



Edgar Filing: CENTRAL VALLEY COMMUNITY BANCORP - Form 10-K

Yes

No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

Yes

No

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

No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

Yes

No

As of **June 30, 2006**, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was \$63,023,000 based on the average bid and asked price.

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

Common Stock, No Par Value

Outstanding at March 21, 2007

[Common Stock, No par value per share]

6,018,246 shares

**DOCUMENTS INCORPORATED BY REFERENCE**

Document

Parts Into Which Incorporated

Proxy Statement for the Annual Meeting of Shareholders to be held May 16, 2007 (Proxy Statement)

Part III

**TABLE OF CONTENTS**

<u>ITEM 1 -</u>	<u>DESCRIPTION OF BUSINESS</u>
<u>ITEM 2 -</u>	<u>DESCRIPTION OF PROPERTY</u>
<u>ITEM 3 -</u>	<u>LEGAL PROCEEDINGS</u>
<u>ITEM 4 -</u>	<u>SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS</u>
<u>ITEM 5 -</u>	<u>MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS</u>
<u>ITEM 7-</u>	<u>MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION</u>
<u>ITEM 8 -</u>	<u>FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u>
<u>ITEM 9 -</u>	<u>CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE</u>
<u>ITEM 10 -</u>	<u>DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(a) OF THE EXCHANGE ACT</u>
<u>ITEM 11 -</u>	<u>EXECUTIVE COMPENSATION</u>
<u>ITEM 12 -</u>	<u>SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u>
<u>ITEM 13 -</u>	<u>CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS</u>
<u>ITEM 15 -</u>	<u>EXHIBITS</u>
<u>SIGNATURES</u>	

---

**ADDITIONAL INFORMATION; INQUIRIES**

Under the Securities Exchange Act of 1934, Sections 13 and 15 (d), periodic and current reports must be filed with the SEC. We electronically file the following reports with the SEC:

- Form 10-K Annual Report
- Form 10-Q Quarterly Report
- Form 8-K Report of Unscheduled Material Events
- Form DEF 14A Proxy Statement.

We may file additional forms. The SEC maintains an Internet site, [www.sec.gov](http://www.sec.gov), in which all forms filed electronically may be accessed. Additional shareholder information regarding the Company and our Directors is available on our website: [www.cvcb.com](http://www.cvcb.com). None of the information on or hyperlinked from our website is incorporated into this Report.

**Copies of the annual report on Form 10-K for the year ended December 31, 2006 may be obtained without charge upon written request to Dave Kinross, Chief Financial Officer, at the Company's administrative offices, 600 Pollasky Ave., Clovis, CA 93612.**

Inquiries regarding Central Valley Community Bancorp's accounting, internal controls or auditing concerns should be directed to Steven D. McDonald, chairman of the Board of Directors' Audit Committee, at [steve.mcdonald@cvcb.com](mailto:steve.mcdonald@cvcb.com) or anonymously at [www.ethicspoint.com](http://www.ethicspoint.com) or EthicsPoint, Inc. at 1-866-294-9588.

General inquiries about the Central Valley Community Bancorp or Central Valley Community Bank should be directed to Cathy Ponte, Assistant Corporate Secretary at 1-800-298-1775.

**PART I**

**ITEM 1 - DESCRIPTION OF BUSINESS**

**General**

Central Valley Community Bancorp (the "Company") was incorporated on February 7, 2000 as a California corporation, for the purpose of becoming the holding company for Central Valley Community Bank (the "Bank"), formerly known as Clovis Community Bank, a California state chartered bank, through a corporate reorganization. In the reorganization, the Bank became the wholly-owned subsidiary of the Company, and the shareholders of the Bank became the shareholders of the Company. The Company is registered as a bank holding company under the Bank Holding Company Act of 1956, as amended (the "BHC Act"), and is subject to supervision and regulation by the Board of Governors of the Federal Reserve System (the "Board of Governors").

At December 31, 2006, we had one banking subsidiary, the Bank. Our principal business is to provide, through our banking subsidiary, financial services in our primary market area in California. We serve Fresno County, Madera County, and Sacramento County and their surrounding areas through the Bank. We do not currently conduct any operations other than through the Bank. Unless the context otherwise requires, references to us refer to the Company and the Bank on a consolidated basis. At December 31, 2006, we had consolidated total assets of approximately \$500,059,000. See Items 7 and 8, Management's Discussion and Analysis or Plan of Operation and Financial Statements.

During 2004, the Company approved a stock repurchase plan authorizing the purchase of shares of the Company's common stock up to a total cost of \$500,000, or approximately 2% of its outstanding shares of common stock. As of December 31, 2004, the Company repurchased 18,000 at an average price of \$11.83 for a total cost of \$213,000. On October 20, 2004, the Company announced the suspension of the 2004 stock repurchase plan. We had no repurchase plan in place for 2005.

## Edgar Filing: CENTRAL VALLEY COMMUNITY BANCORP - Form 10-K

During 2006, the Company approved a stock repurchase plan authorizing the purchase of shares of the Company's common stock up to a total cost of \$1,000,000 or approximately 1% of its outstanding shares of common stock during the period from October 23, 2006 to June 30, 2007. As of December 31, 2006, the Company had repurchased 26,200 shares at an average price of \$15.08 for a total cost of \$395,000.

As of March 15, 2007, we had a total of 162 employees and 136.4 full time equivalent employees, including the employees of the Bank.

After the close of business on December 31, 2004, we completed our merger with Bank of Madera County ( BMC ) and BMC was merged into the Bank. We believe that the merger allows us to further accommodate a growing customer base in Madera County, provided Bank of Madera County customers with more convenient locations in the Central Valley, as well as offering new advancement and geographic opportunities for the BMC employees. As a result of the above factors, we believe that the potential for the combined performance exceeded what each entity could accomplish independently and the goodwill in this transaction arose from the synergies associated with the merger. The acquisition was part of our long-term strategy to increase our presence from Sacramento to Bakersfield along the Highway 99 corridor and the surrounding foothills.

As of the date of acquisition, BMC had total assets of \$68,080,000, comprised of \$2,842,000 in cash and due from banks, \$19,250,000 in Federal funds sold, \$45,028,000 in loans (net of allowance for credit losses of \$751,000), \$390,000 in premises and equipment and \$570,000 in other assets. Total liabilities acquired amounted to \$64,208,000, including \$63,769,000 in deposits. The accompanying audited Consolidated Financial Statements included in Item 8 of this Annual Report include the accounts of BMC since January 1, 2005.

### **The Bank**

The Bank was organized in 1979 and commenced business as a California state chartered bank in 1980. The deposits of the Bank are insured by the Federal Deposit Insurance Corporation (the FDIC ) up to applicable limits. The Bank is not a member of the Federal Reserve System.

The Bank operates 12 full-service banking offices in Clovis, Fresno, Kerman, Madera, Oakhurst, Sacramento, and Prather, California. The Oakhurst and Madera branches were added through the BMC merger. One of the offices is in a Save Mart Supermarket and offers extended banking hours, including Saturday hours, for the convenience of the Bank's customers. The Bank has a Real Estate Division and an SBA Lending Division located at our corporate headquarters in Fresno. All real estate related transactions are conducted and processed through the Real Estate Division, including interim construction loans for single family residences and commercial buildings. All types of permanent single family residential loans are also offered. According to the June 30, 2006 FDIC data, the seven branches in Fresno County (Clovis, Fresno, Kerman, and Prather branches) have a 4.8% combined deposit market share of all banks and 3.9% of all depositories including credit unions, thrifts, and savings banks.

The Bank opened full service retail offices in the Fresno downtown area on February 13, 2006 and in the Sunnyside area of Fresno on November 13, 2006. During October 2006, the Company consolidated its administrative offices into a single location on North Financial Drive in Fresno and opened a small branch there.

Branch expansions provide the Company with opportunities to expand its loan and deposit base; however, based on past experience, management expects these new offices will initially have a negative impact on earnings until the volume of business grows to cover fixed overhead expenses. The Bank anticipates additional branch openings to meet the growing service needs of its customers, although none are planned during 2007.

The Bank established an interest in Central Valley Community Insurance Services, LLC ( Insurance Services ) at the end of 2006. The purpose of this new entity is to market insurance products and services primarily to business customers in the area of employee benefit plans.

The Bank conducts a commercial banking business, which includes accepting demand, savings and time deposits and making commercial, real estate and consumer loans. It also issues cashier's checks, sells traveler's checks and provides safe deposit boxes and other customary banking services. The Bank also has offered Internet Banking since 2000. Internet Banking consists of inquiry, account status, bill paying, account transfers, and cash management. The Bank does not offer trust services or international banking services and does not currently plan to do so in the near future.

## Edgar Filing: CENTRAL VALLEY COMMUNITY BANCORP - Form 10-K

Since August of 1995 the Bank has been a party to an agreement with Investment Centers of America, pursuant to which Investment Centers of America provides Bank customers with access to investment services. In connection with entering into this agreement, the Bank adopted a policy intended to comply with FDIC Regulation Section 337.4, which outlines the guidelines under which an insured non-member bank may be affiliated with a company that directly engages in the sale, distribution, or underwriting of stock, bonds, debentures, notes, or other securities.

The Bank's operating policy since its inception has emphasized serving the banking needs of individuals and the business and professional communities in the central valley area of California. At December 31, 2006, we had total loans of \$323,414,000. Total commercial and industrial loans outstanding were \$78,895,000; total agricultural loans outstanding were \$17,102,000, total real estate construction, land development and other land loans outstanding were \$48,424,000; total other real estate loans outstanding were \$149,586,000, total equity lines of credit were \$21,858,000 and total consumer installment loans outstanding were \$7,549,000. We accept real estate, listed securities, savings and time deposits, automobiles, inventory, machinery and equipment as collateral for loans.

No individual or single group of related accounts is considered material in relation to the Bank's assets or deposits, or in relation to the overall business of the Company. However, at December 31, 2006 approximately 68.0% of our loan portfolio held for investment consisted of real estate-related loans, including construction loans, real estate mortgage loans and commercial loans secured by real estate and 24.2% consisted of commercial loans. See Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations. We believe that these concentrations are mitigated by the diversification of our loan portfolio among commercial, commercial and residential construction, commercial mortgage, home equity and consumer loans. In addition, our business activities currently are mainly concentrated in Fresno County, California. Consequently, our results of operations and financial condition are dependent upon the general trends in this part of the California economy and, in particular, the residential and commercial real estate markets. In addition, our concentration of operations in this area of California exposes us to greater risk than other banking companies with a wider geographic base in the event of catastrophes, such as earthquakes, fires and floods in this region or as a result of energy shortages in California.

Our deposits are attracted from individual and commercial customers. A material portion of our deposits have not been obtained from a single person or a few persons, the loss of any one or more of which would have a material adverse effect on our business.

In order to attract loan and deposit business from individuals and small businesses, we maintain the following lobby hours at our branches:

<b>Branch</b>	<b>Monday</b>	<b>Thursday</b>	<b>Friday</b>	<b>Saturday</b>
Clovis Main	9:00 a.m. to 4:00 p.m.		9:00 a.m. to 6:00 p.m.	None
Clovis Main Drive Up	8:00 a.m. to 5:30 p.m.		8:00 a.m. to 6:00 p.m.	None
Foothill	9:00 a.m. to 5:00 p.m.		9:00 a.m. to 6:00 p.m.	9:00 a.m. to 1:00 p.m.
Herndon & Fowler	10:00 a.m. to 7:00 p.m.		10:00 a.m. to 7:00 p.m.	10:00 a.m. to 5:00 p.m.
Fig Garden Village	9:00 a.m. to 5:00 p.m.		9:00 a.m. to 6:00 p.m.	10:00 a.m. to 2:00 p.m.
Kerman	9:00 a.m. to 5:00 p.m.		9:00 a.m. to 6:00 p.m.	None
River Park	9:00 a.m. to 5:00 p.m.		9:00 a.m. to 6:00 p.m.	10:00 a.m. to 2:00 p.m.
River Park Drive Up	9:00 a.m. to 5:30 p.m.		9:00 a.m. to 6:00 p.m.	10:00 a.m. to 2:00 p.m.
Sacramento Private Banking	9:00 a.m. to 4:00 p.m.		9:00 a.m. to 4:00 p.m.	None

Edgar Filing: CENTRAL VALLEY COMMUNITY BANCORP - Form 10-K

Oakhurst	8:30 a.m. to 5:00 p.m.	8:30 a.m. to 6:00 p.m.	None
Madera	8:30 a.m. to 5:00 p.m.	8:30 a.m. to 6:00 p.m.	None
Sunnyside	9:00 a.m. to 5:00 p.m.	9:00 a.m. to 6:00 p.m.	10:00 a.m. to 2:00 p.m.
Sunnyside Drive Up	8:00 a.m. to 5:00 p.m.	8:00 a.m. to 6:00 p.m.	10:00 a.m. to 2:00 p.m.
Financial Drive	8:00 a.m. to 5:00 p.m.	8:00 a.m. to 5:00 p.m.	None
Fresno Downtown	9:00 a.m. to 4:00 p.m. Walkup window 8:00 a.m. to 9:00 a.m.	9:00 a.m. to 5:00 p.m.	None

Automated teller machines operate at 11 branch locations and two non-branch location 24 hours per day, seven days per week. No automated teller machines are currently located at the Sacramento office. Our Real Estate and Small Business Administration ( SBA ) Departments maintain business hours of 8:00 A.M. to 5:00 P.M., Monday through Friday, and extended hours are available upon customer request.

To compete effectively, we rely substantially on local promotional activity, personal contacts by our officers, directors and employees, referrals by our shareholders, extended hours, personalized service and our reputation in the communities we serve.

In Fresno and Madera Counties, in addition to our 10 full-service and one limited service branch locations, serving the Bank's primary service areas, as of December 31, 2006 there were 183 operating banking and credit union offices in our primary service area, which consists of the cities of Clovis, Fresno, Kerman, Oakhurst, Madera, and Prather, California. Prather does not contain any banking offices other than our office. Business activity in our primary service area is oriented toward light industry, small business and agriculture. The June 2006 FDIC Summary of Deposits report indicated the Company had 3.1% of the total deposits held by all depositories in Fresno County and 4.7% in Madera County. In Sacramento County, in addition to our one branch, as of December 31, 2006 there were 246 operating banking and credit union offices in our primary service area.

The banking business in California generally, and our primary service area specifically, is highly competitive with respect to both loans and deposits, and is dominated by a relatively small number of major banks with many offices operating over a wide geographic area. Among the advantages such major banks have over us is their ability to finance wide-ranging advertising campaigns and to allocate their investment assets, including loans, to regions of higher yield and demand. Major banks offer certain services such as international banking and trust services which are not offered directly but which usually can be offered indirectly through correspondent institutions. In addition, by virtue of their greater total capitalization, such banks have substantially higher lending limits than we do. Legal lending limits to an individual customer are limited to a percentage of our total capital accounts. As of December 31, 2006, the Bank's legal loan limits to individual customers were \$6,428,000 for unsecured loans and \$10,714,000 for unsecured and secured loans combined. For borrowers desiring loans in excess of the Bank's lending limits, the Bank makes and may, in the future, make such loans on a participation basis with other community banks taking the amount of loans in excess of the Bank's lending limits. In other cases, the Bank may refer such borrowers to larger banks or other lending institutions.

Other entities, both governmental and in private industry, seeking to raise capital through the issuance and sale of debt or equity securities also provide competition for us in the acquisition of deposits. Banks also compete with money market funds and other money market instruments, which are not subject to interest rate ceilings. In recent years, increased competition has also developed from specialized finance and non-finance companies that offer wholesale finance, credit card, and other consumer finance services, including on-line banking services and personal finance software. Competition for deposit and loan products remains strong, from both banking and non-banking firms, and affects the rates of those products as well as the terms on which they are offered to customers.

Technological innovation continues to contribute to greater competition in domestic and international financial services markets. Technological innovation has, for example, made it possible for non-depository institutions to offer customers automated transfer payment services that previously have been traditional banking products. In addition, customers now expect a choice of several delivery systems and channels, including telephone, mail, home computer, ATMs, self-service branches, and in-store branches.

Mergers between financial institutions have placed additional pressure on banks to streamline their operations, reduce expenses, and increase revenues to remain competitive. In addition, competition has intensified due to federal and state interstate banking laws, which permit banking organizations to expand geographically with fewer restrictions than in the past. Such laws allow banks to merge with other banks across state lines, thereby enabling banks to establish or expand banking operations in our market. The competitive environment also is significantly impacted by federal and state legislation, which may make it easier for non-bank financial institutions to compete with us.

#### **Statistical Disclosure**

The information in the tables set out below should be read in conjunction with the Company's audited consolidated financial statements and the notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations, which are included in Items 7 and 8 of this annual report.

#### **Distribution of Average Assets, Liabilities and Shareholders' Equity; Interest Rates and Interest Differential**

Table A sets forth our average consolidated balance sheets for the years ended December 31, 2006, 2005 and 2004 and an analysis of interest rates and the interest rate differential for the years then ended. Table B sets forth the changes in interest income and interest expense in 2006 and 2005 resulting from changes in volume and changes in rates.

#### **Investment Portfolio**

The book value (amortized cost) of investment securities at December 31, 2006, 2005 and 2004 and the book value, maturities and weighted average yield of investment securities at December 31, 2006 are set forth in Table C.

#### **Loan Portfolio**

The composition of the loan portfolio at December 31, 2006, 2005, 2004, 2003, and 2002, is summarized in Table D.

Maturities and sensitivity to changes in interest rates in the loan portfolio at December 31, 2006 are summarized in Table E.

Table F shows the composition of non-accrual, past due and restructured loans at December 31, 2006, 2005, 2004, 2003, and 2002. Set forth in the text accompanying Table F is a discussion of the Company's policy for placing loans on non-accrual status.

#### **Summary of Loan Loss Experience**

Table G sets forth an analysis of loan loss experience as of and for the years ended December 31, 2006, 2005, 2004, 2003, and 2002.

Set forth in the text accompanying Table G is a description of the factors which influenced management's judgment in determining the amount of the additions to the allowance charged to operating expense in each fiscal year, a table showing the allocation of the allowance for credit losses to the various types of loans in the portfolio, as well as a discussion of management's policy for establishing and maintaining the allowance for credit losses.

#### **Deposits**

Table H sets forth the average amount of and the average rate paid on major deposit categories for the years ended December 31, 2006, 2005, and 2004.

Table I sets forth the maturity of time certificates of deposit of \$100,000 or more at December 31, 2006.



**Return on Equity and Assets**

Table J sets forth certain financial ratios for the years ended December 31, 2006, 2005, 2004, 2003 and 2002.

5

---

Table A

**DISTRIBUTION OF AVERAGE ASSETS, LIABILITIES AND SHAREHOLDERS EQUITY; INTEREST RATES AND INTEREST DIFFERENTIAL**

The following table sets forth consolidated average assets, liabilities and shareholders' equity; interest income earned and interest expense paid; and the average yields earned or rates paid thereon for the years ended December 31, 2006, 2005, and 2004. The average balances reflect daily averages except non-accrual loans, which were computed using quarterly averages.

(Dollars in thousands)	2006			2005			2004		
	Average Balance	Interest Income/Expense	Average Interest Rate	Average Balance	Interest Income/Expense	Average Interest Rate	Average Balance	Interest Income/Expense	Average Interest Rate
<b>ASSETS:</b>									
Interest-earning deposits in other banks	\$ 634	\$ 22	3.47 %	\$ 2,136	\$ 59	2.76 %	\$ 2,192	\$ 37	1.69 %
Securities:									
Taxable securities	74,915	3,191	4.26 %	86,857	3,002	3.46 %	77,734	2,462	3.17 %
Non-taxable securities (1)	26,749	1,556	5.82 %	25,096	1,806	7.20 %	18,833	1,271	6.75 %
Total investment securities	101,664	4,747	4.67 %	111,953	4,808	4.29 %	96,567	3,733	3.87 %
Federal funds sold	23,404	1,165	4.98 %	21,590	702	3.25 %	16,310	234	1.43 %
Total	125,702	5,934	4.72 %	135,679	5,569	4.10 %	115,069	4,004	3.48 %
Loans (2)(3)	303,867	25,527	8.40 %	276,957	21,115	7.63 %	195,187	13,227	6.78 %
Federal Home Loan Bank stock	1,799	89	4.95 %	1,621	68	4.19 %	1,200	41	3.42 %
Total interest-earning assets (1)	431,368	\$ 31,550	7.31 %	414,257	\$ 26,752	6.46 %	311,456	\$ 17,272	5.55 %
Allowance for credit losses	(3,483 )			(3,507 )			(2,565 )		
Non-accrual loans	207			898			36		
Cash and due from banks	17,404			19,365			23,567		
Bank premises and equipment	3,369			3,004			2,863		
Other non-earning assets	21,356			21,663			10,860		
Total average assets	\$ 470,221			\$ 455,680			\$ 346,217		

Edgar Filing: CENTRAL VALLEY COMMUNITY BANCORP - Form 10-K

(Dollars in Thousands)	2006			2005			2004			
	Average Balance	Interest Income/Expense	Average Interest Rate	Average Balance	Interest Income/Expense	Average Interest Rate	Average Balance	Interest Income/Expense	Average Interest Rate	
<b>LIABILITIES AND SHAREHOLDERS EQUITY:</b>										
Deposits:										
Savings and NOW accounts	\$ 78,410	\$ 162	0.21	% \$ 83,781	\$ 149	0.18	% \$ 67,099	\$ 118	0.18	%
Money market accounts (MMA)	105,632	2,467	2.34	% 111,519	1,500	1.35	% 84,178	660	0.78	%
Time certificates of deposit, under \$100,000	53,208	1,499	2.82	% 50,841	1,017	2.00	% 37,082	550	1.48	%
Time certificates of deposit, \$100,000 and over	44,910	2,082	4.64	% 36,872	1,220	3.31	% 21,884	465	2.12	%
Total interest-bearing deposits	282,160	6,210	2.20	% 283,013	3,886	1.37	% 210,243	1,793	0.85	%
Other borrowed funds	6,774	349	5.15	% 6,725	253	3.76	% 7,311	185	2.53	%
Federal funds purchased							2			
Total interest-bearing liabilities	288,934	\$ 6,559	2.27	% 289,738	\$ 4,139	1.43	% 217,556	\$ 1,978	0.91	%
Non-interest bearing demand deposits	132,150			124,175			97,210			
Other liabilities	3,573			3,076			3,248			
Shareholders' equity	45,564			38,691			28,203			
Total average liabilities and shareholders' equity	\$ 470,221			\$ 455,680			\$ 346,217			
Interest income and rate earned on average earning assets (1)		\$ 31,550	7.31	%	\$ 26,752	6.46	%	\$ 17,272	5.55	%
Interest expense and interest cost related to average interest-bearing liabilities		6,559	2.27	%	4,139	1.43	%	1,978	0.91	%
Net interest income and net interest margin (4)		\$ 24,991	5.79	%	\$ 22,613	5.46	%	\$ 15,294	4.91	%

- (1) Computed on a tax equivalent basis, which includes Federal tax benefits relating to income earned on municipal bonds totaling \$529, \$614, and \$432 in 2006, 2005 and 2004, respectively.
- (2) Loan interest income includes loan fees of \$798 in 2006; \$961 in 2005; and \$808 in 2004.
- (3) Average loans do not include non-accrual loans.
- (4) Net interest margin is computed by dividing net interest income by total average interest-earning assets.

Table B

**VOLUME AND RATE ANALYSIS**

The following table sets forth, for the years indicated, a summary of the changes in interest earned and interest paid resulting from changes in asset and liability volumes and changes in rates. The change in interest due to both volume and rate has been allocated to change due to volume and rate in proportion to the relationship of absolute dollar amounts of change in each.

(In thousands)	Year Ended December 31			2005 Compared to 2004		
	2006 Compared to 2005		Net	Volume	Rate	Net
	Volume	Rate				
Increase (decrease) due to changes in:						
Interest income:						
Interest-earning deposits in other banks	\$ (59 )	\$ 22	\$ (37 )	\$ (1 )	\$ 23	\$ 22
Investment securities:						
Taxable	(274 )	463	189	304	236	540
Non-taxable (1)	131	(381 )	(250 )	446	89	535
Total investment securities	(143 )	82	(61 )	750	325	1,075
Federal funds sold	63	400	463	95	373	468
Loans	2,154	2,258	4,412	6,009	1,879	7,888
FHLB Stock	8	13	21	16	11	27
Total earning assets (1)	2,023	2,775	4,798	6,869	2,611	9,480
Interest expense:						
Deposits:						
Savings, NOW and MMA	(89 )	1,069	980	272	599	871
Certificates of deposit under \$100,000	49	433	482	241	226	467
Certificates of deposit \$100,000 and over	304	558	862	416	339	755
Total interest-bearing deposits	264	2,060	2,324	929	1,164	2,093
Other borrowed funds	2	94	96	(13 )	81	68
Total interest bearing liabilities	266	2,154	2,420	916	1,245	2,161
Net interest income (1)	\$ 1,757	\$ 621	\$ 2,378	\$ 5,953	\$ 1,366	\$ 7,319

(1) Computed on a tax equivalent basis for securities exempt from federal income taxes.

**Table C****INVESTMENT PORTFOLIO**

The book value of investment securities at December 31, 2006, 2005, and 2004 is set forth in the following table. At December 31, 2006, we held no investment securities from any issuer which totaled over 10% of our shareholders' equity.

Available for Sale (In thousands)	Book Value at December 31		
	2006	2005	2004
U.S. Treasury securities and obligations of other U.S. government agencies and corporations	\$ 28,643	\$ 23,314	\$ 22,492
Mortgage-backed securities	45,561	48,479	52,292
Obligations of states and political subdivisions	26,210	31,036	19,993
Other securities	3,703	3,608	3,644
Total Available-for-Sale Securities	\$ 104,117	\$ 106,437	\$ 98,421

Edgar Filing: CENTRAL VALLEY COMMUNITY BANCORP - Form 10-K

The book value, maturities and weighted average yield of investment securities at December 31, 2006 are summarized in the following table.

(Dollars in Thousands) Available for Sale	In one year or less		After one through five years		After five through ten years		After ten years		Total		
	Amount	Yield(1)	Amount	Yield(1)	Amount	Yield(1)	Amount	Yield(1)	Amount	Yield(1)	
Obligations of other U.S. Government agencies and corporations	\$ 10,148	3.89	% \$ 18,495	4.21	% \$		\$		\$ 28,643	4.10	%
Mortgage-backed securities	157	4.50	% 1,263	4.50	% 4,907	5.21	% 39,234	5.46	% 45,561	5.40	%
Obligations of states & political subdivisions	300	4.75	% 1,377	4.30	% 12,993	4.47	% 11,540	2.85	% 26,210	3.60	%
Other securities	3,703	4.60	%						3,703	4.60	%
<b>Total Available for Sale</b>	<b>\$ 14,308</b>	<b>4.10</b>	<b>% \$ 21,135</b>	<b>4.24</b>	<b>% \$ 17,900</b>	<b>4.67</b>	<b>% \$ 50,774</b>	<b>4.87</b>	<b>% \$ 104,117</b>	<b>4.56</b>	<b>%</b>

(1) Not computed on a tax equivalent basis.

10

**Table D****LOAN PORTFOLIO**

The composition of the loan portfolio at December 31, 2006, 2005, 2004, 2003, and 2002 is summarized in the table below.

<b>(In thousands)</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>	<b>2002</b>
Commercial and industrial	\$ 78,441	\$ 82,978	\$ 57,669	\$ 55,506	\$ 47,790
Real estate					
Construction, land development & other land loans	48,424	46,523	35,364	25,232	20,379
Other	149,586	124,043	75,424	77,468	72,252
Equity lines of credit	21,858	23,604	18,714	12,565	6,086
Loans to finance agricultural production or other loans to farmers	17,102	17,547	15,946	10,714	3,285
Installment loans to individuals for household, family and other personal expenditures	7,549	7,539	6,420	5,117	5,581
Leases					3,828
Other	454	160	240	320	13
Subtotal	323,414	302,394	209,777	186,922	159,214
Deferred loan fees, net	(752 )	(592 )	(498 )	(648 )	(488 )
Subtotal	322,662	301,802	209,279	186,274	158,726
Allowance for credit losses	(3,809 )	(3,339 )	(2,697 )	(2,425 )	(2,433 )
Total (1)	\$ 318,853	\$ 298,463	\$ 206,582	\$ 183,849	\$ 156,293

(1)Includes non-accrual loans of:

<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>	<b>2002</b>
	\$ 616		\$ 634	\$ 466

**Table E****LOAN MATURITIES AND SENSITIVITY TO CHANGES IN INTEREST RATES**

The following table presents information concerning loan maturities and sensitivity to changes in interest rates of the indicated categories of our loan portfolio, as well as loans in those categories maturing after one year that have fixed or floating interest rates at December 31, 2006.

(In thousands)	One Year or Less	After One Through Five Years	After Five Years	Total
Real estate construction	\$ 46,146	\$ 2,278	\$	\$ 48,424
Other real estate	64,085	92,445	14,914	171,444
Commercial, agricultural and other	72,488	20,860	2,649	95,997
Installment	4,918	1,683	948	7,549
	\$ 187,637	\$ 117,266	\$ 18,511	\$ 323,414
Sensitivity to Changes in Interest Rates:				
Loans with Fixed Interest Rates	\$ 19,105	\$ 27,897	\$ 15,772	\$ 62,774
Loans with Floating Interest Rates	168,532	89,369	2,739	260,640
Total	\$ 187,637	\$ 117,266	\$ 18,511	\$ 323,414

**Table F****COMPOSITION OF NON-ACCRUAL, PAST DUE AND RESTRUCTURED LOANS**

A summary of non-accrual, restructured and past due loans at December 31, 2006, 2005, 2004, 2003, and 2002 is set forth below:

(Dollars in thousands)	December 31				
	2006	2005	2004	2003	2002
Non-accrual	\$	\$ 616	\$	\$ 634	\$ 466
Accruing loans past due 90 days or more					
Restructured loans					615
	\$	\$ 616	\$	\$ 634	\$ 1,081
Non-accrual loans to total loans	0.0	% 0.2	% 0.0	% 0.3	% 0.3

Our consolidated financial statements are prepared on the accrual basis of accounting, including the recognition of interest income on loans. Interest income from non-accrual loans is recorded only if collection of principal in full is not in doubt and when and if received.



Loans are placed on non-accrual status and any accrued but unpaid interest income is reversed and charged against income when the payment of interest or principal is 90 days or more past due. Loans in the non-accrual category are treated as non-accrual loans even though we may ultimately recover all or a portion of the interest due. These loans return to accrual status when the loan becomes contractually current and future collectibility of amounts due is reasonably assured. There were no loans on non-accrual at December 31, 2006 or interest foregone on nonaccrual loans for the year then ended. See Note 4 of Company's audited Consolidated Financial Statements in Item 8 of this Annual Report.

There were \$616,000 in loans on non-accrual at December 31, 2005. At December 31, 2005 interest foregone on nonaccrual loans totaled \$76,000 for the year then ended. There were no loans on nonaccrual at December 31, 2004 or interest foregone on nonaccrual loans for the year then ended.

In 2002, we had one restructured loan in the principal amount of \$615,000. At December 31, 2006, 2005, 2004 and 2003 the Company had no restructured loans. See Note 4 of the Company's audited Consolidated Financial Statements in Item 8 of this Annual Report concerning our recorded investment in loans for which an impairment has been recognized. Impaired loans are identified from internal credit review reports, past due reports, overdraft listings, and regulatory reports of examination. Borrowers experiencing problems such as operating losses, marginal working capital, inadequate cash flow or business interruptions which jeopardize collection of the loan are also reviewed for possible impairment classification.

When a loan is classified as impaired, the net fair value (i.e., the measure of the impaired loan) is computed based on the present value of expected future cash flows discounted at the loan's effective interest rate. Alternatively, if the loan is collateral dependent, impairment is measured based on the fair value or market price of the collateral. If the net fair value of the impaired loan is less than the recorded investment in the loan, then the resulting impairment amount is recognized through the allowance for credit losses with a corresponding charge to the provision for credit losses. A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due (including both principal and interest) in accordance with the contractual terms of the loan agreement.

As of December 31, 2006, we had no loans where known information about possible credit problems of borrowers caused management to have serious doubts as to the ability of such borrowers to comply with the present loan repayment terms and which may result in disclosure of such loans as impaired loans.

Table G

**SUMMARY OF LOAN LOSS EXPERIENCE**

The following table summarizes loan loss experience as of and for the years ended December 31, 2006, 2005, 2004, 2003, and 2002.

(Dollars in Thousands)	2006	2005	2004	2003	2002	
Loans outstanding at December 31,	\$ 323,414	\$ 302,394	\$ 209,777	\$ 186,922	\$ 159,214	
Average loans outstanding during year	\$ 304,074	\$ 277,855	\$ 195,223	\$ 174,708	\$ 148,654	
Allowance for credit losses:						
Balance at beginning of year	\$ 3,339	\$ 2,697	\$ 2,425	\$ 2,433	\$ 2,474	
Deduct loans charged-off:						
Commercial and industrial	(539 )	(702 )		(172 )	(289 )	
Real estate construction						
Real estate other						
Loans to finance agricultural and other loans to farmers						
Loans to individuals for household, family and other personal expenditures	(182 )	(85 )	(24 )	(45 )	(63 )	
Other						
Total loans charged-off	(721 )	(787 )	(24 )	(217 )	(352 )	
Add recoveries of loans charged off:						
Commercial and industrial	293	10	273	167	275	
Real estate construction						
Real estate other		25		9		
Loans to finance agricultural and other loans to farmers						
Loans to individuals for household, family and other personal expenditures	98	48	23	33	36	
Other		85				
Total recoveries	391	168	296	209	311	
Net (charge-offs) recoveries	(330 )	(619 )	272	(8 )	(41 )	
Allowance acquired in merger of Bank of Madera County		751				
Add provision charged to operating expense	800	510				
Balance at end of year	\$ 3,809	\$ 3,339	\$ 2,697	\$ 2,425	\$ 2,433	
Allowance for credit losses as a percentage of outstanding loan balance	1.18	% 1.11	% 1.29	% 1.30	% 1.53	%
Net (charge-offs) recoveries to average loans outstanding	(0.11	)(0.22	)0.14	%(0.01	)(0.03	)%

Managing credits identified through the risk evaluation methodology includes developing a business strategy with the customer to mitigate our losses. Our management continues to monitor these credits with a view to identifying as early as possible when, and to what extent, additional provisions may be necessary.

The allowance for credit losses is reviewed at least quarterly by the Bank's and our Board of Directors' Audit/Compliance Committee and by the Bank's and our Board of Directors. Reserves are allocated to loan portfolio segments using percentages which are based on both historical risk elements such as delinquencies and losses and predictive risk elements such as economic, competitive and environmental factors. We have adopted the specific reserve approach to allocate reserves to each adversely graded asset, as well as to each impaired asset for the purpose of estimating potential loss exposure. Although the allowance for credit losses is allocated to various portfolio categories, it is general in nature and available for the loan portfolio in its entirety. Additions may be required based on the results of independent loan portfolio examinations, regulatory agency examinations, or our own internal review process. Additions are also required when, in management's judgment, the reserve does not properly reflect the potential loss exposure.

For 2006, the bank added \$800,000 to the allowance for credit losses. The increase in 2006 is due in part to the increase in the volume of outstanding loans and our assessment of the overall adequacy of the allowance for credit losses after the first quarter charge off of one commercial relationship which resulted in a net charge off of \$348,000. For 2005, we added \$510,000 to the allowance for credit losses. The main reason for the provision in 2005 was two commercial loans that were charged off in the fourth quarter. The loans were to related borrowers whose business suffered a major event in the fourth quarter which affected their ability to continue their business. We made no additions to the allowance for credit losses in 2004, 2003 and 2002 due mainly to decreased levels of risk-rated loans and increased recoveries on previously charged-off loans.

15

---

Edgar Filing: CENTRAL VALLEY COMMUNITY BANCORP - Form 10-K

Using the criteria on the previous page, the allocation of the allowance for credit losses is set forth below:

(Dollars in thousands)	2006		2005		2004		2003		2002		Percent of Loans in Each Category to Total Loans
	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans	
Commercial and industrial	\$ 1,656	24.2	% \$ 1,325	27.5	% \$ 786	27.5	% \$ 717	28.8	% \$ 985	41.9	%
Real estate construction, land development and other land loans	294	15.0	% 378	15.4	% 197	16.9	% 249	13.6	% 85	13.8	%
Real estate - other	1,210	46.3	% 1,138	41.0	% 898	35.9	% 777	48.5	% 1,039	36.3	%
Equity lines of credit	171	6.8	% 175	7.8	% 136	8.9	%				
Loans to finance agricultural and other loans to farmers	227	5.3	% 198	5.8	% 151	7.6	% 540	5.8	% 159	2.5	%
Loans to individuals for household, family and other personal expenditures and other loans	193	2.3	% 120	2.5	% 178	3.1	% 85	2.3	% 58	3.0	%
Lease contracts							3	0.9	%	2.3	%
Other	1	0.1	% 1	0.0	% 51	0.1	% 47	0.2	% 40	0.2	%
Non-specific reserve	57		4		300		7		67		
	\$ 3,809		\$ 3,339		\$ 2,697		\$ 2,425		\$ 2,433		

Loans are charged to the allowance for credit losses when the loans are deemed uncollectible. It is the policy of management to make additions to the allowance so that it remains adequate to cover all probable loan charge-offs that exist in the portfolio at that time

**Table H****DEPOSITS**

We have no known foreign deposits. The following table sets forth the average amount of and the average rate paid on certain deposit categories which were in excess of 10% of average total deposits for the years ended December 31, 2006, 2005, and 2004.

(Dollars in thousands)	2006 Balance	Rate	2005 Balance	Rate	2004 Balance	Rate
Savings, money market and NOW accounts	\$ 184,042	1.43	% \$ 195,300	0.84	% \$ 151,277	0.51 %
Time certificates of deposit	\$ 98,118	3.65	% \$ 87,713	2.55	% \$ 58,966	1.72 %
Non-interest bearing demand	\$ 132,150	N/A	\$ 124,175	N/A	\$ 97,210	N/A
Total deposits	\$ 414,310		\$ 407,188		\$ 307,453	

**Table I****TIME DEPOSITS**

The following table sets forth the maturity of time certificates of deposit and other time deposits of \$100,000 or more at December 31, 2006.

(In Thousands)

Three months or less	\$ 26,332
Over 3 months through 6 months	22,283
Over 6 through 12 months	7,588
Over 12 months	3,980
	\$ 60,183

**Table J****FINANCIAL RATIOS**

The following table sets forth certain financial ratios for the years ended December 31, 2006, 2005, and 2004.

	2006	2005	2004	
Net Income:				
To average assets	1.47	% 1.33	% 1.07	%
To average shareholders equity	15.17	% 15.63	% 13.10	%
Dividends declared per share to net income per share	N/A	N/A	7.87	%
Average shareholders equity to average assets	9.69	% 8.49	% 8.15	%

## SUPERVISION AND REGULATION

### GENERAL

The banking and financial services businesses in which we engage are highly regulated. Such regulation is intended, among other things, to protect depositors whose deposits are insured by the FDIC and the banking system as a whole. The monetary and fiscal policies of the federal government and the policies of regulatory agencies, particularly the Board of Governors, also influence the commercial banking business. The Board of Governors implements national monetary policies (with objectives such as curbing inflation and combating recession) by its open-market operations in United States Government securities, by adjusting the required level of reserves for financial intermediaries subject to its reserve requirements and by varying the discount rates applicable to borrowings by depository institutions. The actions of the Board of Governors in these areas influence the growth of bank loans, investments and deposits and also affect interest rates charged on loans and paid on deposits. Indirectly such actions may also affect the ability of non-bank financial institutions to compete with the Bank. The nature and impact of any future changes in monetary policies cannot be predicted.

The laws, regulations, and policies affecting financial services businesses are continuously under review by Congress and state legislatures, and federal and state regulatory agencies. From time to time, legislation is enacted which has the effect of increasing the cost of doing business, limiting or expanding permissible activities or affecting the competitive balance between banks and other financial intermediaries. Proposals to change the laws and regulations governing the operations and taxation of banks, bank holding companies and other financial intermediaries are frequently made in Congress, in the California legislature and before various bank regulatory and other professional agencies. Changes in the laws, regulations or policies that affect us cannot necessarily be predicted, but they may have a material effect on our business and earnings.

### BANK HOLDING COMPANY REGULATION

The Company, as a bank holding company, is subject to regulation under the BHC Act, and is subject to the supervision and examination of the Board of Governors. Pursuant to the BHC Act, we are required to obtain the prior approval of the Board of Governors before we may acquire all or substantially all of the assets of any bank, or ownership or control of voting shares of any bank if, after giving effect to such acquisition, we would own or control, directly or indirectly, more than five percent of such bank.

Under the BHC Act, we may not engage in any business other than managing or controlling banks or furnishing services to our subsidiaries that the Board of Governors deems to be so closely related to banking as to be a proper incident to banking. We are also prohibited, with certain exceptions, from acquiring direct or indirect ownership or control of more than five percent of the voting shares of any company unless the company is engaged in banking activities or the Board of Governors determines that the activity is so closely related to banking to be a proper incident to banking. The Board of Governors' approval must be obtained before the shares of any such company can be acquired and, in certain cases, before any approved company can open new offices.

The BHC Act and regulations of the Board of Governors also impose certain constraints on the redemption or purchase by a bank holding company of its own shares of stock.

Our earnings and activities are affected by legislation, by actions of regulators, and by local legislative and administrative bodies and decisions of courts in the jurisdictions in which both the Company and the Bank conduct business. For example, these include limitations on the ability of the Bank to pay dividends to the Company and the ability of the Company to pay dividends to its shareholders. It is the policy of the Board of Governors that bank holding companies should pay cash dividends on common stock only out of income available over the past year and

only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividends that undermines the bank holding company's ability to serve as a source of strength to its banking subsidiaries. Various federal and state statutory provisions limit the amount of dividends that subsidiary banks can pay to their holding companies without regulatory approval. In addition to these explicit limitations, the federal regulatory agencies are authorized to prohibit a banking subsidiary or bank holding company from engaging in an unsafe or unsound banking practice. Depending upon the circumstances, the agencies could take the position that paying a dividend would constitute an unsafe or unsound banking practice.

In addition, banking subsidiaries of bank holding companies are subject to certain restrictions imposed by federal law in dealings with their holding companies and other affiliates. Subject to certain exceptions set forth in the Federal Reserve Act and the recently enacted Regulation W, a bank can make a loan or extend credit to an affiliate, purchase or invest in the securities of an affiliate, purchase assets from an affiliate, accept securities of an affiliate as collateral security for a loan or extension of credit to any person or company, issue a guarantee, or accept letters of credit on behalf of an affiliate only if the aggregate amount of the above transactions of such subsidiary does not exceed 10 percent of such subsidiary's capital stock and surplus on a per affiliate basis or 20 percent of such subsidiary's capital stock and surplus on an aggregate affiliate basis. Such transactions must be on terms and conditions that are consistent with safe and sound banking practices. A bank and its subsidiaries generally may not purchase a low-quality asset, as that term is defined in the Federal Reserve Act, from an affiliate. Such restrictions also generally prevent a holding company and its other affiliates from borrowing from a banking subsidiary of the holding company unless the loans are secured by collateral.

A holding company and its banking subsidiaries are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit, sale or lease of property or provision of services. For example, with certain exceptions a bank may not condition an extension of credit on a customer obtaining other services provided by it, a holding company or any of its other bank affiliates, or on a promise by the customer not to obtain other services from a competitor.

The Board of Governors has cease and desist powers over parent bank holding companies and non-banking subsidiaries where actions of a parent bank holding company or its non-financial institution subsidiaries represent an unsafe or unsound practice or violation of law. The Board of Governors has the authority to regulate debt obligations (other than commercial paper) issued by bank holding companies by imposing interest ceilings and reserve requirements on such debt obligations.

We are also a bank holding company within the meaning of Section 3700 of the California Financial Code. As such, we and our subsidiaries are subject to examination by the Department of Financial Institutions (DFI).

Further, we are required by the Board of Governors to maintain certain capital levels. See Capital Standards.

#### REGULATION OF THE BANK

Banks are extensively regulated under both federal and state law. The Bank, as a California state-chartered bank, is subject to primary supervision, regulation and periodic examination by the DFI and the FDIC. The Bank is not a member of the Federal Reserve System, but is nevertheless subject to certain regulations of the Board of Governors.

If, as a result of an examination of a bank, the FDIC should determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity, or other aspects of the Bank's operations are unsatisfactory or that the Bank or its management is violating or has violated any law or regulation, various remedies are available to the FDIC. Such remedies include the power to enjoin unsafe or unsound practices, to require affirmative action to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in capital, to restrict the growth of the Bank, to assess civil monetary penalties, to remove officers and directors, and ultimately to terminate the Bank's deposit insurance, which for a California chartered bank would result in a revocation of the Bank's charter. The DFI has many of the same remedial powers.

The Bank is a member of the FDIC, which currently insures customer deposits in each member bank to a maximum of \$100,000 per depositor. For this protection, the Bank is subject to the rules and regulations of the FDIC, and, as is the case with all insured banks, may be required to pay a semi-annual statutory assessment.

Various requirements and restrictions under the laws of the State of California and the United States affect the operations of the Bank. State and federal statutes and regulations relate to many aspects of the Bank's operations, including standards for safety and soundness, reserves against deposits, interest rates payable on deposits, loans, investments, mergers and acquisitions, borrowings, dividends, locations of branch offices, fair lending requirements, Community Reinvestment Act activities, and loans to affiliates.

#### PAYMENT OF DIVIDENDS

##### THE COMPANY

Our shareholders are entitled to receive dividends when and as declared by our Board of Directors, out of funds legally available, subject to the dividends preference, if any, on preferred shares that may be outstanding, and also subject to the restrictions of the California Corporations Code. At December 31, 2006, we had no outstanding shares of preferred stock.

The principal source of cash revenue to the Company is dividends received from the Bank. The Bank's ability to make dividend payments to the Company is subject to state and federal regulatory restrictions.

##### THE BANK

Dividends payable by the Bank to the Company are restricted under California law to the lesser of the Bank's retained earnings, or the Bank's net income for the latest three fiscal years, less dividends paid during that period, or, with the approval of the DFI, to the greater of the retained earnings of the Bank, the net income of the Bank for its last fiscal year or the net income of the Bank for its current fiscal year.

In addition to the regulations concerning minimum uniform capital adequacy requirements described below, the FDIC has established guidelines regarding the maintenance of an adequate allowance for credit losses. Therefore, the future payment of cash dividends by the Bank will generally depend, in addition to regulatory constraints, upon the Bank's earnings during any fiscal period, the assessment of the Board of Directors of the capital requirements of the Bank and other factors, including the maintenance of an adequate allowance for credit losses.

#### CAPITAL STANDARDS

The Board of Governors, the FDIC and other federal banking agencies have issued risk-based capital adequacy guidelines intended to provide a measure of capital adequacy that reflects the degree of risk associated with a banking organization's operations for both transactions reported on the balance sheet as assets, and transactions, such as letters of credit and recourse arrangements, which are reported as off-balance-sheet items. Under these guidelines, nominal dollar amounts of assets and credit equivalent amounts of off-balance-sheet items are multiplied by one of several risk adjustment percentages, which range from 0% for assets with low credit risk, such as certain U.S. government securities, to 100% for assets with relatively higher credit risk, such as business loans.

A banking organization's risk-based capital ratios are obtained by dividing its qualifying capital by its total risk-adjusted assets and off-balance-sheet items. The regulators measure risk-adjusted assets and off-balance-sheet items against both total qualifying capital (the sum of Tier 1 capital and limited amounts of Tier 2 capital) and Tier 1 capital. Tier 1 capital consists of common stock, retained earnings, noncumulative perpetual preferred stock and minority interests in certain subsidiaries, less most other intangible assets. Tier 2 capital may consist of a limited amount of the allowance for possible loan and lease losses and certain other instruments with some characteristics of equity. The inclusion of elements of Tier 2 capital is subject to certain other requirements and limitations of the



## Edgar Filing: CENTRAL VALLEY COMMUNITY BANCORP - Form 10-K

federal banking agencies. Since December 31, 1992, the federal banking agencies have required a minimum ratio of qualifying total capital to risk-adjusted assets and off-balance-sheet items of 8%, and a minimum ratio of Tier 1 capital to risk-adjusted assets and off-balance-sheet items of 4%.

In addition to the risk-based guidelines, federal banking regulators require banking organizations to maintain a minimum amount of Tier 1 capital to average total assets, referred to as the leverage ratio. For a banking organization rated in the highest of the five categories used by regulators to rate banking organizations, the minimum leverage ratio of Tier 1 capital to total assets is 3%. It is improbable, however, that an institution with a 3% leverage ratio would receive the highest rating by the regulators since a strong capital position is a significant part of the regulators' rating. For all banking organizations not rated in the highest category, the minimum leverage ratio is at least 100 to 200 basis points above the 3% minimum. Thus, the effective minimum leverage ratio, for all practical purposes, is at least 4% or 5%. In addition to these uniform risk-based capital guidelines and leverage ratios that apply across the industry, the regulators have the discretion to set individual minimum capital requirements for specific institutions at rates significantly above the minimum guidelines and ratios.

A bank that does not achieve and maintain the required capital levels may be issued a capital directive by the FDIC to ensure the maintenance of required capital levels. As discussed above, the Company and the Bank are required to maintain certain levels of capital. The regulatory capital guidelines as well as the actual capitalization for the Bank and the Company on a consolidated basis as of December 31, 2006 follow:

	REQUIREMENT		ACTUAL				
	ADEQUATELY CAPITALIZED		FOR THE BANK TO BE WELL CAPITALIZED	BANK		COMPANY	
<b>Total risk-based capital ratio</b>	8.00	%	10.00	% 11.77	%	12.02	%
<b>Tier 1 risk-based capital ratio</b>	4.00	%	6.00	% 10.72	%	10.97	%
<b>Tier 1 leverage capital ratio</b>	4.00	%	5.00	% 8.24	%	8.41	%

### USA PATRIOT ACT

In the wake of the tragic events of September 11th, on October 26, 2001, the President signed the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT) Act of 2001. The USA PATRIOT Act also made significant changes to the Bank Secrecy Act. Under the USA PATRIOT Act, financial institutions are subject to prohibitions against specified financial transactions and account relationships as well as enhanced due diligence and of identifying customers when establishing new relationships and standards in their dealings with foreign financial institutions and foreign customers. For example, the enhanced due diligence policies, procedures, and controls generally require financial institutions to take reasonable steps:

- To conduct enhanced scrutiny of account relationships to guard against money laundering and report any suspicious transaction;
- To ascertain the identity of the nominal and beneficial owners of, and the source of funds deposited into, each account as needed to guard against money laundering and report any suspicious transactions;
- To ascertain for any foreign bank, the shares of which are not publicly traded, the identity of the owners of the foreign bank, and the nature and extent of the ownership interest of each such owner; and
- To ascertain whether any foreign bank provides correspondent accounts to other foreign banks and, if so, the identity of those foreign banks and related due diligence information.

Under the USA PATRIOT Act, financial institutions are to establish anti-money laundering programs to enhance their Bank Secrecy Act program. The USA PATRIOT Act sets forth minimum standards for these programs, including:

- The development of internal policies, procedures, and controls;
- The designation of a compliance officer;
- An ongoing employee training program; and
- An independent audit function to test the programs.

Bank management believes that the Bank is currently in compliance with the Act.

#### FINANCIAL SERVICES MODERNIZATION LEGISLATION

On November 12, 1999, President Clinton signed into law the Gramm-Leach-Bliley Act, also known as the Financial Services Modernization Act. This legislation eliminated many of the barriers that have separated the insurance, securities and banking industries since the Great Depression. The federal banking agencies (the Board of Governors, FDIC and the Office of the Comptroller of the Currency) among others, continue to draft regulations to implement the Gramm-Leach-Bliley Act. The Gramm-Leach-Bliley Act is the result of a decade of debate in the Congress regarding a fundamental reformation of the nation's financial system. The law is subdivided into seven titles, by functional area.

The major provisions of the Gramm-Leach-Bliley Act are:

**FINANCIAL HOLDING COMPANIES AND FINANCIAL ACTIVITIES.** Title I establishes a comprehensive framework to permit affiliations among commercial banks, insurance companies, securities firms, and other financial service providers by revising and expanding the BHC Act framework to permit a holding company system to engage in a full range of financial activities through qualification as a new entity known as a financial holding company.

Final regulations adopted by the FDIC in January 2001, in the form of amendments to Part 362 of the FDIC rules and regulations, provide the framework for subsidiaries of state nonmember banks to engage in financial activities that the Gramm-Leach-Bliley Act permits national banks to conduct through a financial subsidiary.

Activities permissible for financial subsidiaries of national banks, and, pursuant to Section 362 of the FDIC rules and regulations, also permissible for financial subsidiaries of state nonmember banks, include, but are not limited to, the following: (a) Lending, exchanging, transferring, investing for others, or safeguarding money or securities; (b) Insuring, guaranteeing, or indemnifying against loss, harm, damage, illness, disability, or death, or providing and issuing annuities, and acting as principal, agent, or broker for purposes of the foregoing, in any State; (c) Providing financial, investment, or economic advisory services, including advising an investment company; (d) Issuing or selling instruments representing interests in pools of assets permissible for a bank to hold directly; and (e) Underwriting, dealing in, or making a market in securities.

**SECURITIES ACTIVITIES.** Title II narrows the exemptions from the securities laws previously enjoyed by banks and creates a new, voluntary investment bank holding company. The Board of Governors and the SEC continue to work together to draft rules governing certain securities activities of banks.

**INSURANCE ACTIVITIES.** Title III restates the proposition that the states are the functional regulators for all insurance activities, including the insurance activities of federally-chartered banks, and bars the states from prohibiting insurance activities by depository institutions.

PRIVACY. Under Title V, federal banking regulators were required to adopt rules that have limited the ability of banks and other financial institutions to disclose non-public information about consumers to nonaffiliated third parties. These limitations require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to a nonaffiliated third party. Federal banking regulators issued final rules on May 10, 2000 to implement the privacy provisions of Title V. Under the rules, financial institutions must provide:

- initial notices to customers about their privacy policies, describing the conditions under which they may disclose nonpublic personal information to nonaffiliated third parties and affiliates;
- annual notices of their privacy policies to current customers; and
- a reasonable method for customers to opt out of disclosures to nonaffiliated third parties.

Compliance with these rules was mandatory after July 1, 2001. The Company and the Bank were in full compliance with the rules as of or prior to their respective effective dates.

SAFEGUARDING CONFIDENTIAL CUSTOMER INFORMATION. Under Title V, federal banking regulators are required to adopt rules requiring financial institutions to implement a program to protect confidential customer information. In January 2000, the federal banking agencies adopted guidelines requiring financial institutions to establish an information security program.

The Bank implemented a security program appropriate to its size and complexity and the nature and scope of its operations prior to the July 1, 2001 effective date of the regulatory guidelines, and since initial implementation has, as necessary, updated and improved that program.

COMMUNITY REINVESTMENT ACT SUNSHINE REQUIREMENTS. The federal banking agencies have adopted final regulations implementing Section 711 of Title VII of the Gramm-Leach-Bliley Act, the Sunshine Requirements. The regulations require nongovernmental entities or persons and insured depository institutions and affiliates that are parties to written agreements made in connection with the fulfillment of the institution's CRA obligations to make available to the public and the federal banking agencies a copy of each agreement. Neither the Company nor the Bank is a party to any agreement that would be the subject of reporting pursuant to the CRA Sunshine Requirements.

The Company continues to evaluate the strategic opportunities presented by the broad powers granted to bank holding companies that elect to be treated as financial holding companies. In the event that the Company determines that access to the broader powers of a financial holding company is in the best interests of the Company, its shareholders and the Bank, the Company will file the appropriate election with the Board of Governors.

The Company and the Bank intend to comply with all provisions of the Gramm-Leach-Bliley Act and all implementing regulations as they become effective.

#### CONSUMER PROTECTION LAWS AND REGULATIONS

The bank regulatory agencies are focusing greater attention on compliance with consumer protection laws and their implementing regulations. Examination and enforcement have become more intense in nature, and insured institutions have been advised to monitor carefully compliance with such laws and regulations. The Bank is subject to many federal consumer protection statutes and regulations, some of which are discussed below.

The Community Reinvestment Act (CRA) is intended to encourage insured depository institutions, while operating safely and soundly, to help meet the credit needs of their communities. The CRA specifically directs the federal regulatory agencies, in examining insured depository institutions, to assess a bank's record of helping meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound banking practices. The CRA further requires the agencies to take a financial institution's record of meeting its community credit needs into account when evaluating applications for, among other things, domestic branches, mergers or acquisitions, or holding company formations. The agencies use the CRA assessment factors in order to provide a rating to the financial institution. The ratings range from a high of outstanding to a low of substantial noncompliance. The Bank was last examined for CRA compliance by its primary regulator, the FDIC, as of March 2001.



The Equal Credit Opportunity Act ( ECOA ) generally prohibits discrimination in any credit transaction, whether for consumer or business purposes, on the basis of race, color, religion, national origin, sex, marital status, age (except in limited circumstances), receipt of income from public assistance programs, or good faith exercise of any rights under the Consumer Credit Protection Act.

The Truth in Lending Act ( TILA ) is designed to ensure that credit terms are disclosed in a meaningful way so that consumers may compare credit terms more readily and knowledgeably. As a result of the TILA, all creditors must use the same credit terminology to express rates and payments, including the annual percentage rate, the finance charge, the amount financed, the total of payments and the payment schedule, among other things.

The Fair Housing Act ( FH Act ) regulates many practices, including making it unlawful for any lender to discriminate in its housing-related lending activities against any person because of race, color, religion, national origin, sex, handicap or familial status. A number of lending practices have been found by the courts to be, or may be considered, illegal under the FH Act, including some that are not specifically mentioned in the FH Act itself.

The Home Mortgage Disclosure Act ( HMDA ) grew out of public concern over credit shortages in certain urban neighborhoods and provides public information that will help show whether financial institutions are serving the housing credit needs of the neighborhoods and communities in which they are located. The HMDA also includes a fair lending aspect that requires the collection and disclosure of data about applicant and borrower characteristics as a way of identifying possible discriminatory lending patterns and enforcing anti-discrimination statutes.

Finally, the Real Estate Settlement Procedures Act ( RESPA ) requires lenders to provide borrowers with disclosures regarding the nature and cost of real estate settlements. Also, RESPA prohibits certain abusive practices, such as kickbacks, and places limitations on the amount of escrow accounts. Penalties under the above laws may include fines, reimbursements and other penalties.

Due to heightened regulatory concern related to compliance with the CRA, TILA, FH Act, ECOA, HMDA and RESPA generally, the Bank may incur additional compliance costs or be required to expend additional funds for investments in its local community.

#### CALIFORNIA FINANCIAL INFORMATION PRIVACY ACT/FAIR CREDIT REPORTING ACT

In 1970, the federal Fair Credit Reporting Act (the FCRA ) was enacted to insure the confidentiality, accuracy, relevancy and proper utilization of consumer credit report information. Under the framework of the FCRA, the United States has developed a highly advanced and efficient credit reporting system. The information contained in that broad system is used by financial institutions, retailers and other creditors of every size in making a wide variety of decisions regarding financial transactions. Employers and law enforcement agencies have also made wide use of the information collected and maintained in databases made possible by the FCRA. The FCRA affirmatively preempts state law in a number of areas, including the ability of entities affiliated by common ownership to share and exchange information freely, and the requirements on credit bureaus to reinvestigate the contents of reports in response to consumer complaints, among others.

The California Financial Information Privacy Act, which was enacted in 2003, requires a financial institution to provide specific information to a consumer related to the sharing of that consumer's nonpublic personal information. The Act allows a consumer to direct the financial institution not to share his or her nonpublic personal information with affiliated or nonaffiliated companies with which a financial institution has contracted to provide financial products and services, and requires that permission from each such consumer be acquired by a financial institution prior to sharing such information.

The FACT Act, (Fair and Accurate Credit Transaction Act) became law in 2003, effectively extending and amending provisions of the Fair Credit Reporting Act (FCRA). The FACT Act created many new responsibilities for consumer reporting agencies and users of consumer reports. It contains many new consumer disclosure requirements as well as provisions to address identity theft.

## CHECK 21 ACT

On December 22, 2003, the Board of Governors amended Regulation CC and its commentary to implement the Check Clearing for the 21st Century Act (Check 21 Act). The Check 21 Act became effective on October 28, 2004.

To facilitate check truncation and electronic check exchange, the Check 21 Act authorizes a new negotiable instrument called a substitute check and provides that a properly prepared substitute check is the legal equivalent of the original check for all purposes. A substitute check is a paper reproduction of the original check that can be processed just like the original check. The Check 21 Act does not require any bank to create substitute checks or to accept checks electronically. The amendments: 1) set forth the requirements of the Check 21 Act that apply to banks; 2) provide a model disclosure and model notices relating to substitute checks; and 3) set forth bank endorsement and identification requirements for substitute checks.

The Bank has been imaging its customers' checks since 2000. Check 21 Act has had limited impact on the Bank.

## Recent Accounting Pronouncements

### *Fair Value Measurements*

In September 2006, the FASB issued Statement No. 157 (SFAS 157), *Fair Value Measurements*. SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS 157 applies whenever other standards require (or permit) assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances. In this standard, the FASB clarifies the principle that fair value should be based on the assumptions market participants would use when pricing the asset or liability. In support of this principle, SFAS 157 establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. The provisions of SFAS 157 are effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The provisions should be applied prospectively, except for certain specifically identified financial instruments. Management does not expect the adoption of SFAS 157 to have a material impact to the Bank's financial position or result of operations.

### *Accounting for Uncertainty in Income Taxes*

In July 2006, the FASB issued Financial Accounting Standards Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109*. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement standard for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosures and transition.

The Company presently recognizes income tax positions based on management's estimate of whether it is reasonably possible that a liability has been incurred for unrecognized income tax benefits by applying FASB Statement No. 5, *Accounting for Contingencies*.

The provisions of FIN 48 will be effective for the Company on January 1, 2007 and are to be applied to all tax positions upon initial application of this standard. Only tax positions that meet the more-likely-than-not recognition threshold at the effective date may be recognized or continue to be recognized upon adoption.

The cumulative effect of applying the provisions of FIN 48, if any, will be reported as an adjustment to the opening balance of retained earnings for the fiscal year of adoption. Management does not expect the adoption of FIN 48 to have a material impact on the Company's financial position or results of operations.

*Accounting for Purchases of Life Insurance*

In September 2006, the FASB ratified the consensuses reached by the Emerging Issues Task Force (the Task Force) on Issue No. 06-5 (EITF 06-5), *Accounting for the Purchases of Life Insurance - Determining the Amount that Could be Realized in Accordance with FASB Technical Bulletin No.85-4 (FTB 85-4)*. FTB 85-4 indicates that the amount of the asset included in the balance sheet for life insurance contracts within its scope should be the amount that could be realized under the insurance contract as of the date of the statement of financial position. Questions arose in applying the guidance in FTB 85-4 to whether the amount that could be realized should consider 1) any additional amounts included in the contractual terms of the insurance policy other than the cash surrender value and 2) the contractual ability to surrender all of the individual-life policies (or certificates in a group policy) at the same time. EITF 06-5 determined that the amount that could be realized should 1) consider any additional amounts included in the contractual terms of the policy and 2) assume the surrender of an individual-life by individual-life policy (or certificate by certificate in a group policy). Any amount that is ultimately realized by the policy holder upon the assumed surrender of the final policy (or final certificate in a group policy) shall be included in the amount that could be realized. An entity should apply the provisions of EITF 06-5 through either a change in accounting principle through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption or a change in accounting principle through retrospective application to all prior periods. The provisions of EITF 06-5 are effective for fiscal years beginning after December 15, 2006. Management has not yet completed its evaluation of the impact that EITF 06-5 will have.

*Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*

In September 2006, the FASB ratified the consensuses reached by the Task Force on Issue No. 06-4 (EITF 06-4), *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. A question arose when an employer enters into an endorsement split-dollar life insurance arrangement related to whether the employer should recognize a liability for the future benefits or premiums to be provided to the employee. EITF 06-4 indicates that an employer should recognize a liability for future benefits and that a liability for the benefit obligation has not been settled through the purchase of an endorsement type policy. An entity should apply the provisions of EITF 06-4 either through a change in accounting principle through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption or a change in accounting principle through retrospective application to all prior periods. The provisions of EITF 06-4 are effective for fiscal years beginning after December 15, 2007. Management has not yet completed its evaluation of the impact that EITF 06-4 will have.

*Consideration of the Effects of Prior Year Misstatements*

In September, 2006, the Securities and Exchange Commission published Staff Accounting Bulletin ( SAB ) No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements*. The interpretations in this Staff Accounting Bulletin was issued to address diversity in practice in quantifying financial statement misstatements and the potential under current practice to build up improper amounts on the balance sheet. This guidance will apply to the first fiscal year ending after November 15, 2006 or December 31, 2006 for the Company. The adoption of SAB 108 did not have a material impact on the Company's financial position or results of operations and no cumulative adjustment was required.

**Other**

Other legislation which has been or may be proposed to the United States Congress and the California Legislature and regulations which may be proposed by the Board of Governors, FDIC and the DFI may affect our business. It cannot be predicted whether any pending or proposed legislation or regulations will be adopted or the effect such legislation or regulations may have upon our business.

**ITEM 1A - RISK FACTORS**

**Risks, Uncertainties and Other Factors That May Affect Our Future Results**

*Our profitability depends significantly on economic conditions.*

Our success depends primarily on the general economic conditions of the Central Valley and California. Unlike larger banks that are more geographically diversified, we provide banking and financial services to customers primarily in the market areas in which we operate. The local economic conditions of these areas have a significant impact on our commercial, real estate and construction loans, the ability of the borrowers to repay these loans and the value of the collateral securing these loans. A significant decline in general economic conditions, such as inflation, recession, acts of terrorism, an outbreak of hostilities, unemployment and other factors beyond our control will impact these local economic conditions and will negatively affect the financial results of our banking operations. In addition, the Central Valley remains largely dependent on agriculture. A downturn in agriculture and agricultural related business could indirectly and adversely affect our results of operations and financial condition.

*We rely on the small to medium sized business market.*

Our business development and marketing strategy primarily targets the banking and financial needs of small to medium sized businesses with non-complex credit needs. These businesses are diverse and not dependent upon one industry and represent a major sector of the Central Valley economies. If general economic conditions negatively impact this economic sector in the Central Valley in which we operate, our results of operations and financial condition will be significantly affected.

*If our allowance for credit losses is not sufficient to cover actual loan losses, our earnings could decrease.*

Our loan customers may not repay their loans according to the terms of these loans, and the collateral securing the payment of these loans may be insufficient to assure repayment. We may experience significant credit losses that could have a material adverse effect on our operating results. We make various assumptions and judgments about the collectibility of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of our loans. In determining the size of the allowance, we rely on our experience and our evaluation of economic conditions. If our assumptions prove to be incorrect, our current allowance may not be sufficient to cover future loan losses and adjustments may be necessary to allow for different economic conditions or adverse developments in our loan portfolio. Significant additions to our allowance would materially decrease our net income.

In addition, federal and state regulators periodically review our allowance for credit losses and may require us to increase our provision for credit losses or recognize further loan charge-offs, based on judgments different than those we make. Any increase in our allowance or charge-offs as required by these regulatory agencies could have a negative affect on us.

*Fluctuations in interest rates could reduce our profitability.*

We realize income primarily from the difference between interest earned on loans and securities and the interest paid on deposits and borrowings. We expect that we will periodically experience gaps in the interest rate sensitivities of our assets and liabilities, meaning that either our interest-bearing liabilities will be more sensitive to changes in market interest rates than our interest-earning assets, or vice versa. In either event, if market interest rates should move contrary to our position, this gap will work against us, and our earnings may be negatively affected.

We are unable to predict fluctuations of market interest rates, which are affected by the following factors:

- inflation;
- recession;
- a rise in unemployment;
- tightening money supply;
- international disorder; and



- instability in domestic and foreign financial markets.

Our asset/liability management strategy, which is designed to address the risk from changes in market interest rates and the shape of the yield curve, may not prevent changes in interest rates from having a material adverse effect on our results of operations and financial condition.

27

---

***Competition with other financial institutions could adversely affect our profitability.***

We face vigorous competition from banks and other financial institutions, including savings institutions, finance companies and credit unions. A number of these banks and other financial institutions have substantially greater resources and lending limits, larger branch systems and a wider array of banking services. To a limited extent, we also compete with other providers of financial services, such as money market mutual funds, brokerage firms, consumer finance companies and insurance companies. This competition may reduce or limit our margins on banking services, reduce our market share and adversely affect our results of operations and financial condition. Additionally, we face competition primarily from other banks in attracting, developing and retaining qualified banking professionals.

***We may not be able to maintain our historical growth rate which may adversely impact our results of operations and financial condition.***

We have initiated internal growth programs, completed various acquisitions and opened additional offices in the past few years. We may not be able to sustain our historical rate of growth or may not even be able to grow at all. We may not be able to obtain the financing necessary to fund additional growth and may not be able to find suitable candidates for acquisition. Various factors, such as economic conditions and competition, may impede or prohibit the opening of new branch offices. Further, our inability to attract and retain experienced bankers may adversely affect our internal growth. A significant decrease in our historical rate of growth may adversely impact our results of operations and financial condition.

***We may be unable to complete acquisitions, and once complete, may not be able to integrate our acquisitions successfully.***

Our growth strategy includes our desire to acquire other financial institutions. We may not be able to complete any future acquisitions and, if completed, we may not be able to successfully integrate the operations, management, products and services of the entities we acquire. We may not realize expected cost savings or make revenue enhancements. Following each acquisition, we must expend substantial managerial, operating, financial and other resources to integrate these entities. In particular, we may be required to install and standardize adequate operational and control systems, deploy or modify equipment, implement marketing efforts in new as well as existing locations and employ and maintain qualified personnel. Our failure to successfully integrate the entities we acquire into our existing operations may adversely affect our financial condition and results of operations.

***We operate in a highly regulated environment and may be adversely affected by changes in federal and local laws and regulations.***

We are subject to extensive regulation, supervision and examination by federal and state banking authorities. Any change in applicable regulations or federal or state legislation could have a substantial impact on us and our operations. Additional legislation and regulations may be enacted or adopted in the future that could significantly affect our powers, authority and operations, which could have a material adverse effect on our financial condition and results of operations. Further, regulators have significant discretion and power to prevent or remedy unsafe or unsound practices or violations of laws by banks and bank holding companies in the performance of their supervisory and enforcement duties. The exercise of this regulatory discretion and power may have a negative impact on us.

***We are experiencing an influx of locally based competition that could affect near term results.***

Recently, several new banks have opened in our service areas. We are seeing price competition from these new banks, as they work to establish their markets. The existence of competitors, large and small, is a normal and expected part of our operations, but in responding to the particular short-term impact on business of new entrants to the marketplace, we could see a negative impact on revenue and income. Moreover, these near term impacts could be accentuated by the seasonal impact on revenue and income generated by the borrowing and deposit habits of the agricultural community that comprises a significant component of our customer base.

**ITEM 2 - DESCRIPTION OF PROPERTY.**

The Company owns the property on which the Main Office, a full-service branch office, is located in Clovis, California. In addition, the Company owns the property on which the Foothill Office, a full-service branch office, is located in Prather, California, and the property on which the Kerman Office, a full-service branch office, is located in Kerman, California.

All other property is leased by the Company, including the principal executive offices in Fresno. This facility houses the Company's corporate offices, comprised of various departments, including accounting, information services, human resources, real estate department, loan servicing, credit administration, SBA department, branch support operations, and compliance.

The Company continually evaluates the suitability and adequacy of the Company's offices and has a program of relocating or remodeling them as necessary to be efficient and attractive facilities. Management believes that its existing facilities are adequate for its present purposes.

Properties owned by the Bank are held without loans or encumbrances. All of the property leased is leased directly from independent parties. Management considers the terms and conditions of each of the existing leases to be in the aggregate favorable to the Company.

**ITEM 3 - LEGAL PROCEEDINGS.**

Neither the Company nor the Bank is a party to, nor are any of their properties the subject of, any material pending legal proceedings other than ordinary, routine litigation incidental to the Company's and the Bank's businesses, nor are any of such proceedings known to be contemplated by government authority.

None of our directors, officers, affiliates, more than 5% shareholder or any associates of these persons is a party adverse to the Company or the Bank or has a material interest adverse to the Company or the Bank in any material legal proceeding.

**ITEM 4 - SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.**

No matters were submitted to our shareholders during the fourth quarter of the year ended December 31, 2006.

**PART II**

**ITEM 5 - MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.**

Our common stock is listed for trading on the Nasdaq Capital Market under the ticket symbol CVCY. As of February 28, 2007, we had approximately 385 shareholders of record.

The following table shows the high and low sales prices for the common stock for each quarter as reported by NASDAQ. The prices have been adjusted to reflect a two-for-one stock split on October 31, 2005.

## Common Stock Prices

	Qtr 1 2006	Qtr 2 2006	Qtr 3 2006	Qtr 4 2006	Qtr 1 2005	Qtr 2 2005	Qtr 3 2005	Qtr 4 2005
High	\$ 19.25	\$ 16.69	\$ 16.74	\$ 15.64	\$ 13.13	\$ 16.36	\$ 14.98	\$ 16.00
Low	\$ 14.11	\$ 14.75	\$ 14.50	\$ 14.50	\$ 11.25	\$ 11.06	\$ 11.00	\$ 13.95

On October 31, 2005, we effected a two-for-one stock split. We paid \$0.05 per share cash dividends in 2004. As a result of the borrowing from a major bank, during the time the borrowing remains outstanding, which is expected to be until December 2007, we do not anticipate paying dividends to our shareholders. The Bank does not anticipate paying any dividends to the Company except for dividends that are necessary to meet the ordinary and usual operating expenses of the Company provided that the Bank would not pay any dividend that would cause it to be deemed not well capitalized under applicable banking laws and regulations. See Note 7 in the audited Consolidated Financial Statements in Item 8 of this Annual Report.

## ISSUER PURCHASES OF EQUITY SECURITIES

A summary of the repurchase activity for the Company's year ending December 31, 2006 follows.

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan (1)	Approximate Dollar Value of Shares that May Yet Be Purchased Under Current Plan
10/01/2006 - 10/31/2006				\$ 1,000,000
11/01/2006 - 11/30/2006	20,000	\$ 15.07	20,000	\$ 698,600
12/01/2006 - 12/31/2006	6,200	\$ 15.10	6,200	\$ 605,000
Total	26,200	\$ 15.08	26,200	

- (1) The Company approved a stock repurchase program effective October 23, 2006 and ending June 30, 2007 with the intent to purchase shares for an aggregate amount of \$1,000,000. For the year ended December 31, 2006, the Company repurchased 26,200 shares at a cost of \$395,000.
- (2) All share repurchases were effected in accordance with the safe harbor provisions of Rule 10b-18 of the Securities Exchange Act.

## Equity Compensation Plan Information

The following chart sets forth information for the year ended December 31, 2006, regarding equity based compensation plans of the Company.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders	899,834	\$ 6.45	549,446
Equity compensation plans not approved by security holders	N/A	N/A	N/A
Total	899,834	\$ 6.45	549,446



**PERFORMANCE GRAPH**

Source : SNL Financial LC, Charlottesville, VA © 2007

31

---

## ITEM 6 SELECTED CONSOLIDATED FINANCIAL DATA

Statements of Income	Years Ended December 31, (in thousands, except per share amounts)				
	2006	2005	2004	2003	2002
Total interest income	\$ 30,932	\$ 26,070	\$ 16,799	\$ 14,970	\$ 14,536
Total interest expense	6,559	4,139	1,978	2,290	2,728
Net interest income before provision for credit losses	24,373	21,931	14,821	12,680	11,808
Provision for credit losses	800	510			
Net interest income after provision for credit losses	23,573	21,421	14,821	12,680	11,808
Non-interest income	5,177	3,760	3,937	4,546	4,212
	28,750	25,181	18,758	17,226	16,020
Non-interest expense	18,541	15,793	13,119	12,355	11,988
Income before provision for income taxes	10,209	9,388	5,639	4,871	4,032
Provision for income taxes	3,298	3,344	1,944	1,499	1,248
Net income	\$ 6,911	\$ 6,044	\$ 3,695	\$ 3,372	\$ 2,784
Basic earnings per share	\$ 1.16	\$ 1.03	\$ 0.71	\$ 0.65	\$ 0.54
Diluted earnings per share	\$ 1.07	\$ 0.94	\$ 0.64	\$ 0.60	\$ 0.51
Cash dividends declared per common share	\$ 0.00	\$ 0.00	\$ 0.05	\$ 0.05	\$ 0.03

	December 31, (in thousands)				
	2006	2005	2004	2003	2002
<b>Balances at end of year:</b>					
Investment securities, Federal funds sold and deposits in other banks	\$ 128,463	\$ 136,340	\$ 127,895	\$ 107,300	\$ 95,901
Net loans	318,853	298,463	206,582	183,849	156,293
Total deposits	440,627	430,989	326,186	290,565	246,337
Total assets	500,059	483,677	368,147	327,930	283,006
Shareholders' equity	49,778	41,523	29,606	26,720	24,099
Earning assets	453,211	440,646	338,032	292,494	251,895
<b>Average balances:</b>					
Investment securities, Federal funds sold and deposits in other banks	\$ 125,702	\$ 135,679	\$ 115,069	\$ 101,222	\$ 74,111
Net loans	300,591	274,348	192,658	172,310	146,264
Total deposits	414,310	407,188	307,453	270,159	212,629
Total assets	470,221	455,680	346,217	306,384	248,948
Shareholders' equity	45,564	38,691	28,203	25,484	22,604
Earning assets	431,368	414,257	311,456	275,846	222,067

Data from 2005 forward reflects the impact of the merger with Bank of Madera County.

**ITEM 7- MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.**

Management's discussion and analysis should be read in conjunction with the Company's audited Consolidated Financial Statements, including the Notes thereto, in Item 8 of this Annual Report.

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 (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 Annual Report the words anticipate, estimate, expect, project, intend, commit, believe 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 Annual Report. 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 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.

**INTRODUCTION:**

Central Valley Community Bancorp (NASDAQ: CVCY) (the Company) was incorporated on February 7, 2000. The formation of the holding company offered the Company more flexibility in meeting the long-term needs of customers, shareholders, and the communities it serves. The Company currently has one bank subsidiary, Central Valley Community Bank (the Bank). The Company's market area includes the central valley area from Sacramento, California to Bakersfield, California.

After the close of business on December 31, 2004, the Company completed the merger with Bank of Madera County (BMC). The Madera and Oakhurst branches of BMC were merged into the Bank. For details of the merger, refer to Note 2 to the Company's audited Consolidated Financial Statements in Item 8 of the Annual Report.

During 2006, the Company focused on assuring competitive products and services to our clients were made available while adjusting to the many new laws and regulations that affect the banking industry. The Bank opened full service retail offices in the Fresno downtown area on February 13, 2006 and in the Sunnyside area of Fresno on November 13, 2006. During October 2006, the Company consolidated its administrative offices into a single location on Financial Drive in Fresno and opened a limited service branch there, bringing the total number of branches to 12.



## **ECONOMIC CONDITIONS**

Fresno County's economy has been relatively stable for the past three to four years, but during 2006, the local economy has shown signs of slowing. Most industries in the County are either stable or contracting very modestly. Fresno County's unemployment rate has historically been one of the highest rates in California and the nation; however in the fourth quarter of 2006, the County reported the lowest single digit rate in 27 years. Agriculture and agricultural related businesses remain a critical part of the County's economy. The County's agricultural production is widely diversified, producing cotton, nuts, vegetables, fruit, cattle, and dairy products. Due to low land costs, relative to the rest of the state, Fresno's economy has been significantly affected by the real estate construction segment in the past five years. However, during 2006, growth in the residential housing market stagnated as housing starts and appreciation in median home prices decreased compared to 2005.

Fresno County also offers lower living costs compared with metropolitan areas to the North and South of the County. Fresno County's home appreciation has averaged 20% annually over the four year period prior to 2006. In 2006 home appreciation was approximately 3%. While affordability has declined as a result, the area is still considered more affordable than other places in California.

## **STOCK SPLIT**

On September 21, 2005 the Company's Board of Directors approved a two-for-one stock split for shareholders of record at the close of business on October 5, 2005 and effective on October 31, 2005. All share and per share data in the consolidated financial statements and the following management's discussion and analysis have been retroactively restated to give effect to the stock split.

## **OVERVIEW**

We are pleased to report continued growth in consolidated earnings and total assets during 2006. Diluted earnings per share (EPS) for the year ended December 31, 2006 was \$1.07 compared to \$0.94 and \$0.64 for years ended December 31, 2005 and 2004, respectively. Net income for 2006 was \$6,911,000 compared to \$6,044,000 and \$3,695,000 for the years ended December 31, 2005 and 2004, respectively. Total assets at December 31, 2006 were \$500,059,000 compared to \$483,677,000 at December 31, 2005.

Return on average equity for 2006 was 15.17% compared to 15.63% and 13.10% for 2005 and 2004, respectively. Return on average assets for 2006 was 1.47% compared to 1.33% and 1.07% for 2005 and 2004, respectively. Total equity was \$49,778,000 at December 31, 2006 compared to \$41,523,000 at December 31, 2005.

Total loans continued to grow during 2006. Average total loans increased \$26,219,000 or 9.44% in 2006 compared to 2005. Asset quality continues to be strong. In 2006, we recorded a provision for credit losses of \$800,000 compared to \$510,000 for 2005 and none in 2004. The Company had no non-accrual loans at December 31, 2006 compared to two non-accrual loans totaling \$616,000 at December 31, 2005. Net charge-offs for 2006 were \$330,000 compared to \$619,000 for 2005 and net recoveries of \$272,000 for 2004. Refer to Asset Quality below for further information. We had no other real estate owned at either December 31, 2006 or 2005.

## **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; and
- Operating efficiency.



*Return to Our Stockholders.*

## Edgar Filing: CENTRAL VALLEY COMMUNITY BANCORP - Form 10-K

Our return to our stockholders is measured in the form of return on average equity ( ROE ). Our net income for the year ended December 31, 2006 increased \$867,000 compared to increases of \$2,349,000 and \$323,000 for 2005 and 2004, respectively. Net income increased mainly due to an increase in net interest income provided by the increase in interest rates and the additional loan volume from the 2005 BMC merger and our own organic growth, and increases in non-interest income. This increase was partially offset by an increase in interest expenses, addition to the provision for credit losses, and operating expenses. Basic EPS increased to \$1.16 for 2006 compared to \$1.03 and \$0.71 for years ended 2005 and 2004, respectively. Diluted EPS increased to \$1.07 for the year ended 2006 compared to \$0.94 and \$0.64 for years ended 2005 and 2004, respectively. The increase in EPS was due primarily to the increase in net income, partially offset by the increase in average shares outstanding as a result of the merger and the exercise of stock options. Our ROE was 15.17% for the year ended 2006 compared to 15.63% and 13.10% for the years ended 2005 and 2004, respectively. The decrease in ROE for 2006 is primarily due to the increase in capital from the exercise of stock options and current year earnings.

### *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 ROA for the year ended 2006 increased to 1.47% compared to 1.33% and 1.07% for the years ended December 31, 2005 and 2004, respectively. The 2006 increase in ROA is due to the increase in net income relative to our increase in average assets. ROA for our peer group was 1.11% at September 30, 2006. Peer group information from SNL Financial data includes all bank holding companies in California with assets from \$300M to \$500M and not subchapter S.

### *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 the 2005 merger, loan generation and retention and improved net interest margin by focusing on core deposit growth and managing the cost of funds. As a result, our net interest income before provision for credit losses increased \$2,442,000 or 11.13% to \$24,373,000 for the year ended 2006 compared to \$21,931,000 and \$14,821,000 for the years ended 2005 and 2004, respectively. Our net interest margin also improved 33 basis points to 5.79% for the year ended 2006 compared to 5.46% and 4.91% for the years ended 2005 and 2004, respectively.

Our non-interest income is generally made up of service charges and fees on deposit accounts, fee income from loan placements, and gain on sale from investment securities. Non-interest income in 2006 increased \$1,168,000 or 29.13% to \$5,177,000 compared to \$4,009,000 and \$4,084,000 in 2005 and 2004, respectively. Customer service charges increased slightly to \$2,532,000 in 2006 compared to \$2,414,000 and \$2,340,000 in 2005 and 2004, respectively, mainly due to an increase in the number of transaction accounts. Non-interest income in 2006 also included tax-exempt proceeds from a life insurance policy of \$625,000, gains from the sale of real estate of \$265,000, realized gains from the sale of investments of \$123,000 and loan placement fees of \$350,000. During 2005, non-interest income included gains from the sale of investments of \$92,000 compared to \$483,000 in 2004 and loan placement fees of \$390,000 in 2005 compared to \$330,000 for 2004. Further detail on non-interest income is provided below.

### *Asset Quality*

For all banks and bank holding companies, asset quality has a significant impact on the overall financial condition and results of operations. Asset quality is measured in terms of percentage of total loans and total assets, and is a key element in estimating the future earnings of a company. We had no non-performing loans as of December 31, 2006, compared to two non-accrual loans totaling \$616,000 as of December 31, 2005. Management maintains certain loans that have been brought current by the borrower (less than 30 days delinquent) on non-accrual status until such time as management has determined that the loans are likely to remain current in future periods. There were no non-performing loans at December 31, 2006 and 0.20% of gross loans were non-performing at December 31, 2005. The Company did not have any other real estate owned at December 31, 2006 or 2005.

*Asset Growth*

As revenues from both net interest income and non-interest income are a function of asset size, the continued growth in assets has a direct impact in increasing net income and therefore ROE and ROA. The majority of our assets are loans and investment securities, and the majority of our liabilities are deposits, and therefore the ability to generate deposits as a funding source for loans and investments is fundamental to our asset growth. Total assets increased 3.39% during 2006 to \$500,059,000 as of December 31, 2006 from \$483,677,000 as of December 31, 2005. Total gross loans increased 6.91% to \$322,662,000 as of December 31, 2006, compared to \$301,802,000 at December 31, 2005. Total investment securities decreased 1.58% to \$103,922,000 as of December 31, 2006 compared to \$105,592,000 as loan growth exceeded deposit growth. Total deposits increased 2.24% to \$440,627,000 as of December 31, 2006 compared to \$430,989,000 as of December 31, 2005. We continue to under perform in our loan to deposit ratio compared to our peers. Our loan to deposit ratio at December 31, 2006 was 73.2% compared to 70.0% at December 31, 2005. The loan to deposit ratio of our peers was 92.61% at September 30, 2006.

*Operating Efficiency*

Operating efficiency is the measure of how efficiently earnings before taxes are generated as a percentage of revenue. The Company's efficiency ratio (non-interest expenses, excluding amortization of intangibles divided by net interest income plus non-interest income, excluding gain from sale of securities) deteriorated slightly to 62.28% for 2006 compared to 61.20% for 2005 and 72.00% for 2004. The deterioration in the efficiency ratio in 2006 is due to the increase in operating expenses exceeding the increase in revenues. The Company's net interest income before provision for credit losses plus non-interest income increased 13.84% to \$29,427,000 in 2006 compared to \$25,848,000 in 2005 and \$18,426,000 in 2004, while operating expenses increased 15.85% in 2006, 19.25% in 2005, and 7.37% in 2004. The increase in operating expenses in 2006 can be partially attributed to the opening of two new full service branches and the relocation of our administrative offices, including a limited service branch.

**RESULTS OF OPERATIONS**

**Net Income:**

## Edgar Filing: CENTRAL VALLEY COMMUNITY BANCORP - Form 10-K

Net income increased to \$6,911,000 in 2006 compared to \$6,044,000 and \$3,695,000 in 2005 and 2004, respectively. Basic earnings per share were \$1.16, \$1.03, and \$0.71 for 2006, 2005 and 2004, respectively. Diluted earnings per share were \$1.07, \$0.94, and \$0.64 for 2006, 2005 and 2004, respectively. ROE was 15.17% for 2006 compared to 15.63% for 2005 and 13.10% for 2004. ROA for 2006 was 1.47% compared to 1.33% for 2005 and 1.07% for 2004.

The increase in net income and profitability for 2006 compared to 2005 was mainly due to the increases in net interest income and non-interest income and was partially offset by increases in the provision for credit losses and non-interest expenses. Net interest income increased due to an increase in average interest earning assets provided by our organic growth, the 2005 merger and the positive effect of our asset sensitive position expanding our net interest margin in response to the 17 increases in the Federal funds interest rate since June 30, 2004. Non interest-income in 2006 included tax-exempt proceeds from a life insurance policy, gains from the sale of real estate, and realized gains from the sale of investments. Non-interest expenses increased in 2006 primarily due to salaries and benefits, and equipment and occupancy expenses that were all affected by our continued organic expansion and the 2005 merger.

### **Interest Income and Expense**

Net interest income is the most significant component of our income from operations. Net interest income (the interest rate spread) is the difference between the gross interest and fees earned on the loan and investment portfolios and the interest paid on deposits and other borrowings. Net interest income depends on the volume of and interest rate earned on interest earning assets and the volume of and interest rate paid on interest bearing liabilities.

The following table sets forth a summary of average balances with corresponding interest income and interest expense as well as average yield and cost information for the periods presented. Average balances are derived from daily balances, and non-accrual loans are not included as interest earning assets for purposes of this table.

36

---

## CENTRAL VALLEY COMMUNITY BANCORP

## SCHEDULE OF AVERAGE BALANCES AND AVERAGE YIELDS AND RATES

(Dollars in thousands)

(Unaudited)	FOR THE YEAR ENDED DECEMBER 31, 2006			FOR THE YEAR ENDED DECEMBER 31, 2005		
	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate
<b>ASSETS</b>						
Interest-earning deposits in other banks	\$ 634	\$ 22	3.47	% \$ 2,136	\$ 59	2.76 %
Securities						
Taxable securities	74,915	3,191	4.26	% 86,857	3,002	3.46 %
Non-taxable securities (1)	26,749	1,556	5.82	% 25,096	1,806	7.20 %
Total investment securities	101,664	4,747	4.67	% 111,953	4,808	4.29 %
Federal funds sold	23,404	1,165	4.98	% 21,590	702	3.25 %
Total	125,702	5,934	4.72	% 135,679	5,569	4.10 %
Loans (2) (3)	303,867	25,527	8.40	% 276,957	21,115	7.63 %
Federal Home Loan Bank stock	1,799	89	4.95	% 1,621	68	4.19 %
<b>Total interest-earning assets</b>	<b>431,368</b>	<b>\$ 31,550</b>	<b>7.31</b>	<b>% 414,257</b>	<b>\$ 26,752</b>	<b>6.46 %</b>
Allowance for credit losses	(3,483)					