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 September 30, 2013

or

¨ **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: 0-10140

CVB FINANCIAL CORP.

(Exact name of registrant as specified in its charter)

California	**95-3629339**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
701 North Haven Ave, Suite 350, Ontario, California	**91764**
(Address of Principal Executive Offices)	**(Zip Code)**

(909) 980-4030

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. 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 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, accelerated filer, non-accelerated filer or smaller reporting company. See definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨	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

Number of shares of common stock of the registrant: 105,239,634 outstanding as of October 31, 2013.

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PART I FINANCIAL INFORMATION (UNAUDITED)

GENERAL

Forward Looking Statements

Certain statements in this Report on Form 10-Q, including, but not limited to, statements under the heading Management Discussion and Analysis of Financial Condition and Results of Operations constitute forward-looking statements under the Private Securities Litigation Reform Act of 1995, including but not limited to, statements about anticipated future operating and financial performance, financial position and liquidity, business prospects, strategic alternatives, business strategies, regulatory policies, competitive outlook, capital and financing needs and availability, acquisition and divestiture opportunities, investment and expenditure plans, plans and objectives of management for future operations, management hiring and retention and other similar forecasts and statements of expectations of assumptions underlying any of the foregoing. Words such as will likely result , aims , anticipates , believes , could , estimates , expects , hopes , intends , may , plans , projects , seeks , should , will and variations of these expressions are intended to identify these forward looking statements, which involve risks and uncertainties. Our actual results may differ significantly from the results discussed in such forward-looking statements. Factors that might cause such a difference include, but are not limited to, local, regional, national and international economic conditions and events and the impact they may have on us and our customers; ability to attract and maintain deposits, borrowings and other sources of liquidity; supply of property inventory and renewed fluctuation or deterioration in values of real estate in California or other jurisdictions where we lend, whether involving residential or commercial property; a prolonged slowdown or decline in construction activity; changes in the financial performance and/or condition of our loan and deposit customers ; changes in the levels of performing and nonperforming assets and charge-offs; the cost or effect of acquisitions or divestitures we may make; the effect of changes in laws and regulations (including laws, regulations and judicial decisions concerning financial reform, taxes, bank or holding company capital levels, securities, employment, executive compensation, insurance, and information security) with which we and our subsidiaries must comply; changes in the applicability or costs of deposit insurance; changes in estimates of future reserve requirements and minimum capital requirements based upon the periodic review thereof under relevant legal, regulatory and accounting requirements; inflation, interest rate, securities market and monetary fluctuations; internal and external fraud and cyber-security threats, including theft or loss of Company or customer funds, loss of system functionality or access, or theft or loss of data; political instability; acts of war or terrorism, or natural disasters, such as earthquakes, or the effects of pandemic diseases; the timely development and acceptance of new banking products and services (including technology-based services and products) and the perceived overall value of these products and services by users; changes in consumer spending, borrowing and savings habits; the effects of technological changes, the expanding use of technology in banking (including the adoption of mobile banking applications) and product innovation; the ability to retain or increase market share, retain or grow customers and control expenses; changes in the risk or competitive environment among financial and bankentities, holding companies and other financial service providers; continued volatility in the credit and equity markets and its effects on the general economy or local business conditions; the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as by the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other national or international accounting standard setters; changes in our organization, management, compensation and benefit plans, and our ability to retain or expand our management team; the costs and effects of legal and regulatory changes or developments; the favorable or unfavorable resolution of legal proceedings or regulatory or other governmental inquiries, including, but not limited to, the current investigation by the Securities and Exchange Commission and the related class-action lawsuits filed against us; and the results of regulatory examinations or reviews or other government actions. The Company cautions that the foregoing factors are not exclusive. For additional information concerning these factors and other factors which may cause actual results to differ from the results discussed in our forward-looking statements, see the periodic filings the Company makes with the Securities and Exchange Commission, and, in particular, the information set forth in Item 1A herein and in Item 1A. Risk Factors contained in the Company s Annual Report on Form 10-K for the year ended December 31, 2012. The Company does not undertake, and specifically disclaims, any obligation to update any forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements except as required by law.

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ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CVB FINANCIAL CORP. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except share data)

(Unaudited)

	September 30, 2013	**December 31, 2012**
ASSETS		
Cash and due from banks	$ 127,728	$ 87,274
Interest-earning balances due from Federal Reserve	3,714	11,157
Total cash and cash equivalents	131,442	98,431
Interest-earning balances due from depository institutions	70,000	70,000
Investment securities available-for-sale, at fair value (with amortized cost of $2,609,959 at September 30, 2013, and $2,374,816 at December 31, 2012)	2,617,307	2,449,387
Investment securities held-to-maturity	1,850	2,050
Investment in stock of Federal Home Loan Bank (FHLB)	39,420	56,651
Loans and lease finance receivables, excluding covered loans	3,281,352	3,252,313
Allowance for loan losses	(80,713)	(92,441)
Net loans and lease finance receivables	3,200,639	3,159,872
Covered loans and lease finance receivables, net	163,334	195,215
Premises and equipment, net	33,604	35,080
Bank owned life insurance	122,538	119,744
Accrued interest receivable	21,860	22,355
Intangibles	2,386	3,389
Goodwill	55,097	55,097
FDIC loss sharing asset	7,034	18,489
Non-covered other real estate owned	6,524	14,832
Covered other real estate owned	906	1,067
Income tax assets, net	59,226	16,978
Other assets	24,116	44,727
TOTAL ASSETS	$ 6,557,283	$ 6,363,364
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities:		
Deposits:		
Noninterest-bearing	$ 2,538,461	$ 2,420,993

Interest-bearing	2,357,025	2,352,994
Total deposits	4,895,486	4,773,987
Customer repurchase agreements	565,883	473,244
FHLB advances	199,138	198,934
Other borrowings	42,482	26,000
Accrued interest payable	1,106	1,493
Deferred compensation	9,316	8,781
Junior subordinated debentures	25,774	67,012
Other liabilities	49,876	50,943
TOTAL LIABILITIES	5,789,061	5,600,394
COMMITMENTS AND CONTINGENCIES		
Stockholders Equity:		
Common stock, authorized, 225,000,000 shares without par; issued and outstanding 105,209,875 at September 30, 2013, and 104,889,586 at December 31, 2012.	488,555	484,709
Retained earnings	275,405	235,010
Accumulated other comprehensive income, net of tax	4,262	43,251
Total stockholders equity	768,222	762,970
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 6,557,283	$ 6,363,364

See accompanying notes to the condensed consolidated financial statements.

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CVB FINANCIAL CORP. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS AND COMPREHENSIVE INCOME

(Dollars in thousands, except per share amounts)

(Unaudited)

	For the Three Months Ended September 30, 2013	For the Three Months Ended September 30, 2012	For the Nine Months Ended September 30, 2013	For the Nine Months Ended September 30, 2012
Interest income:				
Loans and leases, including fees	$ 41,706	$ 45,559	$ 124,879	$ 139,289
Accretion on acquired loans	2,947	7,045	10,796	19,258
Loans, including fees	44,653	52,604	135,675	158,547
Investment securities:				
Taxable	7,102	7,246	19,280	25,202
Tax-advantaged	5,517	5,640	16,569	17,221
Total investment income	12,619	12,886	35,849	42,423
Dividends from FHLB stock	622	79	1,432	263
Federal funds sold	58	158	158	539
Interest-earning deposits with other institutions	122	118	366	317
Total interest income	58,074	65,845	173,480	202,089
Interest expense:				
Deposits	1,228	1,398	3,627	4,605
Borrowings	2,768	4,086	8,184	13,933
Junior subordinated debentures	105	617	512	2,245
Total interest expense	4,101	6,101	12,323	20,783
Net interest income before provision for loan losses	53,973	59,744	161,157	181,306
Provision for loan losses	(3,750)		(9,950)	
Net interest income after provision for loan losses	57,723	59,744	171,107	181,306
Noninterest income:				
Service charges on deposit accounts	4,011	4,040	11,982	12,232
Trust and investment services	2,021	2,037	6,098	6,264
Bankcard services	920	962	2,697	2,888
BOLI income	497	781	1,867	2,271
Gain on sale of investment securities, net			2,094	
Decrease in FDIC loss sharing asset, net	(3,248)	(7,059)	(10,715)	(19,339)
Gain on OREO, net	(3)	524	3,129	1,458

Other	759	1,341	2,245	4,400
Total noninterest income	4,957	2,626	19,397	10,174
Noninterest expense:				
Salaries and employee benefits	18,389	17,489	52,777	50,856
Occupancy and equipment	3,641	4,010	10,888	11,582
Professional services	1,316	1,570	4,299	5,666
Software licenses and maintenance	1,077	1,062	3,392	2,960
Promotion	1,105	1,176	3,503	3,741
Provision for unfunded commitments	500		500	
Amortization of intangibles	127	449	1,002	1,717
Debt termination expense		20,379		20,379
OREO expense	21	405	384	1,458
Insurance reimbursements	(4,139)	(48)	(4,139)	(451)
Other	3,677	3,528	12,154	11,273
Total noninterest expense	25,714	50,020	84,760	109,181
Earnings before income taxes	36,966	12,350	105,744	82,299
Income taxes	12,727	3,093	35,424	27,155
Net earnings	$ 24,239	$ 9,257	$ 70,320	$ 55,144
Other comprehensive income/(loss):				
Unrealized gain/(loss) on investment securities arising during the period	$ 421	$ 8,417	$ (65,129)	$ 12,064
Less: Reclassification adjustment for net gain on investment securities included in net income			(2,094)	
Other comprehensive income (loss), before tax	421	8,417	(67,223)	12,064
Income tax (expense) benefit related to items of other comprehensive income (loss)	(176)	(3,536)	28,234	(5,068)
Other comprehensive income (loss), net of tax	245	4,881	(38,989)	6,996
Comprehensive income	$ 24,484	$ 14,138	$ 31,331	$ 62,140
Basic earnings per common share	$ 0.23	$ 0.09	$ 0.67	$ 0.53
Diluted earnings per common share	$ 0.23	$ 0.09	$ 0.67	$ 0.53
Cash dividends declared per common share	$ 0.10	$ 0.085	$ 0.285	$ 0.255

See accompanying notes to the condensed consolidated financial statements.

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CVB FINANCIAL CORP. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

Nine Months Ended September 30, 2013 and 2012

(Dollars and shares in thousands)

(Unaudited)

	Common Shares Outstanding	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Total
Balance January 1, 2012	104,482	$ 479,973	$ 193,372	$ 41,469	$ 714,814
Exercise of stock options	331	2,412			2,412
Tax benefit from exercise of stock options		179			179
Shares issued pursuant to stock-based compensation plan		1,387			1,387
Cash dividends declared Common ($0.255 per share)			(26,725)		(26,725)
Net earnings			55,144		55,144
Other comprehensive income				6,996	6,996
Balance September 30, 2012	104,813	$ 483,951	$ 221,791	$ 48,465	$ 754,207
Balance January 1, 2013	104,890	$ 484,709	$ 235,010	$ 43,251	$ 762,970
Repurchase of common stock	(36)	(459)			(459)
Exercise of stock options	259	2,651			2,651
Tax benefit from exercise of stock options		215			215
Shares issued pursuant to stock-based compensation plan	97	1,439			1,439
Cash dividends declared Common ($0.285 per share)			(29,925)		(29,925)
Net earnings			70,320		70,320
Other comprehensive income				(38,989)	(38,989)
Balance September 30, 2013	105,210	$ 488,555	$ 275,405	$ 4,262	$ 768,222

See accompanying notes to the condensed consolidated financial statements.

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CVB FINANCIAL CORP. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

(Unaudited)

	For the Nine Months Ended September 30, 2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Interest and dividends received	$ 181,608	$ 200,601
Service charges and other fees received	23,103	28,144
Interest paid	(12,506)	(22,531)
Net cash paid to vendors and employees	(69,441)	(105,347)
Income taxes paid	(50,200)	(3,455)
Proceeds from FDIC loss share agreement	239	17,842
Net cash provided by operating activities	72,803	115,254
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from redemption of FHLB stock	17,231	10,261
Proceeds from sale of investment securities	99,155	
Proceeds from repayment of investment securities	344,660	401,229
Proceeds from maturity of investment securities	62,175	74,287
Purchases of investment securities	(759,609)	(567,391)
Net decrease in loan and lease finance receivables	13,375	61,475
Proceeds from sales of premises and equipment	9	26
Purchase of premises and equipment	(2,080)	(3,382)
Proceeds from sales of other real estate owned	12,922	17,274
Net cash used in investing activities	(212,162)	(6,221)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in transaction deposits	147,349	275,109
Net decrease in time deposits	(25,850)	(98,541)
Repayment of FHLB advances		(250,000)
Repayment of junior subordinated debentures	(41,238)	(48,043)
Net increase in other borrowings	16,482	
Net increase/(decrease) in customer repurchase agreements	92,639	(60,582)
Cash dividends on common stock	(19,419)	(26,725)
Repurchase of common stock	(459)	
Proceeds from exercise of stock options	2,651	2,412
Tax benefit related to exercise of stock options	215	179
Net cash provided by/(used in) financing activities	172,370	(206,191)

NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	33,011	(97,158)
CASH AND CASH EQUIVALENTS, beginning of period	98,431	345,343
CASH AND CASH EQUIVALENTS, end of period	$ 131,442	$ 248,185

See accompanying notes to the condensed consolidated financial statements.

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CVB FINANCIAL CORP. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)

(Dollars in thousands)

(Unaudited)

	For the Nine Months Ended September 30, 2013	2012
RECONCILIATION OF NET EARNINGS TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Net earnings	$ 70,320	$ 55,144
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Gain on sale of investment securities	(2,094)	
Loss/(gain) on sale of premises and equipment, net	2	(1)
Gain on sale of other real estate owned	(3,048)	(1,341)
Amortization of capitalized prepayment penalty on borrowings	204	204
Increase in bank owned life insurance	(1,805)	(2,252)
Net amortization of premiums and discounts on investment securities	20,770	17,578
Accretion of SJB discount	(10,796)	(19,258)
Provision for loan losses	(9,950)	
Provision for unfunded commitments	500	
Valuation adjustment on other real estate owned	87	490
Change in FDIC loss share asset	10,715	19,339
Proceeds from FDIC loss share agreement	239	17,842
Stock-based compensation	1,439	1,387
Depreciation and amortization, net	2,029	5,776
Change in accrued interest receivable	495	627
Change in accrued interest payable	(387)	(1,952)
Change in other assets and liabilities	(5,917)	21,671
Total adjustments	2,483	60,110
Net cash provided by operating activities	$ 72,803	$ 115,254
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING ACTIVITIES		
Transfer of loans to other real estate owned	$ 1,492	$ 4,582

See accompanying notes to the condensed consolidated financial statements.

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CVB FINANCIAL CORP. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

For the Three and Nine Months Ended September 30, 2013, and 2012

(Unaudited)

1. BUSINESS

The condensed consolidated financial statements include the accounts of CVB Financial Corp. and its wholly owned subsidiaries (the Company) Citizens Business Bank (the Bank) after elimination of all intercompany transactions and balances. The Company also has three inactive subsidiaries; CVB Ventures, Inc.; Chino Valley Bancorp; and ONB Bancorp. The Company is also the common stockholder of CVB Statutory Trust III. CVB Statutory Trust III was created in January 2006 to issue trust preferred securities in order to raise capital for the Company. In accordance with ASC 810 Consolidation (previously Financial Accounting Standards Board (FASB) Interpretation No. 46R Consolidation of Variable Interest Entities), this trust does not meet the criteria for consolidation.

The Company s primary operations are related to traditional banking activities, including the acceptance of deposits and the lending and investing of money through the operations of the Bank. The Bank also provides automobile and equipment leasing to customers through its Citizens Financial Services Group and trust and investment-related services to customers through its CitizensTrust Division. The Bank s customers consist primarily of small to mid-sized businesses and individuals located in San Bernardino County, Riverside County, Los Angeles County, Orange County, San Diego County, Madera County, Fresno County, Tulare County, Kern County and San Joaquin County, California. The Bank operates 39 Business Financial Centers, six Commercial Banking Centers, and three trust office locations, with its headquarters located in the city of Ontario, California.

2. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements and notes thereto have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (SEC) for Form 10-Q and conform to practices within the banking industry and include all of the information and disclosures required by accounting principles generally accepted in the United States of America (GAAP) for interim financial reporting. The results of operations for the three and nine months ended September 30, 2013 are not necessarily indicative of the results for the full year. These unaudited financial statements should be read in conjunction with the financial statements, accounting policies and financial notes thereto included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2012, filed with the Securities and Exchange Commission. In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments), which are necessary for a fair presentation of financial results for the interim periods presented. A summary of the significant accounting policies consistently applied in the preparation of the accompanying unaudited condensed consolidated financial statements follows.

Reclassification Certain amounts in the prior periods financial statements and related footnote disclosures have been reclassified to conform to the current presentation with no impact on previously reported net income or stockholders equity.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Investment Securities The Company classifies as held-to-maturity those debt securities that the Company has the positive intent and ability to hold to maturity. Securities classified as trading are those securities that are bought and held principally for the purpose of selling them in the near term. All other debt and equity securities are classified as available-for-sale. Securities held-to-maturity are accounted for at cost and adjusted for amortization of premiums and accretion of discounts. Trading securities are accounted for at fair value with the unrealized gains and losses being included in current earnings. Available-for-sale securities are accounted for at fair value, with the net unrealized gains and losses, net of income tax effects, presented as a separate component of stockholders equity. Realized gains and losses on sales of securities are recognized in earnings at the time of sale and are determined on a specific-identification basis. Purchase premiums and discounts are recognized in interest income using the effective-yield method over the expected terms of the securities. For mortgage-backed securities (MBS), the amortization or accretion is based on the estimated average lives of the securities. The lives of these securities can fluctuate based on the amount of prepayments received on the underlying collateral of the securities. The Company s investment in the Federal Home Loan Bank of San Francisco (FHLB) stock is carried at cost.

At each reporting date, securities are assessed to determine whether there is an other-than-temporary impairment (OTTI). Other-than-temporary impairment on investment securities is recognized in earnings when there are credit losses on a debt security for which management does not intend to sell and for which it is more-likely-than-not that the Company will not have to sell prior to recovery of the noncredit impairment. In those situations, the portion of the total impairment that is attributable to the credit loss would be recognized in earnings, and the remaining difference between the debt security s amortized cost and its fair value would be included in other comprehensive income.

Loans and Lease Finance Receivables Non-covered loans and lease finance receivables that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, less deferred net loan origination fees. In the ordinary course of business, the Company enters into commitments to extend credit to its customers. To the extent that such commitments are unfunded, the related unfunded amounts are not reflected in the accompanying unaudited condensed consolidated financial statements.

Interest on non-covered loans and lease finance receivables is credited to income based on the principal amounts of such loans or receivables outstanding. Non-covered loans are considered delinquent when principal or interest payments are past due 30 days or more and generally remain on accrual status between 30 and 89 days past due. Interest income is not recognized on non-covered loans and lease finance receivables when collection of interest is deemed by management to be doubtful. Non-covered loans on which the accrual of interest has been discontinued are designated as nonaccrual loans. In general, the accrual of interest on non-covered loans is discontinued when the loan becomes 90 days past due, or when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Factors considered in determining that the full collection of principal and interest is no longer probable include cash flow and liquidity of the borrower or property, the financial position of the guarantors and their willingness to support the loan as well as other factors, and this determination involves significant judgment. When an asset is placed on nonaccrual status, previously accrued but unpaid interest is reversed against income. Subsequent collections of cash are applied as reductions to the principal balance unless the loan is returned to accrual status. Interest is not recognized using a cash-basis method. Nonaccrual loans may be restored to accrual status when principal and interest become current and when the borrower is able to demonstrate payment performance for a sustained period, typically for six months. A nonaccrual loan may return to accrual status sooner based on other significant events or mitigating circumstances. This policy is consistently applied to all classes of non-covered financing receivables.

The Company receives collateral to support loans, lease finance receivables, and commitments to extend credit for which collateral is deemed necessary. The most significant categories of collateral are real estate, principally commercial and industrial income-producing properties, real estate mortgages, and assets utilized in dairy, livestock and agribusiness, and various personal property assets utilized in commercial and industrial business governed by the Uniform Commercial Code.

Nonrefundable fees and direct costs associated with the origination or purchase of non-covered loans are deferred and netted against outstanding loan balances. The deferred net loan fees and costs are recognized in interest income over the loan term using the effective-yield method.

Troubled Debt Restructurings Loans are reported as a Troubled Debt Restructuring (TDR) if the Company, for economic or legal reasons related to the debtor s financial difficulties, grants a concession to the debtor that it would not otherwise consider. Types of modifications that may be considered concessions, which in turn result in a TDR include, but are not limited to, (i) a reduction of the stated interest rate for the remaining original life of the debt, (ii) an extension of the maturity date or dates at a stated interest rate lower than the current market rate for new debt with similar risk, (iii) a reduction of the face amount or maturity amount of the debt as stated in the instrument or other agreement, or (iv) a reduction of interest. In addition, the Company may provide a concession to the debtor where the debtor offers collateral and the value of such collateral is significant in proportion to the nature of the concession requested, and it substantially reduces the Company s risk of loss. In such cases, these modifications may not be considered a TDR as, in substance, no concession was made as a result of the significant additional collateral obtained.

When determining whether or not a loan modification is a TDR under ASC 310-40, the Company evaluates loan modification requests from borrowers experiencing financial difficulties on a case-by-case basis. Any such modifications granted are unique to the borrower s circumstances. Because of the Company s focus on the commercial lending sector, each business customer has unique attributes, which in turn means that modifications of loans to those customers are not easily categorized by type, key features, or other terms, but are evaluated individually based on all relevant facts and circumstances pertaining to the modification request and the borrower s/guarantor s financial condition at the time of the request. The evaluation of whether or not a borrower is experiencing financial difficulties will include, among other relevant factors considered by the Company, a review of (i) whether the borrower is in default on any of its debt, (ii) whether the borrower is experiencing payment delinquency, (iii) whether the global cash flows of the borrower and the owner guarantor(s) of the borrower have diminished below what is necessary to service existing debt obligations, (iv) whether the borrowers forecasted cash flows will be insufficient to service the debt in future periods or in accordance with the contractual terms of the existing agreement with the Company (or agreements with other lenders) through maturity, (v) whether the borrower is unable to refinance the subject debt from other financing sources with similar terms, and (vi) whether the borrower is in jeopardy as a going-concern and/or considering bankruptcy. In any case, the debtor is presumed to be experiencing financial difficulties if the Company determines it is probable the debtor will default on the original loan if the modification is not granted.

The types of loans subject to modification vary greatly, but during the subject period are concentrated in commercial and industrial loans, dairy and agricultural loans, and term loans to commercial real estate investors. Some examples of key features include payment deferrals and delays, interest rate reductions, and extensions or renewals where the contract rate may or may not be below the market rate of interest for debt with similar characteristics as those of the modified debt. The typical length of the modified terms ranges from three (3) to twelve (12) months but may in some cases apply for the remaining term of the loan; however, all actual modified terms will depend on the facts, circumstances and attributes of the specific borrower requesting a modification. In general, after a careful evaluation of all relevant facts and circumstances taken together, including the nature of any concession, certain modification requests will result in troubled debt restructurings while certain other modifications will not, pursuant to the criteria and judgments as discussed throughout this report. In certain cases, modification requests for delays or deferrals of principal were evaluated and determined to be exempt from TDR reporting because they constituted insignificant delays under ASC 310-40-15.

In situations where the Company has determined that the borrower is experiencing financial difficulties and is evaluating whether a concession is *insignificant,* and therefore does not result in a troubled debt restructuring, such analysis is based on an evaluation of both the *amount* and the *timing* of the restructured payments, including the following factors:

1. Whether the amount of the restructured payments subject to delay is insignificant relative to the unpaid principal balance or collateral value of the debt and will result in an insignificant shortfall in the contractual amount due; and

2. The delay is insignificant relative to any of the following:

   The frequency of payments due;

   The debt s original contractual maturity; or

   The debt s original expected duration.

Most modified loans *not* classified and accounted for as troubled debt restructurings were performing and paying as agreed under their original terms in the six-month period immediately preceding a request for modification. Subsequently, these modified loans have continued to perform under the modified terms and deferrals that amounted to insignificant delays, which in turn is supported by the facts and circumstances of each individual customer and loan as described above. Payment performance continues to be monitored once modifications are made. The Company s favorable experience regarding re-defaults under modified terms, or upon return of the loan to its original terms, indicates that such relief may improve ultimate collection and reduces the Company s risk of loss.

A loan is generally considered impaired, when based on current events and information, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. A loan, including a restructured loan, for which there is an insignificant delay relative to the frequency of payments due, and/or the original contractual maturity, is not considered an impaired loan. Generally, impaired loans include loans on nonaccrual status and TDRs.

The Company s policy is to record a specific valuation allowance, which is included in the allowance for loan losses, or to charge off that portion of an impaired loan that represents the impairment or shortfall amount as determined utilizing one of the three methods described in ASC 310-10-35-22. Impairment on non-collateral dependent restructured loans is measured by comparing the present value of expected future cash flows on the restructured loans discounted at the interest rate of the original loan agreement to the loan s carrying value. The impairment amount, if any, is generally charged off and recorded against the allowance for loan losses at the time impairment is measurable and a probable loss is determined. As a result, most of the TDRs have no specific allowance allocated because, consistent with the Company s stated practice, any impairment is typically charged off in the period in which it is identified. Impairment on collateral dependent restructured loans is measured by determining the amount by which the impaired loan exceeds the fair value of the collateral less estimated selling costs. The fair value is generally determined by one or more appraisals of the collateral, performed by a Company approved third-party independent appraiser. The majority of impaired loans that are collateral dependent are charged off down to their estimated fair value of the collateral (less selling costs) at each reporting date based on current appraised value.

Appraisals of the collateral for impaired collateral dependent loans are typically ordered at the time the loan is identified as showing signs of inherent weakness. These appraisals are normally updated at least annually, or more frequently, if there are concerns or indications that the value of the collateral may have changed significantly since the previous appraisal. On an exception basis, a specific valuation allowance is recorded on collateral dependent impaired loans when a current appraisal is not yet available, a recent appraisal is still under review or on single-family mortgage loans if the loans are currently under review for a loan modification. Such valuation allowances are generally based on previous appraisals adjusted for current market conditions, based on preliminary appraisal values that are still being reviewed or for single-family loans under review for modification on an appraisal or indications of comparable home sales from external sources.

Charge-offs of unsecured consumer loans are recorded when the loan reaches 120 days past due or sooner as circumstances indicate. Except for the charge-offs of unsecured consumer loans, the charge-off policy is generally applied consistently across all portfolio segments.

The Company measures impairment based on the present value of expected future cash flows discounted at the loan s effective interest rate, except that as a practical expedient, the Company may measure impairment based on a loan s observable market price, or the fair value of the collateral if the loan is a collateral-dependent loan. Impaired single-family mortgage loans that have been modified in accordance with the various government modification programs are also measured based on the present value of the expected cash flows discounted at the loan s pre-modification interest rate. The Company recognizes the change in present value attributable to the passage of time as interest income on such performing single-family mortgage loans and the amount of interest income recognized to date has been insignificant.

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Covered Loans We refer to covered loans as those loans that we acquired in the San Joaquin Bank (SJB) acquisition for which we will be reimbursed for a substantial portion of any future losses under the terms of the Federal Deposit Insurance Corporation (FDIC) loss sharing agreement. We account for loans under ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality* (acquired impaired loan accounting) when (i) we acquire loans deemed to be impaired when there is evidence of credit deterioration since their origination and it is probable at the date of acquisition that we would be unable to collect all contractually required payments and (ii) as a general policy election for non-impaired loans that we acquire in a distressed bank acquisition. Acquired impaired loans are accounted for individually or in pools of loans based on common risk characteristics. The excess of the loan s or pool s scheduled contractual principal and interest payments over all cash flows expected at acquisition is the nonaccretable difference. The remaining amount, representing the excess of the loan s cash flows expected to be collected over the fair value is the accretable yield (accreted into interest income over the remaining life of the loan or pool).

Provision and Allowance for Loan Losses The allowance for loan losses is management s estimate of probable losses inherent in the loan and lease receivables portfolio. The allowance is increased by the provision for losses and decreased by charge-offs when management believes the uncollectability of a loan is confirmed. Subsequent recoveries, if any, are credited to the allowance. The determination of the balance in the allowance for loan losses is based on an analysis of the loan and lease finance receivables portfolio using a systematic methodology and reflects an amount that, in management s judgment, is appropriate to provide for probable loan losses inherent in the portfolio, after giving consideration to the character of the loan portfolio, current economic conditions, past loan loss experience, and such other factors that would deserve current recognition in estimating inherent loan losses.

There are different qualitative risks for the loans in each portfolio segment. The construction and real estate segments predominant risk characteristic is the collateral and the geographic location of the property collateralizing the loan as well as the operating cash flow for commercial real estate properties. The commercial and industrial segment s predominant risk characteristics are the cash flows of the businesses we lend to, the global cash flows and liquidity of the guarantors of such losses, as well as economic and market conditions. The dairy & livestock segment s predominant risk characteristics are milk and beef prices in the market as well as the cost of feed and cattle. The municipal lease segment s predominant risk characteristics are the municipality s general financial condition and tax revenues or if applicable the specific project related financial condition. The consumer, auto and other segment s predominant risk characteristics are employment and income levels as they relate to consumers and cash flows of the businesses as they relate to equipment and vehicle leases to businesses. The Agribusiness segment s predominant risk characteristics are the supply and demand conditions of the product, production seasonality, the scale of operations and ability to control costs, the availability and cost of water, and operator experience.

The Company s methodology is consistently applied across all portfolio segments taking into account the applicable historical loss rates and the qualitative factors applicable to each pool of loans. A key factor in the Company s methodology is the loan risk rating (Pass, Special Mention, Substandard, Doubtful and Loss). Loan risk ratings are updated as facts related to the loan or borrower become available. In addition, all term loans in excess of $1.0 million are subject to an annual internal credit review process where all factors underlying the loan, borrower and guarantors are subject to review which may result in changes to the loan s risk rating. Periodically, we assess various attributes utilized in adjusting our historical loss factors to reflect our view of current economic conditions. The estimate is reviewed quarterly by the Board of Directors and management and periodically by various regulatory agencies and, as adjustments become necessary, they are reported in earnings in the periods in which they become known.

A provision for loan losses on the covered portfolio will be recorded if there is deterioration in the expected cash flows on covered loans as a result of deteriorated credit quality, compared to those previously estimated without regard to the reimbursement from the FDIC under the FDIC loss sharing agreement. The portion of the loss on covered loans reimbursable from the FDIC is recorded in noninterest income as an increase in the FDIC loss sharing asset. Decreases in expected cash flows on the acquired impaired loans as of the measurement date compared to previously estimated are recognized by recording a provision for loan losses on acquired impaired loans. Loans accounted for as part of a pool are measured based on the expected cash flows of the entire pool.

FDIC Loss Sharing Asset On October 16, 2009, the Bank acquired substantially all of the assets and assumed substantially all of the liabilities of SJB from the FDIC in an FDIC-assisted transaction. The Bank entered into a loss sharing agreement with the FDIC, whereby the FDIC will cover a substantial portion of any future losses on certain acquired assets. The acquired assets subject to the loss sharing agreement are referred to collectively as covered assets. Under the terms of such loss sharing agreement, the FDIC will absorb 80% of losses and share in 80% of loss recoveries up to $144.0 million with respect to covered assets, after a first loss amount of $26.7 million. The FDIC will reimburse the Bank for 95% of losses and share in 95% of loss recoveries in excess of $144.0 million with respect to covered assets. The loss sharing agreement is in effect for 5 years for commercial loans and 10 years for single-family residential loans from the October 16, 2009 acquisition date and the loss recovery provisions are in effect for 8 and 10 years, respectively, for commercial and single-family residential loans from the acquisition date.

The FDIC loss sharing asset was initially recorded at fair value which represents the present value of the estimated cash payments from the FDIC for future losses on covered loans. The ultimate collectability of this asset is dependent upon the performance of the underlying covered loans, the passage of time and claims paid by the FDIC. The loss estimates used in calculating the FDIC loss sharing asset are determined on the same basis as the loss estimates on the related covered loans and is the present value of the cash flows the Company expects to collect from the FDIC under the loss sharing agreement. The difference between the present value and the undiscounted cash flow the Company expects to collect from the FDIC is accreted (or amortized) into noninterest income over the life of the FDIC indemnification asset. The FDIC indemnification asset is adjusted for any changes in expected cash flows based on covered loan performance. Any increases in the cash flows of covered loans over those expected will reduce the FDIC indemnification asset and any decreases in the cash flows of covered loans over those expected will increase the FDIC indemnification asset, with the remaining balance amortized on the same basis as the discount, not to exceed its remaining contract life. These increases and decreases to the FDIC indemnification asset are recorded as adjustments to noninterest income.

Goodwill and Intangible Assets Goodwill resulting from business combinations prior to January 1, 2009, represents the excess of the purchase price over the fair value of the net assets of the businesses acquired. Goodwill resulting from business combinations after January 1, 2009, is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interest in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but tested for impairment at least annually, or more frequently if events and circumstances exists that indicate that a goodwill impairment test should be performed.

Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Goodwill is the only intangible asset with an indefinite life on our balance sheet. Based on the Company s annual impairment test, there was zero recorded impairment as of September 30, 2013.

Other intangible assets consist of core deposit intangible assets arising from business combinations and are amortized using an accelerated method over their estimated useful lives.

At September 30, 2013, goodwill was $55.1 million. As of September 30, 2013, intangible assets that continue to be subject to amortization include core deposit premiums of $2.4 million (net of $29.6 million of accumulated amortization). Amortization expense for such intangible assets was $127,000, and $1.0 million for the three and nine months ended September 30, 2013. Estimated amortization expense for the remainder of 2013 is expected to be $124,000. Estimated amortization expense for the succeeding years is $475,000 for 2014, $437,000 for 2015, $395,000 for 2016, $366,000 for 2017, and $589,000 for the period from 2018 to 2019. The weighted average remaining life of intangible assets is approximately 2.0 years.

Fair Value of Financial Instruments We use fair value measurements to record fair value adjustments to certain financial instruments and to determine fair value disclosures. Investment securities available-for-sale and interest-rate swaps are financial instruments recorded at fair value on a recurring basis. Additionally, from time to time, we may be required to record at fair value other financial assets on a non-recurring basis, such as impaired loans and other real estate owned (OREO). These nonrecurring fair value adjustments typically involve application of lower-of-cost-or-market accounting or write-downs of individual assets. Further, we include in Note 8 of the unaudited condensed consolidated financial statements information about the extent to which fair value is used to measure assets and liabilities, the valuation methodologies used and its impact to earnings. Additionally, for financial instruments not recorded at fair value we disclose the estimate of their fair value.

Earnings per Common Share The Company calculates earnings per common share (EPS) using the two-class method. The two-class method requires the Company to present EPS as if all of the earnings for the period are distributed to common shareholders and any participating securities. All outstanding unvested share-based payment awards that contain rights to non-forfeitable dividends are considered participating securities. The Company grants restricted shares under the 2008 Equity Incentive Plan that qualify as participating securities. Restricted shares issued under this plan are entitled to dividends at the same rate as common stock. A reconciliation of the numerator and the denominator used in the computation of basic and diluted earnings per common share is included in Note 7 of these unaudited condensed consolidated financial statements.

Stock-Based Compensation Consistent with the provisions of ASC 718, Stock Compensation , we recognize expense for the grant date fair value of stock options and restricted shares issued to employees, officers and non-employee directors over the their requisite service periods (generally the vesting period). The service periods may be subject to performance conditions.

At September 30, 2013, the Company had three stock-based employee compensation plans. The Company accounts for stock compensation using the modified prospective method. Under this method, awards that are granted, modified, or settled after December 31, 2005, are measured at fair value as of the grant date with compensation costs recognized over the vesting period on a straight-lined basis. Also under this method, unvested stock awards as of January 1, 2006 are recognized over the remaining service period with no change in historical reported earnings.

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The fair value of each stock option grant is estimated as of the grant date using the Black-Scholes option-pricing model. Management assumptions used at the time of grant impact the fair value of the option calculated under the Black-Scholes option-pricing model, and ultimately, the expense that will be recognized over the life of the option.

The grant date fair value of restricted stock awards is measured at the fair value of the Company s common stock as if the restricted share was vested and issued on the date of grant.

Additional information is included in Note 19, Stock Option Plan and Restricted Stock Awards , of the Company s Annual Report on Form 10-K.

Derivative Financial Instruments All derivative instruments, including certain derivative instruments embedded in other contracts, are recognized on the consolidated balance sheets at fair value. For derivatives designated as fair value hedges, changes in the fair value of the derivative and the hedged item related to the hedged risk are recognized in earnings. Changes in fair value of derivatives designated and accounted for as cash flow hedges, to the extent they are effective as hedges, are recorded in Other Comprehensive Income, net of deferred taxes, and are subsequently reclassified to earnings when the hedged transaction affects earnings. Any hedge ineffectiveness would be recognized in the income statement line item pertaining to the hedged item.

Use of Estimates in the Preparation of Financial Statements The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent 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. A material estimate that is particularly susceptible to significant change in the near term relates to the determination of the allowance for loan losses. Other significant estimates which may be subject to change include fair value determinations and disclosures, impairment of investments, goodwill, loans, determining the amount and realization of the FDIC loss sharing asset, and valuation of deferred tax assets, other intangibles and OREO.

Other Contingencies In the ordinary course of business, the Company becomes involved in litigation. Based upon the Company s internal records and discussions with legal counsel, the Company records reserves as appropriate, for estimates of the probable outcome of all cases brought against the Company. Except as discussed in Part II Other Information, Item 1. Legal Proceedings, at September 30, 2013, the Company does not have any litigation reserves, and is not aware of any material pending legal action or complaints asserted against the Company.

Recent Accounting Pronouncements In July 2013, the FASB issued Accounting Standards Update (ASU) No. 2013-11, Income Taxes (Topic 740) *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists* . This ASU requires an entity to present an unrecognized tax benefit as a reduction of a deferred tax asset for a net operating loss carryforward, or similar tax loss or tax credit carryforward, rather than a liability when (1) the uncertain tax position would reduce the net operating loss or other carryforward under the tax law of the applicable jurisdiction and (2) the entity intends to use the deferred tax asset for that purpose. The ASU does not require new recurring disclosures. ASU No. 2013-11 is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2013. The adoption of this new guidance is not expected to have a material impact on the Company s consolidated financial statements.

4. FEDERALLY ASSISTED ACQUISITION OF SAN JOAQUIN BANK

On October 16, 2009, the Bank acquired SJB and entered into a loss sharing agreement with the FDIC that is more fully discussed in the Significant Accounting Policies (Note 3) included herein.

At September 30, 2013, the remaining discount associated with the SJB loans approximated $14.5 million. Based on the Company s regular forecast of expected cash flows from these loans, approximately $9.0 million of the related discount is expected to accrete into interest income over the remaining average lives of the respective pools and individual loans, which approximates 4.4 years and 1.0 year, respectively. Due to the decrease in estimated losses to be incurred in the remaining portfolio, the expected reimbursement from the FDIC under the loss sharing agreement decreased. The FDIC loss sharing asset of $7.0 million at September 30, 2013 will continue to be reduced by reimbursements of loss claims submitted to the FDIC with the remaining balance amortized on the same basis as the discount on the related loans, not to exceed its remaining contract life of approximately 1.0 year.

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5. INVESTMENT SECURITIES

The amortized cost and estimated fair value of investment securities are summarized below. The majority of securities held are publicly traded, and the estimated fair values were obtained from an independent pricing service based upon market quotes.

	September 30, 2013				
	Amortized Cost	Gross Unrealized Holding Gain	Gross Unrealized Holding Loss	Fair Value	Total Percent
	(Dollars in thousands)				
Investment securities available-for-sale:					
Government agency	$ 353,580	$ 36	$ (20,603)	$ 333,013	12.72%
Residential mortgage-backed securities	1,286,448	19,249	(16,073)	1,289,624	49.28%
CMO s / REMIC s residential	383,268	7,002	(1,062)	389,208	14.87%
Municipal bonds	581,663	22,206	(3,145)	600,724	22.95%
Other securities	5,000		(262)	4,738	0.18%
Total investment securities	$ 2,609,959	$ 48,493	$ (41,145)	$ 2,617,307	100.00%

	December 31, 2012				
	Amortized Cost	Gross Unrealized Holding Gain	Gross Unrealized Holding Loss	Fair Value	Total Percent
	(Dollars in thousands)				
Investment securities available-for-sale:					
Government agency	$ 357,960	$ 1,588	$ (248)	$ 359,300	14.67%
Residential mortgage-backed securities	862,196	25,529	(127)	887,598	36.24%
CMO s / REMIC s residential	565,968	7,402	(1,410)	571,960	23.35%
Municipal bonds	583,692	41,920	(183)	625,429	25.53%
Other securities	5,000	100		5,100	0.21%
Total investment securities	$ 2,374,816	$ 76,539	$ (1,968)	$ 2,449,387	100.00%

Approximately 77% of the available-for-sale portfolio at September 30, 2013 represents securities issued by the U.S government or U.S. government-sponsored agencies and enterprises, with the implied guarantee of payment of principal and interest. The remaining CMO/REMICs are backed by agency-pooled collateral or whole loan collateral. All non-agency available-for-sale CMO/REMIC issues held are rated investment grade or better by either Standard & Poor s or Moody s, as of September 30, 2013 and December 31, 2012. The Company had $679,000 and $1.2 million in CMO/REMIC s backed by whole loans issued by private-label companies (non-government sponsored) as of September 30, 2013, and December 31, 2012, respectively.

During the first quarter of 2013, we identified 13 securities with a par value of $94.2 million that were experiencing accelerated prepayment speeds that were causing a deterioration in yield. We elected to sell these securities and recognized a net pre-tax gain on sale of $2.1 million. There were no gains or losses recognized during the second and third quarters of 2013. In the third quarter of 2013, we purchased $314.7 million of investment securities and utilized short-term borrowings to facilitate a portion of these purchases.

The tables below show the Company s investment securities gross unrealized losses and fair value by investment category and length of time that individual securities have been in a continuous unrealized loss position at September 30, 2013 and December 31, 2012. The Company has reviewed individual securities to determine whether a decline in fair value below the amortized cost basis is other-than-temporary.

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	September 30, 2013					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses
	(Dollars in thousands)					
Available-for-sale:						
Government agency	$ 312,948	$ 20,603	$	$	$ 312,948	$ 20,603
Residential mortgage-backed securities	473,190	16,073			473,190	16,073
CMO / REMICs residential	92,281	988	18,700	74	110,981	1,062
Municipal bonds	42,859	2,671	10,393	474	53,252	3,145
Other securities	4,738	262			4,738	262
Total	$ 926,016	$ 40,597	$ 29,093	$ 548	$ 955,109	$ 41,145

	December 31, 2012					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses
	(Dollars in thousands)					
Available-for-sale:						
Government agency	$ 51,134	$ 248	$	$	$ 51,134	$ 248
Residential mortgage-backed securities	55,118	127			55,118	127
CMO / REMICs residential	74,784	572	69,042	838	143,826	1,410
Municipal bonds	13,110	162	975	21	14,085	183
Other securities						
Total	$ 194,146	$ 1,109	$ 70,017	$ 859	$ 264,163	$ 1,968

The following summarizes our analysis of these securities and the unrealized losses. This assessment was based on the following factors: i) the length of the time and the extent to which the fair value has been less than amortized cost; ii) adverse condition specifically related to the security, an industry, or a geographic area and whether or not the Company expects to recover the entire amortized cost, iii) historical and implied volatility of the fair value of the security; iv) the payment structure of the security and the likelihood of the issuer being able to make payments in the future; v) failure of the issuer of the security to make scheduled interest or principal payments, vi) any changes to the rating of the security by a rating agency, and vii) recoveries or additional declines in fair value subsequent to the balance sheet date.

CMO Held-to-Maturity We have one investment security classified as held-to-maturity. This security was issued by Countrywide Financial and is collateralized by Alt-A mortgages. The mortgages are primarily fixed-rate, 30-year loans, originated in early 2006 with average FICO scores of 715 and an average LTV of 71% at origination. The security was a senior security in the securitization, was rated triple AAA at origination and was supported by subordinate securities. This security is classified as held-to-maturity as we have both the intent and ability to hold this debt security to maturity. We acquired this security in February 2008 at a price of 98.25%. The significant decline in the fair value of the security first appeared in August 2008 at the time the financial crisis in the markets occurred and the market for securities collateralized by Alt-A mortgages diminished.

As of September 30, 2013, the unrealized loss on this security was zero and the current fair value on the security was 73% of the current par value. This Alt-A bond, with a book value of $1.8 million as of September 30, 2013, has had $1.9 million in net impairment losses to date. These losses have been recorded as a reduction to noninterest income. The security is rated non-investment grade. We evaluated the security for an other-than-temporary decline in fair value as of September 30, 2013. The key assumptions include default rates, loss severities and prepayment rates. There were no changes in credit related other-than temporary impairment recognized in earnings for the three and nine months ended September 30, 2013, and 2012.

Government Agency & Government-Sponsored Enterprise The government agency bonds are backed by the full faith and credit of agencies of the U.S. Government. While the Government-Sponsored Enterprise bonds are not expressly guaranteed by the U.S. Government, they are currently being supported by the U.S. Government under a conservatorship arrangement. As of September 30, 2013, approximately $144.4 million in U.S. government agency bonds are callable. These securities are bullet securities, that is, they have a defined maturity date on which the principal is paid. The contractual term of these investments provides that the Company will receive the face value of the bond at maturity which will equal the amortized cost of the bond. Interest is received throughout the life of the security.

Mortgage-Backed Securities and CMO/REMICs Almost all of the available-for-sale mortgage-backed and CMO/REMICs securities are issued by government agencies or government-sponsored enterprises such as Ginnie Mae, Fannie Mae and Freddie Mac. These securities are collateralized or backed by the underlying residential mortgages. All mortgage-backed securities are considered to be rated investment grade with a weighted average life of approximately 4.8 years. Of the total MBS/CMO, 99.96% have the implied guarantee of U.S. government-sponsored agencies and enterprises. The remaining 0.04% are issued by banks. Accordingly, it is expected the securities would not be settled at a price less than the amortized cost of the bonds.

Municipal Bonds The majority of our municipal bonds are insured by the largest bond insurance companies with maturities of approximately 8.9 years. The Company diversifies its holdings by owning selections of securities from different issuers and by holding securities from geographically diversified municipal issuers, thus reducing the Company s exposure to any single adverse event. Because we believe the decline in fair value is attributable to the changes in interest rates and not credit quality and because the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of their amortized costs, which may be at maturity, management does not consider these investments to be other than temporarily impaired at September 30, 2013.

We are continually monitoring the quality of our municipal bond portfolio in light of the current financial problems exhibited by certain monoline insurance companies. Many of the securities that would not be rated without insurance are pre-refunded and/or are general obligation bonds. We continue to monitor municipalities, which includes a review of the respective municipalities audited financial statements to determine whether there are any audit or performance issues. We use outside brokers to assist us in these analyses. Based on our monitoring of the municipal marketplace, to our knowledge, none of the municipalities are exhibiting financial problems that would lead us to believe that there is an OTTI for any given security.

At September 30, 2013 and December 31, 2012, investment securities having a carrying value of approximately $2.61 billion and $2.24 billion, respectively, were pledged to secure public deposits, short and long-term borrowings, and for other purposes as required or permitted by law.

The amortized cost and fair value of debt securities at September 30, 2013, by contractual maturity, are shown below. Although mortgage-backed securities and CMO/REMICs have contractual maturities through 2043, expected maturities will differ from contractual maturities because borrowers may have the right to prepay such obligations without penalty. Mortgage-backed securities and CMO/REMICs are included in maturity categories based upon estimated prepayment speeds.

	September 30, 2013	
		Weighted-

	Amortized Cost	Fair Value	Average Yield
	(Dollars in thousands)		
Available-for-sale:			
Due in one year or less	$ 130,984	$ 133,474	2.39%
Due after one year through five years	1,895,032	1,919,812	2.22%
Due after five years through ten years	527,503	508,724	2.37%
Due after ten years	56,440	55,297	3.49%
Total	$ 2,609,959	$ 2,617,307	2.28%

The investment in FHLB stock is periodically evaluated for impairment based on, among other things, the capital adequacy of the FHLB and its overall financial condition. No impairment losses have been recorded through September 30, 2013.

6. LOAN AND LEASE FINANCE RECEIVABLES AND ALLOWANCE FOR LOAN LOSSES

The following tables provide a summary of the components of loan and lease finance receivables:

	September 30, 2013		
	Non-Covered Loans	Covered Loans	Total
	(Dollars in thousands)		
Commercial and industrial	$ 510,566	$ 20,825	$ 531,391
Real estate:			
Commercial real estate	2,126,415	147,289	2,273,704
Construction	47,648	661	48,309
SFR mortgage	192,130	327	192,457
Dairy & livestock and agribusiness	261,638	3,659	265,297
Municipal lease finance receivables	99,188		99,188
Consumer and other loans	52,886	5,102	57,988
Gross loans	3,290,471	177,863	3,468,334
Less:			
Purchase accounting discount		(14,529)	(14,529)
Deferred loan fees, net	(9,119)		(9,119)
Gross loans, net of deferred loan fees and discount	3,281,352	163,334	3,444,686
Less: Allowance for loan losses	(80,713)		(80,713)
Net loans	$ 3,200,639	$ 163,334	$ 3,363,973

	December 31, 2012		
	Non-Covered Loans	Covered Loans	Total
	(Dollars in thousands)		
Commercial and industrial	$ 547,422	$ 26,149	$ 573,571
Real estate:			
Commercial real estate	1,990,107	179,428	2,169,535
Construction	59,721	1,579	61,300
SFR mortgage	159,288	1,415	160,703
Dairy & livestock and agribusiness	336,660	5,651	342,311
Municipal lease finance receivables	105,767		105,767
Consumer and other loans	60,273	6,337	66,610
Gross loans	3,259,238	220,559	3,479,797
Less:			
Purchase accounting discount		(25,344)	(25,344)
Deferred loan fees, net	(6,925)		(6,925)

Gross loans, net of deferred loan fees and discount	3,252,313		195,215	3,447,528
Less: Allowance for loan losses	(92,441)			(92,441)
Net loans	$ 3,159,872	$	195,215	$ 3,355,087

As of September 30, 2013, 65.56% of the total gross loan portfolio consisted of commercial real estate loans and 1.39% of the total gross loan portfolio consisted of construction loans, respectively. Substantially all of the Company s real estate loans and construction loans are secured by real properties located in California. At September 30, 2013, the Company held approximately $1.73 billion of fixed rate loans.

At September 30, 2013 and December 31, 2012, loans totaling $1.99 billion and $2.32 billion, respectively, were pledged to secure borrowings from the FHLB and the Federal Reserve Bank.

Credit Quality Indicators

Central to our credit risk management is our loan risk rating system. The originating credit officer assigns borrowers an initial risk rating, which is reviewed and confirmed or changed, as appropriate, by Credit Management. Approvals are made based upon the amount of inherent credit risk specific to the transaction and are reviewed for appropriateness by senior line and credit management personnel. Credits are monitored by line and credit management personnel for deterioration in a borrower s financial condition, which would impact the ability of the borrower to perform under the contract. Risk ratings are adjusted as necessary.

Loans are risk rated into the following categories (Credit Quality Indicators): Pass, Pass Watch List, Special Mention, Substandard, Doubtful and Loss. Each of these groups is assessed for the proper amount to be used in determining the adequacy of our allowance for losses. These categories can be described as follows:

Pass These loans range from minimal credit risk to lower than average, but still acceptable, credit risk.

Pass Watch List Pass Watch list loans usually require more than normal management attention. Loans which qualify for the Pass Watch List may involve borrowers with adverse financial trends, higher debt/equity ratios, or weaker liquidity positions, but not to the degree of being considered a defined weakness or problem loan where risk of loss may be apparent.

Special Mention Loans assigned to this category are currently protected but are weak. Although concerns exist, the Company is currently protected and loss is unlikely. Such loans have potential weaknesses that may, if not checked or corrected, weaken the asset or inadequately protect the Company s credit position at some future date.

Substandard Loans classified as substandard include poor liquidity, high leverage, and erratic earnings or losses. The primary source of repayment is no longer realistic, and asset or collateral liquidation may be the only source of repayment. Substandard loans are marginal and require continuing and close supervision by credit management. Substandard loans have the distinct possibility that the Company will sustain some loss if deficiencies are not corrected.

Doubtful Loans classified doubtful have all the weaknesses inherent in those classified substandard with the added provision that the weaknesses make collection or the liquidation, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonable specific pending factors which may work to the advantage and strengthening of the assets, their classifications as losses are deferred until their more exact status may be determined.

Loss Loans classified as loss are considered uncollectible and of such little value that their continuance as active assets of the Company is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be achieved in the future.

The following table summarizes our internal risk grouping by loan class as of September 30, 2013 and December 31, 2012:

Credit Quality Indicators

	September 30, 2013					
	Pass	Watch List	Special Mention	Substandard	Doubtful & Loss	Total
	(Dollars in thousands)					
Commercial and industrial	$ 308,271	$ 131,118	$ 53,972	$ 16,730	$ 475	$ 510,566
Real estate:						
Commercial real estate						
Owner occupied	441,739	128,887	89,475	65,455		725,556
Non-owner occupied	1,040,758	217,822	85,784	56,495		1,400,859
Construction						
Speculative	7,568		1,538	18,020		27,126
Non-speculative	6,408	4,895		9,219		20,522
SFR mortgage	152,169	20,960	4,319	14,682		192,130
Dairy & livestock and agribusiness	44,735	39,360	102,464	72,879	2,200	261,638
Municipal lease finance receivables	51,935	19,540	21,283	6,430		99,188
Consumer and other loans	41,555	6,379	3,410	1,539	3	52,886
Total non-covered loans	2,095,138	568,961	362,245	261,449	2,678	3,290,471
Covered loans	35,125	67,347	23,477	51,914		177,863
Total gross loans	$ 2,130,263	$ 636,308	$ 385,722	$ 313,363	$ 2,678	$ 3,468,334

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	December 31, 2012					
	Pass	**Watch List**	**Special Mention**	**Substandard**	**Doubtful & Loss**	**Total**
	(Dollars in thousands)					
Commercial and industrial	$ 347,275	$ 131,186	$ 44,466	$ 22,901	$ 1,594	$ 547,422
Real estate:						
Commercial real estate						
Owner occupied	382,111	159,653	78,087	84,116		703,967
Non-owner occupied						