There have been no significant changes to unrecognized tax benefits or accrued interest and penalties for the six months ended June 30, 2010.

Note 10. Borrowing Arrangements

Federal Home Loan Bank Advances: Advances from the Federal Home Loan Bank (FHLB) of San Francisco consisted of the following:

June 30, 2010

Amount	Rate	Maturity Date
	(Dollars in thousands)	
$ 5,000	3.00%	February 7, 2011
5,000	3.10%	February 14, 2011
4,000	3.59%	February 13, 2013
14,000		
(10,000)	Less short-term portion	
$ 4,000	Long-term debt	

December 31, 2009

Amount	Rate	Maturity Date
	(Dollars in thousands)	
$ 5,000	2.73%	February 5, 2010
5,000	3.00%	February 7, 2011
5,000	3.10%	February 14, 2011
4,000	3.59%	February 13, 2013
19,000		
(5,000)	Less short-term portion	
$ 14,000	Long-term debt	

FHLB advances are secured by investment securities with amortized costs totaling $32,642,000 and $45,239,000, and market values totaling $35,956,000 and $44,808,000 at June 30, 2010 and December 31, 2009, respectively. The Bank s credit limit varies according to the amount and composition of the investment and loan portfolios pledged as collateral.

As of June 30, 2010 and December 31, 2009, the Company had no Federal funds purchased.

ITEM 2: MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Certain matters discussed in this report constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements contained herein that are not historical facts, such as statements regarding the Company s current business strategy and the Company s plans for future development and operations, are based upon current expectations. These statements are forward-looking in nature and involve a number of risks and uncertainties. Such risks and uncertainties include, but are not limited to (1) significant increases in competitive pressure in the banking industry; (2) the impact of changes in interest rates, a decline in economic conditions at the international, national or local level on the Company s results of operations, the Company s ability to continue its internal growth at historical rates, the Company s ability to maintain its net interest margin, and the quality of the Company s earning assets; (3) changes in the regulatory environment; (4) fluctuations in the real estate market; (5) changes in business conditions and inflation; (6) changes in securities markets; and (7) risks associated with acquisitions, relating to difficulty in integrating combined operations and related negative impact on earnings, and incurrence of substantial expenses. Therefore, the information set forth in such forward-looking statements should be carefully considered when evaluating the business prospects of the Company.

When the Company uses in this Quarterly Report on Form 10-Q the words anticipate, estimate, expect, project, intend, commit, and similar expressions, the Company intends to identify forward-looking statements. Such statements are not guarantees of performance and are subject to certain risks, uncertainties and assumptions, including those described in this Quarterly Report on Form 10-Q. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, estimated, expected, projected, intended, committed or believed. The future results and shareholder values of the Company may differ materially from those expressed in these forward-looking statements. Many of the factors that will determine these results and values are beyond the

Table of Contents

Company s ability to control or predict. For those statements, the Company claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

The Securities and Exchange Commission (SEC) maintains a web site which contains reports, proxy statements, and other information pertaining to registrants that file electronically with the SEC, including the Company. The internet address is: www.sec.gov. In addition, our periodic and current reports are available free of charge on our website at www.cvcb.com as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. We believe that the Company s most critical accounting policies are those which the Company s financial condition depends upon, and which involve the most complex or subjective decisions or assessments.

There have been no material changes to the Company s critical accounting policies during 2010. Please refer to the Company s 2009 Annual Report to Shareholders on Form 10-K for a complete listing of critical accounting policies.

This discussion should be read in conjunction with our unaudited consolidated financial statements, including the notes thereto, appearing elsewhere in this report.

OVERVIEW

Second Quarter of 2010

In the second quarter of 2010, our consolidated net income was $504,000 compared to net income of $464,000 for the same period in 2009. Diluted EPS was $0.04 for the second quarter of June 30, 2010 compared to $0.04 for the same period in 2009. The increase in net income was primarily due to decreases in the provision for credit losses, offset by decreases in net interest income and non-interest income, and an increase in non-interest expenses. The provision for credit losses was $1,000,000 for the second quarter of 2010 compared to $2,500,000 for the second quarter of 2009, a decrease of $1,500,000. Net interest income decreased $818,000 or 9.4%. The yield on average total interest-earning assets decreased 80 basis points comparing the three month period ended June 30, 2010 to the same period in 2009 while interest rates on deposits decreased 45 basis points resulting in a 45 basis point decrease in net interest margin. Net interest margin was 5.06% for the three months ended June 30, 2010 compared to 5.51% for the same period in 2009. Non-interest income decreased $654,000 or 46.7% primarily due to an increase in other-than-temporary impairment charges of $700,000, and non-interest expense had a slight increase of $13,000 or 0.18% in the three months ended June 30, 2010 compared to 2009.

Annualized return on average equity for the second quarter of 2010 was 2.11% compared to 2.28% for the same period in 2009. Total average equity was $95,512,000 for the second quarter 2010 compared to $81,537,000 for the second quarter 2009. Equity increased primarily due to capital raised from the private sale of equity in the later part of 2009 to certain accredited investors who purchased preferred and common shares of the Company for a total of $8,000,000. Net income included in retained earnings and a decrease in other comprehensive loss also contributed to the growth in capital.

First Six Months of 2010

For the six months ended June 30, 2010, our consolidated net income was $1,796,000 compared to net income of $1,723,000 for the same period in 2009. Diluted EPS was $0.17 for the first six months of 2010 compared to $0.20 for the first six months of 2009. The increase in net income was primarily due to a decrease in the provision for loan losses offset by decreases in net interest income and non-interest income as well as an increase in non-interest expenses. During the six month period ended June 30, 2010 our net interest margin decreased 35 basis points to 5.02%. Net interest income decreased $1,317,000 or 7.6%. Non-interest income decreased $1,058,000 or 33.7.0%, provision for credit losses decreased $2,817,000 and non-interest expense increased $377,000 in the first six months of 2010 compared to 2009.

Annualized return on average equity for the six months ended June 30, 2010 was 3.80% compared to 4.21% for the same period in 2009. Annualized return on average assets for the six months ended June 30, 2010 was 0.48% compared to 0.46% for the same period in 2009. Total average equity was $94,422,000 for the six months ended June 30, 2010 compared to $81,819,000 for the same period in 2009. Equity increased primarily due to capital raised from the private sale of equity in the later part of 2009 to certain accredited investors who purchased preferred and common shares of the Company for a total of $8,000,000. Net income included in retained earnings and a decrease in other comprehensive loss also contributed to the growth in capital.

Table of Contents

Our average total assets decreased $3,900,000 or 0.52% in the first half of 2010 compared to the first half of 2009. Total average interest-earning assets decreased $5,582,000 or 0.83% comparing the first half of 2010 to the first half of 2009. Average total loans decreased $33,473,000 or 6.9% while average total investments increased $31,128,000 or 16.1% in the six month period ended June 30, 2010 compared to the same period in 2009. Average interest-bearing liabilities decreased only $8,679,000 or 1.7% over the same period.

Our net interest margin for the first six months ended June 30, 2010 was 5.02% compared to 5.37% for the same period in 2009. The margin decreased principally due to the decrease in yields on interest-earning assets outpacing the decrease in rates on interest-bearing liabilities. The effective yield on interest earning assets decreased 75 basis points to 5.72% for the six month period ended June 30, 2010 compared to 6.47% for the same period in 2009. For the six months ended June 30, 2010, the effective yield on investment securities including Federal funds sold and interest-earning deposits in other banks decreased 214 basis points and the effective yield on loans decreased 9 basis points. The cost of total interest-bearing liabilities decreased 53 basis points to 0.93% compared to 1.46% for the same period in 2009. The cost of total deposits, including noninterest bearing accounts decreased 40 basis points to 0.65% for the six months ended June 30, 2010 compared to 1.05% for the same period in 2009.

Net interest income for the first half of 2010 was $15,916,000 compared to $17,233,000 for the same period in 2009, a decrease of $1,317,000 or 7.6%. Net interest income decreased as a result of the decrease in net interest margin as discussed above and a decrease in earning assets. The Bank had non-accrual loans totaling $14,994,000 at June 30, 2010, compared to $18,959,000 at December 31, 2009 and $14,524,000 at June 30, 2009. The Company had other real estate owned at June 30, 2010 totaling $3,502,000, compared to $2,832,000 at December 31, 2009, and $2,550,000 at June 30, 2009.

We participated in the U. S. Treasury Capital Purchase Program (CPP) under the Emergency Economic Stabilization Act. In 2009, the Company issued preferred stock and warrants to issue common stock and received $7,000,000 in cash under this program. The Company agreed to restrict dividend payments on common stock to no more than historic levels while our preferred stock is owned by the U. S. Treasury.

Central Valley Community Bancorp (Company)

We are a central California-based bank holding company for a one-bank subsidiary, Central Valley Community Bank (Bank). We provide traditional commercial banking services to small and medium-sized businesses and individuals in the communities along the Highway 99 corridor in the Fresno, Madera, Merced, Sacramento, Stanislaus, and San Joaquin Counties of central California. Additionally, we have a private banking office in Sacramento County, and a loan production office in Modesto, California. As a bank holding company, the Company is subject to supervision, examination and regulation by the Federal Reserve Bank.

At June 30, 2010, we had total loans of $468,652,000, total assets of $755,989,000, total deposits of $631,309,000, and shareholders equity of $95,451,000.

Central Valley Community Bank (Bank)

The Bank commenced operations in January 1980 as a state-chartered bank. As a state-chartered bank, the Bank is subject to primary supervision, examination and regulation by the Department of Financial Institutions. The Bank s deposits are insured by the Federal Deposit Insurance Corporation (FDIC) up to the applicable limits thereof, and the Bank is subject to supervision, examination and regulations of the FDIC.

The Bank is participating in the FDIC Transaction Account Guarantee Program (TAG) under which all noninterest-bearing transaction accounts are fully guaranteed by the FDIC for the entire amount in the account. On June 28, 2010, the FDIC adopted a final rule extending TAG for six months to December 31, 2010 with the possibility of an additional extension not to exceed December 31, 2011 without further rulemaking. The recently enacted Dodd-Frank Wall Street Reform and Consumer Protection Act permanently raises the current standard maximum deposit insurance amount to $250,000 and extended unlimited FDIC deposit insurance to qualifying noninterest-bearing transaction accounts for two years beginning December 31, 2010.

Coverage under the TAGP is in addition to and separate from the coverage available under the FDIC s general deposit insurance rules. As a participant in TAG, the Bank is assessed an annual fee of 10 basis points for all deposit amounts exceeding the existing deposit insurance limit of $250,000.

The Bank operates 16 branches which serve the communities of Clovis, Fresno, Kerman, Lodi, Madera, Merced, Oakhurst, Prather, Sacramento, Stockton, and Tracy, California; and a loan production office which serves the Modesto, California community. Additionally the Bank operates Real Estate, Agribusiness and SBA departments that originate loans in California. According to the June 30, 2009 FDIC data, the Bank s branches in Fresno, Madera and San Joaquin Counties had a 3.50% combined deposit market share of all depositories including credit unions, thrifts, and savings banks.

Table of Contents

Key Factors in Evaluating Financial Condition and Operating Performance

As a publicly traded community bank holding company, we focus on several key factors including:

- Return to our stockholders;
- Return on average assets;
- Development of core earnings, including net interest income and non-interest income;
- Asset quality;
- Asset growth;
- Capital adequacy;
- Operating efficiency; and
- Liquidity

Return to Our Stockholders

Our return to our stockholders is measured in the form of return on average equity (ROE). Our annualized ROE was 3.80% for the six months ended June 30, 2010 compared to 3.10 % for the year ended December 31, 2009 and 4.21% for the six months ended June 30, 2009. Our net income for the six months ended June 30, 2010 increased $73,000 or 4.2% to $1,796,000 compared to $1,723,000 for the six months ended June 30, 2009. Net income increased due to decreases in the provision for credit losses offset by decreases in net interest income and non-interest income, and an increase in non-interest expenses. Net interest margin (NIM) decreased 35 basis points comparing the three month periods ended June 30, 2010 and 2009. Diluted EPS was $0.17 for the six months ended June 30, 2010 and $0.20 for the same period in 2009.

Return on Average Assets

Our return on average assets (ROA) is a measure we use to compare our performance with other banks and bank holding companies. Our annualized ROA for the six months ended June 30, 2010 was 0.48% compared to 0.34% for the year ended December 31, 2009 and 0.46% for the six months ended June 30, 2009. The increase in ROA compared to December 2009 is due to the increase in net income relative to total average assets. Average assets for the six months ended June 30, 2010 were $750,038,000 compared to $752,509,000 for the year ended December 31, 2009. ROA for our peer group was (0.20%) at March 31, 2010. Peer group from SNL Financial data includes certain bank holding companies in central California with assets from $300 million to $1 billion.

Development of Core Earnings

Over the past several years, we have focused on not only improving net income, but improving the consistency of our revenue streams in order to create more predictable future earnings and reduce the effect of changes in our operating environment on our net income. Specifically, we have focused on net interest income through a variety of processes, including increases in average interest earning assets as a result of loan generation and retention, and minimizing the effects of the recent interest rate decline on our net interest margin by focusing on core deposits and managing the cost of funds. The Company s net interest margin (fully tax equivalent basis) was 5.02% for the first half of June 30, 2010, compared to 5.37 % for the same period in 2009. The decrease in net interest margin is principally due to a decrease in the yield on earning assets which was greater than the decrease in our rates on interest-bearing liabilities. In comparing the two periods, the effective yield on total

earning assets decreased 75 basis points, while the cost of total interest bearing liabilities decreased 53 basis points and the cost of total deposits decreased 40 basis points. The Company s total cost of deposits for first half of June 30, 2010 was 0.65% compared to 1.05% for the same period in 2009. At June 30, 2010, 23.3% of the Company s average deposits were non-interest bearing compared to 23.0% for the Company s peer group as of March 31, 2010. Net interest income for the first half of 2010 was $15,916,000 compared to $17,233,000 for the same period in 2009.