

TRICO BANCSHARES /
Form 10-K
March 18, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2012

Commission File Number 0-10661

TriCo Bancshares

(Exact name of Registrant as specified in its charter)

California
(State or other jurisdiction of
incorporation or organization)

94-2792841
(I.R.S. Employer
Identification No.)

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63 Constitution Drive, Chico, California

(Address of principal executive offices)

95973

(Zip Code)

Registrant's telephone number, including area code: (530) 898-0300

Securities registered pursuant to Section 12(b) of the Act:

Common Stock, without par value

(Title of Class)

Nasdaq Stock Market LLC

(Name of each exchange on
which registered)

Securities registered pursuant to Section 12(g) of the Act: None.

Indicate by check mark whether the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES NO

Indicate by check mark whether the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the 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 periods 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 whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES 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 the Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of the Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES NO

The aggregate market value of the voting common stock held by non-affiliates of the Registrant, as of June 30, 2012, was approximately \$187,758,000 (based on the closing sales price of the Registrant's common stock on the date). This computation excludes a total of 3,800,792 shares that are beneficially owned by the officers and directors of Registrant who may be deemed to be the affiliates of Registrant under applicable rules of the Securities and Exchange Commission.

The number of shares outstanding of Registrant's common stock, as of March 1, 2013, was 16,005,191 shares of common stock, without par value.

DOCUMENTS INCORPORATED BY REFERENCE

The information required to be disclosed pursuant to Part III of this report either shall be (i) deemed to be incorporated by reference from selected portions of TriCo Bancshares' definitive proxy statement for the 2013 annual meeting of stockholders, if such proxy statement is filed with the Securities and Exchange Commission pursuant to Regulation 14A not later than 120 days after the end of the Company's most recently completed fiscal year, or (ii) included in an amendment to this report filed with the Commission on Form 10-K/A not later than the end of such 120 day period.

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FORWARD-LOOKING STATEMENTS

In addition to historical information, this Annual Report on Form 10-K contains forward-looking statements about TriCo Bancshares (the Company, TriCo or we) and its subsidiaries for which it claims the protection of the safe harbor provisions contained in the Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on Management's current knowledge and belief and include information concerning the Company's possible or assumed future financial condition and results of operations. When you see any of the words believes , expects , anticipates , estimates , or similar expressions, these generally indicate that we are making forward-looking statements. A number of factors, some of which are beyond the Company's ability to predict or control, could cause future results to differ materially from those contemplated. These factors include those listed at Item 1A Risk Factors, in this report.

Forward-looking statements speak only as of the date they are made, and the Company does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date the forward-looking statements are made, whether as a result of new information, future developments or otherwise.

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PART I

ITEM 1. BUSINESS

Information About TriCo Bancshares Business

TriCo Bancshares is a bank holding company incorporated in California in 1981 and registered under the Bank Holding Company Act of 1956, as amended (the BHC Act). The Company's principal subsidiary is Tri Counties Bank, a California-chartered commercial bank (the Bank). The Bank offers banking services to retail customers and small to medium-sized businesses through 66 branch offices in Northern and Central California. See Business of Tri Counties Bank. As a bank holding company, TriCo is subject to the supervision of the Board of Governors of the Federal Reserve System (the FRB) under the BHC Act. The Bank is subject to the supervision of the California Department of Financial Institutions (the DFI) and the Federal Deposit Insurance Corporation (the FDIC). The Company and the Bank are headquartered in Chico, California.

On July 31, 2003, the Company formed a subsidiary business trust, TriCo Capital Trust I, to issue trust preferred securities. On June 22, 2004, the Company formed a subsidiary business trust, TriCo Capital Trust II, to issue additional trust preferred securities. See Note 17 in the financial statements at Item 8 of this report for a discussion about the Company's issuance of trust preferred securities. The Bank, TriCo Capital Trust I and TriCo Capital Trust II are TriCo's only subsidiaries and TriCo does not conduct any material business operations independent of the Bank, TriCo Capital Trust I and TriCo Capital Trust II.

Additional information concerning the Company can be found on our website at www.tcbk.com. Copies of our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to these reports are available free of charge through the investors relations page of our website, www.tcbk.com, as soon as reasonably practicable after the Company files these reports with the U.S. Securities and Exchange Commission (SEC). The information on our website is not incorporated into this annual report.

Business of Tri Counties Bank

The Bank was incorporated as a California banking corporation on June 26, 1974, and received its certificate of authority to begin banking operations on March 11, 1975. The Bank engages in the general commercial banking business in the California counties of Butte, Contra Costa, Del Norte, Fresno, Glenn, Kern, Lake, Lassen, Madera, Mendocino, Merced, Napa, Nevada, Placer, Sacramento, Shasta, Siskiyou, Stanislaus, Sutter, Tehama, Tulare, Yolo and Yuba. The Bank currently operates from 41 traditional branches and 25 in-store branches.

The Bank conducts a commercial banking business including accepting demand, savings and time deposits and making commercial, real estate, and consumer loans. It also offers installment note collection, issues cashier's checks, sells travelers checks and provides safe deposit boxes and other customary banking services. Brokerage services are provided at the Bank's offices by the Bank's association with Raymond James Financial Services, Inc., an independent financial services provider and broker-dealer. The Bank does not offer trust services or international banking services.

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The Bank has emphasized retail banking since it opened. Most of the Bank's customers are retail customers and small to medium-sized businesses. The Bank emphasizes serving the needs of local businesses, farmers and ranchers, retired individuals and wage earners. The majority of the Bank's loans are direct loans made to individuals and businesses in northern and central California where its branches are located. At December 31, 2012, the total of the Bank's consumer loans net of deferred fees outstanding was \$386,111,000 (24.7%), the total of commercial loans outstanding was \$135,528,000 (8.7%), and the total of real estate loans including construction loans of \$33,054,000 was \$1,043,184,000 (66.6%). The Bank takes real estate, listed and unlisted securities, savings and time deposits, automobiles, machinery, equipment, inventory, accounts receivable and notes receivable secured by property as collateral for loans.

Most of the Bank's deposits are attracted from individuals and business-related sources. No single person or group of persons provides a material portion of the Bank's deposits, the loss of any one or more of which would have a materially adverse effect on the business of the Bank, nor is a material portion of the Bank's loans concentrated within a single industry or group of related industries.

In order to attract loan and deposit business from individuals and small to medium-sized businesses, branches of the Bank set lobby hours to accommodate local demands. In general, lobby hours are from 9:00 a.m. to 5:00 p.m. Monday through Thursday, and from 9:00 a.m. to 6:00 p.m. on Friday. Some Bank offices also utilize drive-up facilities operating from 9:00 a.m. to 6:00 p.m. The supermarket branches are open from 9:00 a.m. to 7:00 p.m. Monday through Saturday and 11:00 a.m. to 5:00 p.m. on Sunday.

The Bank offers 24-hour ATMs at all branch locations. The Bank's 72 ATMs are linked to several national and regional networks such as CIRRUS and STAR. In addition, banking by telephone on a 24-hour toll-free number is available to all customers. This service allows a customer to obtain account balances and most recent transactions, transfer moneys between accounts, make loan payments, and obtain interest rate information.

In February 1998, the Bank became the first bank based in the Northern Sacramento Valley to offer banking services on the Internet. This banking service provides customers one more tool to access their accounts.

Purchase and Assumption of Certain Assets and Liabilities of Citizens Bank of Northern California

On September 23, 2011, the Bank acquired certain of the assets and assumed substantially all of the liabilities of Citizens Bank of Northern California, Nevada City, California (Citizens), including substantially all the deposits from the FDIC, as receiver for Citizens. The acquisition was made pursuant to the terms of a purchase and assumption agreement entered into by the Bank and the FDIC. Based upon a preliminary closing with the FDIC as of September 23, 2011, the Bank acquired \$167.5 million in loans, \$9.4 million in investment securities, and \$93.5 million in cash and other assets, and assumed an estimated \$239.9 million in deposits, \$22.0 million in borrowings, and \$0.8 million in other liabilities. The Bank paid no cash or other consideration to acquire Citizens. See Note 2 in the financial statements at Item 8 of this report for a discussion about this transaction.

Purchase and Assumption of Certain Assets and Liabilities of Granite Community Bank

On May 28, 2010, the Bank acquired certain of the assets and assumed substantially all of the liabilities of Granite Community Bank, N.A., Granite Bay, California (Granite), including substantially all the deposits from the FDIC, as receiver for Granite. The acquisition was made pursuant to the terms of a purchase and assumption agreement entered into by the Bank and the FDIC. The Bank acquired \$64.8 million in loans, \$3.6 million in investment securities, and \$31.9 million in cash and other assets, and assumed an estimated \$95.0 million in deposits, \$5.0 million in borrowings, and \$0.05 million in other liabilities. The Bank paid no cash or other consideration to acquire Granite. In connection with the Acquisition, the Bank entered into a loss-sharing agreement with the FDIC that covered approximately \$89.3 million of Granite's assets (before fair value adjustments). The Bank will share in the losses on the asset pools (loans, foreclosed loan collateral, and certain investment securities) covered under the loss-sharing agreement. Pursuant to the terms of the loss sharing agreement, the FDIC is obligated to reimburse the Bank for 80% of losses with respect to covered assets. The Bank will reimburse the FDIC for 80% of recoveries with respect to losses for which the FDIC paid the Bank under the loss sharing agreement. See Note 2 in the financial statements at Item 8 of this report for a discussion about this transaction.

Other Activities

The Bank may in the future engage in other businesses either directly or indirectly through subsidiaries acquired or formed by the Bank subject to regulatory constraints. See Regulation and Supervision .

Employees

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At December 31, 2012, the Company and the Bank employed 831 persons, including seven executive officers. Full time equivalent employees were 737. No employees of the Company or the Bank are presently represented by a union or covered under a collective bargaining agreement. Management believes that its employee relations are good.

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Competition

The banking business in California generally, and in the Bank's primary service area of Northern and Central California specifically, is highly competitive with respect to both loans and deposits. It is dominated by a relatively small number of national and regional banks with many offices operating over a wide geographic area. Among the advantages such major banks have over the Bank is their ability to finance wide ranging advertising campaigns and to allocate their investment assets to regions of high yield and demand. By virtue of their greater total capitalization such institutions have substantially higher lending limits than does the Bank.

In addition to competing with savings institutions, commercial banks compete with other financial markets for funds as a result of the deregulation of the financial services industry. Yields on corporate and government debt securities and other commercial paper may be higher than on deposits, and therefore affect the ability of commercial banks to attract and hold deposits. Commercial banks also compete for available funds with money market instruments and mutual funds. During past periods of high interest rates, money market funds have provided substantial competition to banks for deposits and they may continue to do so in the future. Mutual funds are also a major source of competition for savings dollars.

The Bank relies substantially on local promotional activity, personal contacts by its officers, directors, employees and shareholders, extended hours, personalized service and its reputation in the communities it services to compete effectively.

Regulation and Supervision

General

The Company and the Bank are subject to extensive regulation under both federal and state law. This regulation is intended primarily for the protection of depositors, the deposit insurance fund, and the banking system as a whole, and not for the protection of shareholders of the Company. Set forth below is a summary description of the significant laws and regulations applicable to the Company and the Bank. The description is qualified in its entirety by reference to the applicable laws and regulations.

Regulatory Agencies

The Company is a legal entity separate and distinct from the Bank and its other subsidiaries. As a bank holding company, the Company is regulated under the BHC Act, and is subject to supervision, regulation and inspection by the FRB. The Company is also under the jurisdiction of the SEC and is subject to the disclosure and regulatory requirements of the Securities Act of 1933 and the Securities Exchange Act of 1934, each administered by the SEC. The Company's common stock is listed on the Nasdaq Global Select market (Nasdaq) under the trading symbol TCBK and the Company is, therefore, subject to the rules of Nasdaq for listed companies.

The Bank, as a state chartered bank, is subject to broad federal regulation and oversight extending to all its operations by the FDIC and to state regulation by the DFI.

Dodd-Frank Wall Street Reform and Consumer Protection Act

On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) was signed into law. The Dodd-Frank Act is intended to effect a fundamental restructuring of federal banking regulation. The Dodd-Frank Act is expected to have a significant impact on our business operations as its provisions take effect. Among the provisions that are likely to affect us are the following:

The creation of a Financial Services Oversight Counsel to identify emerging systemic risks and improve interagency cooperation;
Expanded FDIC authority to conduct the orderly liquidation of certain systemically significant non-bank financial companies in addition to depository institutions;

The establishment of strengthened capital and liquidity requirements for banks and bank holding companies, including minimum leverage and risk-based capital requirements no less than the strictest requirements in effect for depository institutions as of the date of enactment;

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The requirement by statute that bank holding companies serve as a source of financial strength for their depository institution subsidiaries;

Enhanced regulation of financial markets, including the derivative and securitization markets, and the elimination of certain proprietary trading activities by banks (the Volcker Rule);

The termination of investments by the U.S. Treasury under the Troubled Asset Relief Program (TARP);

The elimination and phase out of trust preferred securities from Tier 1 capital with certain exceptions;

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A permanent increase of the previously implemented temporary increase of FDIC deposit insurance to \$250,000 and an extension of federal deposit coverage until January 1, 2013, for the full net amount held by depositors in non-interest bearing transaction accounts;

Authorization for financial institutions to pay interest on business checking accounts;

Changes in the calculation of FDIC deposit insurance assessments, such that the assessment base will no longer be the institution's deposit base, but instead, will be its average consolidated total assets less its average tangible equity;

The elimination of remaining barriers to de novo interstate branching by banks;

Expanded restrictions on transactions with affiliates and insiders under Section 23A and 23B of the Federal Reserve Act and lending limits for derivative transactions, repurchase agreements, and securities lending and borrowing transactions;

Provisions that affect corporate governance and executive compensation at most United States publicly traded companies, including (i) stockholder advisory votes on executive compensation, (ii) executive compensation clawback requirements for companies listed on national securities exchanges in the event of materially inaccurate statements of earnings, revenues, gains or other criteria, (iii) enhanced independence requirements for compensation committee members, and (iv) giving the SEC authority to adopt proxy access rules which would permit stockholders of publicly traded companies to nominate candidates for election as director and have those nominees included in a company's proxy statement; and

The creation of a Bureau of Consumer Financial Protection, which is authorized to promulgate and enforce consumer protection regulations relating to bank and non-bank financial products and which may examine and enforce its regulations on banks with more than \$10 billion in assets.

The numerous rules and regulations that have been promulgated and are yet to be promulgated and finalized under Dodd-Frank are likely to significantly impact the Company's operations and compliance costs, such as changes in FDIC assessments, the permitted payment of interest on demand deposits and projected enhanced consumer compliance requirements. More stringent capital, liquidity and leverage requirements are expected to impact the Company's business as Dodd-Frank is fully implemented. The federal agencies have issued many proposed rules pursuant to provisions of Dodd-Frank which will apply directly to larger institutions with either more than \$50 billion in assets or more than \$10 billion in assets, such as proposed regulations for financial institutions deemed systemically significant, proposed rules requiring capital plans and stress tests and the Reserve Board's proposed rules to implement the Volcker Rule, as well as a final rule for the largest (over \$250 billion in assets) and internationally active banks setting a new minimum risk-based capital floor. These and other requirements and policies imposed on larger institutions, such as expected countercyclical requirements for increased capital in times of economic expansion and a decrease in times of contraction, may subsequently become expected best practices for smaller institutions, such as the Company. Therefore, as a result of the changes required by Dodd-Frank, the profitability of the Company's business activities may be impacted and the Company may be required to make changes to certain of its business practices. Such developments and new standards would require the Company to devote even more management attention and resources to evaluate and make any changes necessary to comply with new statutory and regulatory requirements.

The Bank Holding Company Act

The Company is registered as a bank holding company under the BHC Act. In general, the BHC Act limits the business of bank holding companies to banking, managing or controlling banks and other activities that the Federal Reserve has determined to be so closely related to banking as to be a proper incident thereto. As a result of the Gramm-Bliley Act, which amended the BHC Act, bank holding companies that are financial holding companies may engage in any activity, or acquire and retain the shares of a company engaged in any activity, that is either (i) financial in nature or incidental to such financial activity (as determined by the FRB in consultation with the Office of the Comptroller of the Currency (the OCC)) or (ii) complementary to a financial activity, and that does not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally (as determined solely by the FRB). Activities that are financial in nature include securities underwriting and dealing, insurance underwriting and agency, and making merchant banking investments.

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If a bank holding company seeks to engage in the broader range of activities that are permitted under the BHC Act for financial holding companies, (i) all of its depository institution subsidiaries must be well capitalized and well managed and (ii) it must file a declaration with the FRB that it elects to be a financial holding company. A depository institution subsidiary is considered to be well capitalized if it satisfies the requirements for this status discussed in the section captioned Capital Adequacy and Prompt Corrective Action, included elsewhere in this item. A depository institution subsidiary is considered well managed if it received a composite rating and management rating of at least satisfactory in its most recent examination. In addition, the subsidiary depository institution must have received a rating of at least satisfactory in its most recent examination under the Community Reinvestment Act. (See the section captioned Consumer Protection Laws and Regulations included elsewhere in this item.) The Company has not elected to become a financial holding company.

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The BHC Act, the Federal Bank Merger Act, and other federal and state statutes regulate acquisitions of commercial banks. The BHC Act requires the prior approval of the FRB for the direct or indirect acquisition of more than 5 percent of the voting shares of a commercial bank or its parent holding company. Under the Federal Bank Merger Act, the prior approval of an acquiring bank's primary federal regulator is required before it may merge with another bank or purchase the assets or assume the deposits of another bank. In reviewing applications seeking approval of merger and acquisition transactions, the bank regulatory authorities will consider, among other things, the competitive effect and public benefits of the transactions, the capital position of the combined organization, the applicant's performance record under the Community Reinvestment Act, fair housing laws and the effectiveness of the subject organizations in combating money laundering activities.

Safety and Soundness Standards

The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) implemented certain specific restrictions on transactions and required the regulators to adopt overall safety and soundness standards for depository institutions related to internal control, loan underwriting and documentation, and asset growth. Among other things, FDICIA limits the interest rates paid on deposits by undercapitalized institutions, the use of brokered deposits and the aggregate extension of credit by a depository institution to an executive officer, director, principal stockholder or related interest, and reduces deposit insurance coverage for deposits offered by undercapitalized institutions for deposits by certain employee benefits accounts.

Section 39 to the Federal Deposit Insurance Act requires the agencies to establish safety and soundness standards for insured financial institutions covering:

internal controls, information systems and internal audit systems;

loan documentation;

credit underwriting;

interest rate exposure;

asset growth;

compensation, fees and benefits;

asset quality, earnings and stock valuation; and

excessive compensation for executive officers, directors or principal shareholders which could lead to material financial loss. If an agency determines that an institution fails to meet any standard established by the guidelines, the agency may require the financial institution to submit to the agency an acceptable plan to achieve compliance with the standard. If the agency requires submission of a compliance plan and the institution fails to timely submit an acceptable plan or to implement an accepted plan, the agency must require the institution to correct the deficiency. An institution must file a compliance plan within 30 days of a request to do so from the institution's primary federal regulatory agency. The agencies may elect to initiate enforcement action in certain cases rather than rely on an existing plan particularly where failure to meet one or more of the standards could threaten the safe and sound operation of the institution.

Restrictions on Dividends and Distributions

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A California corporation such as TriCo may make a distribution to its shareholders if the corporation's retained earnings equal at least the amount of the proposed distribution or if after giving effect to the distribution, the value of the corporation's assets exceed the amount of its liabilities plus the amount of shareholders preferences, if any, and certain other conditions are met.

The primary source of funds for payment of dividends by TriCo to its shareholders will be the receipt of dividends and management fees from the Bank. TriCo's ability to receive dividends from the Bank is limited by applicable state and federal law. Under the California Financial Code, funds available for cash dividend payments by a bank are restricted to the lesser of: (i) retained earnings; or (ii) the bank's net income for its last three fiscal years (less any distributions to shareholders made during such period). However, with the prior approval of the Commissioner of the DFI, a bank may pay cash dividends in an amount not to exceed the greatest of the: (1) retained earnings of the bank; (2) net income of the bank for its last fiscal year; or (3) net income of the bank for its current fiscal year. However, if the DFI finds that the shareholders' equity of the bank is not adequate or that the payment of a dividend would be unsafe or unsound, the Commissioner may order the bank not to pay a dividend to shareholders.

Additionally, under FDICIA, a bank may not make any capital distribution, including the payment of dividends, if after making such distribution the bank would be in any of the undercapitalized categories under the FDIC's Prompt Corrective Action regulations. A bank is undercapitalized for this purpose if its leverage ratios, Tier 1 risk-based capital level and total risk-based capital ratio are not at least four percent, four percent and eight percent, respectively.

The FRB, FDIC and the DFI have authority to prohibit a bank holding company or a bank from engaging in practices which are considered to be unsafe and unsound. Depending on the financial condition of the Bank and upon other factors, the FRB, FDIC or the DFI could determine that payment of dividends or other payments by TriCo or the Bank might constitute an unsafe or unsound practice.

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Consumer Protection Laws and Regulations

The Company is subject to many federal consumer protection statutes and regulations, some of which are discussed below.

The Community Reinvestment Act of 1977 is intended to encourage insured depository institutions, while operating safely and soundly, to help meet the credit needs of their communities. This act specifically directs the federal regulatory agencies 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 practices. This act 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 Community Reinvestment Act 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 Equal Credit Opportunity Act 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 is designed to ensure that credit terms are disclosed in a meaningful way so that consumers may compare credit terms more readily and knowledgeably.

The Fair Housing 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. The Home Mortgage Disclosure Act 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. This act 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.

The Real Estate Settlement Procedures Act requires lenders to provide borrowers with disclosures regarding the nature and cost of real estate settlements. Also, this act 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, injunctive relief and other penalties.

USA Patriot Act of 2001

The USA Patriot Act was enacted in 2001 to combat money laundering and terrorist financing. The impact of the Patriot Act on financial institutions is significant and wide ranging. The Patriot Act contains sweeping anti-money laundering and financial transparency laws and requires various regulations, including:

due diligence requirements for financial institutions that administer, maintain, or manage private bank accounts or correspondent accounts for non-U.S. persons,

standards for verifying customer identification at account opening,

rules to promote cooperation among financial institutions, regulators, and law enforcement entities to assist in the identification of parties that may be involved in terrorism or money laundering,

reports to be filed by non-financial trades and business with the Treasury Department's Financial Crimes Enforcement Network for transactions exceeding \$10,000, and

the filing of suspicious activities reports by securities brokers and dealers if they believe a customer may be violating U.S. laws and regulations.

Capital Requirements

Federal regulation imposes upon all financial institutions a variable system of risk-based capital guidelines designed to make capital requirements sensitive to differences in risk profiles among banking organizations, to take into account off-balance sheet exposures and to promote uniformity in the definition of bank capital uniform nationally.

The Bank and the Company are subject to the minimum capital requirements of the FDIC and the FRB, respectively. As a result of these requirements, the growth in assets is limited by the amount of its capital as defined by the respective regulatory agency. Capital requirements may have an effect on profitability and the payment of dividends on the common stock of the Bank and the Company. If an entity is unable to increase its assets without violating the minimum capital requirements or is forced to reduce assets, its ability to generate earnings would be reduced.

The FRB and the FDIC have adopted guidelines utilizing a risk-based capital structure. Qualifying capital is divided into two tiers. Tier 1 capital consists generally of common stockholders' equity, qualifying noncumulative perpetual preferred stock,

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qualifying cumulative perpetual preferred stock (up to 25% of total Tier 1 capital) and minority interests in the equity accounts of consolidated subsidiaries, less goodwill and certain other intangible assets. Tier 2 capital consists of, among other things, allowance for loan and lease losses up to 1.25% of weighted risk assets, other perpetual preferred stock, hybrid capital instruments, perpetual debt, mandatory convertible debt securities, subordinated debt and intermediate-term preferred stock. Tier 2 capital qualifies as part of total capital up to a maximum of 100% of Tier 1 capital. Amounts in excess of these limits may be issued but are not included in the calculation of risk-based capital ratios. Under these risk-based capital guidelines, the Bank and the Company are required to maintain capital equal to at least 8% of its assets, of which at least 4% must be in the form of Tier 1 capital.

The guidelines also require the Company and the Bank to maintain a minimum leverage ratio of 4% of Tier 1 capital to total assets (the leverage ratio). The leverage ratio is determined by dividing an institution's Tier 1 capital by its quarterly average total assets, less goodwill and certain other intangible assets. The leverage ratio constitutes a minimum requirement for the most well-run banking organizations. See Note 29 in the financial statements at Item 8 of this report for a discussion about the Company's risk-based capital and leverage ratios.

Basel Accords

The current risk-based capital guidelines which apply to the Company and the Bank are based upon the 1988 capital accord (referred to as Basel I) of the International Basel Committee on Banking Supervision (the Basel Committee), a committee of central banks and bank supervisors and regulators from the major industrialized countries. The Basel Committee develops broad policy guidelines for use by each country's supervisors in determining the supervisory policies they apply. A new framework and accord, referred to as Basel II, evolved from 2004 to 2006 out of the efforts to revise capital adequacy standards for internationally active banks. Basel II emphasizes internal assessment of credit, market and operational risk; supervisory assessment and market discipline in determining minimum capital requirements and became mandatory for large or core international banks outside the United States in 2008 (total assets of \$250 billion or more or consolidated foreign exposures of \$10 billion or more). Basel II was optional for others, and if adopted, must first be complied within a parallel run for two years along with the existing Basel I standards. The Company is not required to comply with Basel II and has not elected to apply the Basel II standards.

The United States federal banking agencies issued a proposed rule for banking organizations that do not use the advanced approaches under Basel II. While this proposed rule generally parallels the relevant approaches under Basel II, it diverges where United States markets have unique characteristics and risk profiles. A definitive final rule has not yet been issued. The United States banking agencies indicated, however, that they would retain the minimum leverage requirement for all United States banks.

In 2010 and 2011, the Basel Committee finalized proposed reforms on capital and liquidity, generally referred to as Basel III, to reconsider regulatory capital standards, supervisory and risk-management requirements and additional disclosures to further strengthen the Basel II framework in response to the worldwide economic downturn. Although Basel III is intended to be implemented by participating countries for large, internationally active banks, its provisions are likely to be considered by United States banking regulators in developing new regulations applicable to other banks in the United States. Basel III provides for increases in the minimum Tier 1 common equity ratio and the minimum requirement for the Tier 1 capital ratio. Basel III additionally includes a capital conservation buffer on top of the minimum requirement designed to absorb losses in periods of financial and economic distress; and an additional required countercyclical buffer percentage to be implemented according to a particular nation's circumstances. These capital requirements are further supplemented under Basel III by a non-risk-based leverage ratio. Basel III also reaffirms the Basel Committee's intention to introduce higher capital requirements on securitization and trading activities.

The Basel III liquidity proposals have three main elements: (i) a liquidity coverage ratio designed to meet the bank's liquidity needs over a 30-day time horizon under an acute liquidity stress scenario, (ii) a net stable funding ratio designed to promote more medium and long term funding over a one year time horizon, and (iii) a set of monitoring tools that the Basel Committee indicates should be considered as the minimum types of information that banks should report to supervisors.

Implementation of Basel III in the United States will require regulations and guidelines by United States banking regulators, which may differ in significant ways from the recommendations published by the Basel Committee. The new Basel III capital standards were scheduled to be phased in from January 1, 2013 until January 1, 2019 but United States banking regulators have delayed the adoption of final rules implementing these standards. It is unclear how smaller banking organizations in the United States will be subject to these regulations and guidelines. Basel III standards, if adopted, would lead to significantly higher capital requirements, higher capital charges and more restrictive leverage and liquidity ratios. The Basel III standards, if adopted, could lead to significantly higher capital requirements, higher capital charges and more restrictive leverage and liquidity ratios. The standards would, among other things:

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Impose more restrictive eligibility requirements for Tier 1 and Tier 2 capital;

Increase the minimum Tier 1 common equity ratio to 4.5%, net of regulatory deductions, and introduce a capital conservation buffer of an additional 2.5% of common equity to risk-weighted assets, raising the target minimum common equity ratio to 7.0%;

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Increase the minimum Tier 1 capital ratio to 8.5% inclusive of the capital conservation buffer;

Increase the minimum total capital ratio to 10.5% inclusive of the capital conservation buffer; and

Introduce a countercyclical capital buffer of up to 2.5% of common equity or other fully loss absorbing capital for periods of excess credit growth.

Introduces a non-risk adjusted Tier 1 leverage ratio of 3.0%, based on a measure of total exposure rather than total assets, and new liquidity standards.

Prompt Corrective Action

Prompt Corrective Action Regulations of the federal bank regulatory agencies establish five capital categories in descending order (well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized), assignment to which depends upon the institution's total risk-based capital ratio, Tier 1 risk-based capital ratio, and leverage ratio. Institutions classified in one of the three undercapitalized categories are subject to certain mandatory and discretionary supervisory actions, which include increased monitoring and review, implementation of capital restoration plans, asset growth restrictions, limitations upon expansion and new business activities, requirements to augment capital, restrictions upon deposit gathering and interest rates, replacement of senior executive officers and directors, and requiring divestiture or sale of the institution. The Bank has been classified as well-capitalized since adoption of these regulations.

Premiums for Deposit Insurance

Deposit accounts in the Bank are insured by the FDIC, generally up to a maximum of \$250,000 per separately insured depositor. The Bank's deposits are subject to FDIC deposit insurance assessments. The Bank pays insurance assessments based on its consolidated total assets less tangible equity capital. This assessment is based on the risk category of the institution. To determine the total base assessment rate, the FDIC first establishes an institution's initial base assessment rate and then adjusts the initial base assessment based upon an institution's levels of unsecured debt, secured liabilities, and brokered deposits. The total base assessment rate ranges from 2.5 to 45 basis points of the institution's average consolidated total assets less tangible equity capital.

In May of 2009, the FDIC adopted a final rule imposing a five basis point special assessment on each insured depository institution's assets minus Tier 1 capital as of June 30, 2009. As a result, the Bank's expense for deposit insurance for the fiscal year ended December 31, 2009 includes approximately \$933,000 for this emergency assessment which was levied as of June 30, 2009 and paid on September 30, 2009.

In November of 2009, the FDIC adopted an amendment to its assessment regulations to require insured institutions to prepay, on December 30, 2009, their estimated quarterly risk-based assessments for the fourth quarter of calendar 2009 and for all of the calendar years 2010, 2011 and 2012. The amount of the prepayment was generally determined based upon an institution's assessment rate in effect on September 30, 2009, adjusted to reflect a 5% growth and as an assessment rate increase of three cents per \$100 of deposits effective January 1, 2011. The Bank's prepayment amount was \$10,544,000.

On November 21, 2008, the Board of Directors of the FDIC adopted a final rule relating to the Temporary Liquidity Guarantee Program (TLG Program). The TLG Program was intended to counter the system-wide crisis in the nation's financial sector. Under the TLG Program the FDIC (i) guaranteed, through the earlier of maturity or June 30, 2012, certain newly issued senior unsecured debt issued by participating institutions on or after October 14, 2008, and before June 30, 2009 and (ii) provided unlimited FDIC deposit insurance coverage for non-interest bearing transaction deposit accounts, Negotiable Order of Withdrawal accounts paying not more than 0.25% interest per annum and Interest on Lawyers Trust Accounts held at participating FDIC-insured institutions through December 31, 2010. The Dodd-Frank Act extended unlimited deposit insurance to non-interest bearing transaction accounts through December 31, 2012. The fee assessment for deposit insurance coverage was 10 basis points per quarter on amounts in covered accounts exceeding \$250,000. On December 5, 2008, the Company elected to participate in both guarantee programs. The Company had issued no debt under the TLG Program on December 31, 2012 when the program expired.

The Bank is generally unable to control the amount of premiums that it is required to pay for FDIC insurance. If there are additional bank or financial institution failures or if the FDIC otherwise determines, the Bank may be required to pay even higher FDIC premiums than the recently increased levels. These announced increases and any future increases in FDIC insurance premiums may have a material and adverse affect on the Company's earnings and could have a material adverse effect on the value of, or market for, the Company's common stock.

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The FDIC may terminate a depository institution's deposit insurance upon a finding that the institution's financial condition is unsafe or unsound or that the institution has engaged in unsafe or unsound practices that pose a risk to the DIF or that may prejudice the interest of the bank's depositors. The termination of deposit insurance for the Bank would also result in the revocation of the Bank's charter by the DFI.

Impact of Monetary Policies

Banking is a business that depends on interest rate differentials. In general, the difference between the interest paid by a bank on its deposits and other borrowings, and the interest rate earned by banks on loans, securities and other interest-earning assets comprises the major source of banks earnings. Thus, the earnings and growth of banks are subject to the influence of economic conditions generally, both domestic and foreign, and also to the monetary and fiscal policies of the United States and its agencies, particularly the FRB. The FRB implements national monetary policy, such as seeking to curb inflation and combat recession, by its open-market dealings in United States government securities, by adjusting the required level of reserves for financial institutions subject to reserve requirements and through adjustments to the discount rate applicable to borrowings by banks which are members of the FRB. The actions of the FRB in these areas influence the growth of bank loans, investments and deposits and also affect interest rates. The nature and timing of any future changes in such policies and their impact on the Company cannot be predicted. In addition, adverse economic conditions could make a higher provision for loan losses a prudent course and could cause higher loan loss charge-offs, thus adversely affecting the Company's net earnings.

Securities Laws

The Company is subject to the periodic reporting requirements of the Securities and Exchange Act of 1934, as amended, which include filing annual, quarterly and other current reports with the Securities and Exchange Commission. The Sarbanes-Oxley Act was enacted in 2002 to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to securities laws. Among other things, this act:

prohibits a registered public accounting firm from performing specified nonaudit services contemporaneously with a mandatory audit,

requires the chief executive officer and chief financial officer of an issuer to certify each annual or quarterly report filed with the Securities and Exchange Commission,

requires an issuer to disclose all material off-balance sheet transactions that may have a material effect on an issuer's financial status, and

prohibits insider transactions in an issuer's stock during lock-out periods of an issuer's pension plans.

The Company is also required to comply with the rules and regulations of The NASDAQ Stock Market, Inc., on which its common stock is listed.

ITEM 1A. RISK FACTORS

In analyzing whether to make or continue an investment in the Company, investors should consider, among other factors, the following:

Risks Related to the Nature and Geographic Area of Our Business

We face a challenging economic environment. A return of recessionary conditions in the United States and in California in particular could result in increases in our level of non-performing loans and/or reduce demand for our products and services, which could have an adverse effect on our results of operations.

From December 2007 through June 2009, the U.S. economy was in recession. Business activity across a wide range of industries and regions in the U. S. was greatly reduced, the value of real estate decreased and unemployment increased significantly. Although economic conditions have

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improved, certain sectors, such as real estate and manufacturing, remain weak and unemployment remains high. Business activity across a wide range of industries and regions is greatly reduced and local governments and many businesses continue to be in serious difficulty due to the lack of consumer spending.

Overall, during 2012, the business environment has been adverse for many households and businesses in California and the United States as unemployment remains high. In addition, concerns over the United States credit rating, the European sovereign debt crisis, among other economic indicators, have contributed to increased volatility in the capital markets and diminished expectations for the U.S. economy. These factors have caused, and may continue to cause, many financial institutions to seek additional capital, to merge with larger and stronger institutions and, in some cases, to fail. While we continue to take steps to decrease and limit our exposure to problem loans, we nonetheless retain direct exposure to the residential and commercial real estate markets and the economy generally, so we are affected by these events.

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There can be no assurance that these conditions will improve in the near term. A return of recessionary conditions and/or continued negative developments in the domestic and international credit markets may significantly affect the markets in which we do business, the value of our loans and investments, and our ongoing operations, costs and profitability. Further declines in real estate values and sales volumes and continued high unemployment levels may result in higher than expected loan delinquencies and a decline in demand for our products and services. These negative events may cause us to incur losses and may adversely affect our capital, financial condition and results of operations. .

Our business may be adversely affected by business conditions in Northern and Central California.

We conduct most of our business in Northern and Central California. As a result of this geographic concentration, our results are impacted by the difficult economic conditions in California. The current and on-going deterioration in the economic conditions in California could result in the following consequences, any of which could have a material adverse effect on our business, financial condition, results of operations and cash flows:

problem assets and foreclosures may increase,

demand for our products and services may decline,

low cost or non-interest bearing deposits may decrease, and

collateral for loans made by us, especially real estate, may decline in value, in turn reducing customers' borrowing power, and reducing the value of assets and collateral associated with our existing loans.

In view of the concentration of our operations and the collateral securing our loan portfolio in both Northern and Central California, we may be particularly susceptible to the adverse effects of any of these consequences, any of which could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We are exposed to risks in connection with the loans we make.

A significant source of risk for us arises from the possibility that we will sustain losses because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loans. Our earnings are significantly affected by our ability to properly originate, underwrite and service loans. We have underwriting and credit monitoring procedures and credit policies, including the establishment and review of the allowance for loan losses, that we believe to be appropriate to minimize this risk by assessing the likelihood of nonperformance, tracking loan performance and diversifying our respective loan portfolios. Such policies and procedures, however, may not prevent unexpected losses that could adversely affect our results of operations. We could sustain losses if we incorrectly assess the creditworthiness of our borrowers or fail to detect or respond to deterioration in asset quality in a timely manner.

Our allowance for loan losses may not be adequate to cover actual losses.

Like all financial institutions, we maintain an allowance for loan losses to provide for loan defaults and non-performance. Our allowance for loan losses may not be adequate to cover actual loan losses, and future provisions for loan losses could materially and adversely affect our business, financial condition, results of operations and cash flows. The allowance for loan losses reflects our estimate of the probable losses in our loan portfolio at the relevant balance sheet date. Our allowance for loan losses is based on prior experience, as well as an evaluation of the known risks in the current portfolio, composition and growth of the loan portfolio and economic factors. The determination of an appropriate level of loan loss allowance is an inherently difficult process and is based on numerous assumptions. The amount of future losses is susceptible to changes in economic, operating and other conditions, including changes in interest rates, that may be beyond our control and these losses may exceed current estimates. Federal and state regulatory agencies, as an integral part of their examination process, review our loans and allowance for loan losses. While we believe that our allowance for loan losses is adequate to cover current losses, we cannot assure you that we will not increase the allowance for loan losses further or that the allowance will be adequate to absorb loan losses we actually incur. Either of these occurrences could have a material adverse effect on our business, financial condition and results of operations.

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A significant majority of the loans in our portfolio are secured by real estate and the downturn in our real estate markets could hurt our business.

The downturn in our real estate markets could hurt our business because many of our loans are secured by real estate. Real estate values and real estate markets are generally affected by changes in national, regional or local economic conditions, fluctuations in interest rates and the availability of loans to potential purchasers, changes in tax laws and other governmental statutes, regulations and policies and acts of nature. As real estate prices decline, the value of real estate collateral securing our loans is reduced. As a result, our ability to recover on defaulted loans by foreclosing and selling the real estate collateral could then be diminished and we would be more likely to suffer losses on defaulted loans. As of December 31, 2012, approximately 89.4% of the book value of our loan portfolio consisted of loans collateralized by various types of real estate. Substantially all of our real estate collateral is located in California. So if there is a significant further decline in real estate values in California, the collateral for our loans will provide less security. Real estate values could also be affected by, among other things, earthquakes and national disasters particular to California in particular. Any such downturn could have a material adverse effect on our business, financial condition, results of operations and cash flows.

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We depend on key personnel and the loss of one or more of those key personnel may materially and adversely affect our prospects.

Competition for qualified employees and personnel in the banking industry is intense and there are a limited number of qualified persons with knowledge of, and experience in, the California community banking industry. The process of recruiting personnel with the combination of skills and attributes required to carry out our strategies is often lengthy. Our success depends to a significant degree upon our ability to attract and retain qualified management, loan origination, finance, administrative, marketing and technical personnel and upon the continued contributions of our management and personnel. In particular, our success has been and continues to be highly dependent upon the abilities of our senior management team of Messrs. Smith, O Sullivan, Bailey, Reddish, Carney, Miller and Rios, who have expertise in banking and experience in the California markets we serve and have targeted for future expansion. We also depend upon a number of other key executives who are California natives or are long-time residents and who are integral to implementing our business plan. The loss of the services of any one of our senior executive management team or other key executives could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We are exposed to risk of environmental liabilities with respect to properties to which we take title.

In the course of our business, we may foreclose and take title to real estate and could be subject to environmental liabilities with respect to these properties. We may be held liable to a governmental entity or to third parties for property damage, personal injury, investigation and clean-up costs incurred by these parties in connection with environmental contamination, or may be required to investigate or clean-up hazardous or toxic substances, or chemical releases at a property. The costs associated with investigation or remediation activities could be substantial. In addition, if we are the owner or former owner of a contaminated site, we may be subject to common law claims by third parties based on damages and costs resulting from environmental contamination emanating from the property. If we become subject to significant environmental liabilities, our business, financial condition, results of operations and cash flows could be materially adversely affected.

Strong competition in California could hurt our profits.

Competition in the banking and financial services industry is intense. Our profitability depends upon our continued ability to successfully compete. We compete exclusively in northern and central California for loans, deposits and customers with commercial banks, savings and loan associations, credit unions, finance companies, mutual funds, insurance companies, and brokerage and investment banking firms. In particular, our competitors include several major financial companies whose greater resources may afford them a marketplace advantage by enabling them to maintain numerous locations and mount extensive promotional and advertising campaigns. Additionally, banks and other financial institutions with larger capitalization and financial intermediaries not subject to bank regulatory restrictions may have larger lending limits which would allow them to serve the credit needs of larger customers. Areas of competition include interest rates for loans and deposits, efforts to obtain loan and deposit customers and a range in quality of products and services provided, including new technology-driven products and services. Technological innovation continues to contribute to greater competition in domestic and international financial services markets as technological advances enable more companies to provide financial services. We also face competition from out-of-state financial intermediaries that have opened loan production offices or that solicit deposits in our market areas. If we are unable to attract and retain banking customers, we may be unable to continue our loan growth and level of deposits and our business, financial condition, results of operations and cash flows may be adversely affected.

Our previous results may not be indicative of our future results.

We may not be able to sustain our historical rate of growth and level of profitability or may not even be able to grow our business or continue to be profitable at all. Various factors, such as economic conditions, regulatory and legislative considerations and competition, may also impede or prohibit our ability to expand our market presence and financial performance. If we experience a significant decrease in our historical rate of growth, our results of operations and financial condition may be adversely affected due to a high percentage of our operating costs being fixed expenses.

We may be adversely affected by the soundness of other financial institutions.

Financial services institutions are interrelated as a result of clearing, counterparty, or other relationships. We have exposure to many different industries and counterparties, and routinely executes transactions with counterparties in the financial services industry, including commercial banks, brokers and dealers, and other institutional clients. Many of these transactions expose us to credit risk in the event of a default by a counterparty or client. In addition, our credit risk may be exacerbated when the collateral that we hold cannot be realized upon or is liquidated at prices not sufficient to recover the full amount of the credit or derivative exposure due to us. Any such losses could have a material adverse affect on our financial condition and results of operations.

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Recent health care legislation could increase our expenses or require us to pass further costs on to our employees, which could adversely affect our operations, financial condition and earnings.

Legislation enacted in 2010 requires companies to provide expanded health care coverage to their employees, such as affordable coverage to part-time employees and coverage to dependent adult children of employees. Companies will also be required to enroll new employees automatically into their health plans. Compliance with these and other new requirements of the health care legislation will increase our employee benefits expense, and may require us to pass these costs on to our employees, which could give us a competitive disadvantage in hiring and retaining qualified employees.

Market and Interest Rate Risk

Decreasing interest rates could hurt our profits.

Our ability to earn a profit, like that of most financial institutions, depends on our net interest income, which is the difference between the interest income we earn on our interest-earning assets, such as mortgage loans and investments, and the interest expense we pay on our interest-bearing liabilities, such as deposits. Our profitability depends on our ability to manage our assets and liabilities during periods of changing market interest rates. Recently, the FRB has maintained the targeted federal funds rate at record low levels. A sustained decrease in market interest rates could adversely affect our earnings. When interest rates decline, borrowers tend to refinance higher-rate, fixed-rate loans at lower rates. Under those circumstances, we would not be able to reinvest those prepayments in assets earning interest rates as high as the rates on the prepaid loans on investment securities. In addition, our commercial real estate and commercial loans, which carry interest rates that adjust in accordance with changes in the prime rate, will adjust to lower rates.

Our business is subject to interest rate risk and variations in interest rates may negatively affect our financial performance.

Because of the differences in the maturities and repricing characteristics of our interest-earning assets and interest-bearing liabilities, changes in interest rates do not produce equivalent changes in interest income earned on interest-earning assets and interest paid on interest-bearing liabilities. Accordingly, fluctuations in interest rates could adversely affect our interest rate spread and, in turn, our profitability. In addition, loan origination volumes are affected by market interest rates. Rising interest rates, generally, are associated with a lower volume of loan originations while lower interest rates are usually associated with higher loan originations. Conversely, in rising interest rate environments, loan repayment rates may decline and in falling interest rate environments, loan repayment rates may increase. Although we have been successful in generating new loans during 2012, the continuation of historically low long-term interest rate levels may cause additional refinancing of commercial real estate and 1-4 family residence loans, which may depress our loan volumes or cause rates on loans to decline. In addition, an increase in the general level of short-term interest rates on variable rate loans may adversely affect the ability of certain borrowers to pay the interest on and principal of their obligations or reduce the amount they wish to borrow. Additionally, if short-term market rates rise, in order to retain existing deposit customers and attract new deposit customers we may need to increase rates we pay on deposit accounts. Accordingly, changes in levels of market interest rates could materially and adversely affect our net interest spread, asset quality, loan origination volume, business, financial condition, results of operations and cash flows.

Regulatory Risks

Recently enacted financial reform legislation will, among other things, create a new Consumer Financial Protection Bureau, tighten capital standards and result in new laws and regulations that are expected to increase our costs of operations.

On July 21, 2010, the President signed the Dodd-Frank Act. This new law significantly changes the current bank regulatory structure and affects the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act requires various federal agencies to adopt a broad range of new implementing rules and regulations, and to prepare numerous studies and reports for Congress. The federal agencies are given significant discretion in drafting the implementing rules and regulations, and consequently, many of the details and much of the impact of the Dodd-Frank Act may not be known for many months or years.

Among other things, the Dodd-Frank Act creates a new Consumer Financial Protection Bureau with broad powers to supervise and enforce consumer protection laws. The Consumer Financial Protection Bureau has broad rule-making authority for a wide range of consumer protection laws that apply to all banks and savings institutions, including the authority to prohibit unfair, deceptive or abusive acts and practices. The Consumer Financial Protection Bureau has examination and enforcement authority over all banks and savings institutions with more than \$10 billion in assets. Banks such as the Bank with \$10 billion or less in assets will continue to be examined for compliance with the consumer laws by their primary bank regulators. The Dodd-Frank Act also weakens the federal preemption rules that have been applicable for national banks and federal savings associations, and gives state attorneys general the ability to enforce federal consumer protection laws.

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The Dodd-Frank Act requires minimum leverage (Tier 1) and risk based capital requirements for bank and savings and loan holding companies that are no less than those applicable to banks, which will exclude certain instruments that previously have been eligible for inclusion by bank holding companies as Tier 1 capital, such as trust preferred securities (unless such securities were issued prior to May 19, 2010 by a bank holding company with less than \$15 billion in assets).

It is difficult to predict at this time what specific impact the Dodd-Frank Act and the yet to be written implementing rules and regulations will have on community banks. However, it is expected that at a minimum they will increase our operating and compliance costs and could increase our interest expense.

We operate in a highly regulated environment and we may be adversely affected by changes in laws and regulations. Regulations may prevent or impair our ability to pay dividends, engage in acquisitions or operate in other ways.

We are subject to extensive regulation, supervision and examination by the DFI, FDIC, and the FRB. See Item 1 Regulation and Supervision of this report for information on the regulation and supervision which governs our activities. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on our operations, the classification of our assets and determination of the level of our allowance for loan losses. Banking regulations, designed primarily for the protection of depositors, may limit our growth and the return to you, our investors, by restricting certain of our activities, such as:

the payment of dividends to our shareholders,

possible mergers with or acquisitions of or by other institutions,

desired investments,

loans and interest rates on loans,

interest rates paid on deposits,

the possible expansion of branch offices, and

the ability to provide securities or trust services.

We also are subject to capitalization guidelines set forth in federal legislation and could be subject to enforcement actions to the extent that we are found by regulatory examiners to be undercapitalized. We cannot predict what changes, if any, will be made to existing federal and state legislation and regulations or the effect that such changes may have on our future business and earnings prospects. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, legislation or supervisory action, may have a material impact on our operations.

Compliance with changing regulation of corporate governance and public disclosure may result in additional risks and expenses.

Changing laws, regulations and standards relating to corporate governance and public disclosure, including the Dodd-Frank Act, the Sarbanes-Oxley Act of 2002 and new SEC regulations, are creating additional expense for publicly-traded companies such as TriCo. The application of these laws, regulations and standard may evolve over time as new guidance is provided by regulatory and governing bodies, which could result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing revisions to disclosure and governance practices. We are committed to maintaining high standards of corporate governance and public disclosure. As a result, our efforts to comply with evolving laws, regulations and standards have resulted in, and are likely to continue to result in, increased expenses and a diversion of management time and attention. In particular, our efforts to comply with Section 404 of the Sarbanes-Oxley Act of 2002 and the related

regulations regarding management's required assessment of its internal control over financial reporting and its external auditors' audit of that assessment has required the commitment of significant financial and managerial resources. We expect these efforts to require the continued commitment of significant resources. Further, the members of our board of directors, members of our audit or compensation and management succession committees, our chief executive officer, our chief financial officer and certain other executive officers could face an increased risk of personal liability in connection with the performance of their duties. It may also become more difficult and more expensive to obtain director and officer liability insurance. As a result, our ability to attract and retain executive officers and qualified board and committee members could be more difficult.

We could be adversely affected by new regulations.

Federal and state governments and regulators could pass legislation and adopt policies responsive to current credit conditions that would have an adverse effect on the Company and its financial performance. For example, the Company could experience higher credit losses because of federal or state legislation or regulatory action that limits the Bank's ability to foreclose on property or other collateral or makes foreclosure less economically feasible.

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We could face increased deposit insurance costs.

The FDIC insures deposits at FDIC insured financial institutions up to certain limits. The FDIC charges insured financial institutions premiums to maintain the Deposit Insurance Fund. If the Deposit Insurance Fund suffers further losses, the FDIC could increase assessments rates or impose additional special assessments on the banking industry to replenish the Deposit Insurance Fund. The Company's profitability could be reduced by any increase in assessment rates or special assessments.

Risks Related to Growth and Expansion

If we cannot attract deposits, our growth may be inhibited.

We plan to increase the level of our assets, including our loan portfolio. Our ability to increase our assets depends in large part on our ability to attract additional deposits at favorable rates. We intend to seek additional deposits by offering deposit products that are competitive with those offered by other financial institutions in our markets and by establishing personal relationships with our customers. We cannot assure you that these efforts will be successful. Our inability to attract additional deposits at competitive rates could have a material adverse effect on our business, financial condition, results of operations and cash flows.

There are potential risks associated with future acquisitions and expansions.

We intend to continue to explore expanding our branch system through opening new bank branches and in-store branches in existing or new markets in northern and central California. In the ordinary course of business, we evaluate potential branch locations that would bolster our ability to cater to the small business, individual and residential lending markets in California. Any given new branch, if and when opened, will have expenses in excess of revenues for varying periods after opening that may adversely affect our results of operations or overall financial condition.

In addition, to the extent that we acquire other banks in the future, our business may be negatively impacted by certain risks inherent with such acquisitions. These risks include:

incurring substantial expenses in pursuing potential acquisitions without completing such acquisitions,

losing key clients as a result of the change of ownership,

the acquired business not performing in accordance with our expectations,

difficulties arising in connection with the integration of the operations of the acquired business with our operations,

needing to make significant investments and infrastructure, controls, staff, emergency backup facilities or other critical business functions that become strained by our growth,

management needing to divert attention from other aspects of our business,

potentially losing key employees of the acquired business,

incurring unanticipated costs which could reduce our earnings per share,

assuming potential liabilities of the acquired company as a result of the acquisition, and

an acquisition may dilute our earnings per share, in both the short and long term, or it may reduce our tangible capital ratios. As result of these risks, any given acquisition, if and when consummated, may adversely affect our results of operations or financial condition. In addition, because the consideration for an acquisition may involve cash, debt or the issuance of shares of our stock and may involve the payment of a premium over book and market values, existing shareholders may experience dilution in connection with any acquisition.

Our growth and expansion may strain our ability to manage our operations and our financial resources.

Our financial performance and profitability depend on our ability to execute our corporate growth strategy. In addition to seeking deposit and loan and lease growth in our existing markets, we may pursue expansion opportunities in new markets. Continued growth, however, may present operating and other problems that could adversely affect our business, financial condition, results of operations and cash flows. Accordingly, there can be no assurance that we will be able to execute our growth strategy or maintain the level of profitability that we have recently experienced.

Our growth may place a strain on our administrative, operational and financial resources and increase demands on our systems and controls. This business growth may require continued enhancements to and expansion of our operating and financial systems and controls and may strain or significantly challenge them. In addition, our existing operating and financial control systems and infrastructure may not be adequate to maintain and effectively monitor future growth. Our continued growth may also increase our need for qualified personnel. We cannot assure you that we will be successful in attracting, integrating and retaining such personnel.

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Our decisions regarding the fair value of assets acquired from Citizens and Granite, including the FDIC loss sharing assets associated with Granite, could be inaccurate which could materially and adversely affect our business, financial condition, results of operations, and future prospects.

Management makes various assumptions and judgments about the collectability of acquired loans, including the creditworthiness of borrowers and the value of the real estate and other assets serving as collateral for the repayment of secured loans. In FDIC-assisted acquisitions that include loss sharing agreements, such as our acquisition of Granite, we may record a loss sharing asset that we consider adequate to absorb future losses which may occur in the acquired loan portfolio. In determining the size of the loss sharing asset, we analyze the loan portfolio based on historical loss experience, volume and classification of loans, volume and trends in delinquencies and nonaccruals, local economic conditions, and other pertinent information.

If our assumptions are incorrect, the balance of the FDIC indemnification asset may at any time be insufficient to cover future loan losses, and credit loss provisions may be needed to respond to different economic conditions or adverse developments in the acquired loan portfolio. Any increase in future loan losses could have a negative effect on our operating results.

Our ability to obtain reimbursement under the loss sharing agreement on covered assets purchased from the FDIC depends on our compliance with the terms of the loss sharing agreement.

We must certify to the FDIC on a quarterly basis our compliance with the terms of the FDIC loss sharing agreement as a prerequisite to obtaining reimbursement from the FDIC for realized losses on covered assets. The required terms of the agreements are extensive and failure to comply with any of the guidelines could result in a specific asset or group of assets permanently losing their loss sharing coverage. Additionally, Management may decide to forgo loss share coverage on certain assets to allow greater flexibility over the management of certain assets. As of December 31, 2012, \$43,429,000, or 1.7%, of the Company's assets were covered by these FDIC loss sharing agreements.

Risks Relating to Dividends and Our Common Stock

Our future ability to pay dividends is subject to restrictions.

Since we are a holding company with no significant assets other than the Bank, we currently depend upon dividends from the Bank for a substantial portion of our revenues. Our ability to continue to pay dividends in the future will continue to depend in large part upon our receipt of dividends or other capital distributions from the Bank. The ability of the Bank to pay dividends or make other capital distributions to us is subject to the restrictions in the California Financial Code and the regulatory authority of the DFI. As of December 31, 2012, the Bank could have paid \$23,568,000 in dividends without the prior approval of the DFI. The amount that the Bank may pay in dividends is further restricted due to the fact that the Bank must maintain a certain minimum amount of capital to be considered a well capitalized institution as further described under Item 1 Capital Requirements in this report.

From time to time, we may become a party to financing agreements or other contractual arrangements that have the effect of limiting or prohibiting us or the Bank from declaring or paying dividends. Our holding company expenses and obligations with respect to our trust preferred securities and corresponding junior subordinated deferrable interest debentures issued by us may limit or impair our ability to declare or pay dividends. Finally, our ability to pay dividends is also subject to the restrictions of the California Corporations Code. See Regulation and Supervision Restrictions on Dividends and Distributions .

Only a limited trading market exists for our common stock, which could lead to price volatility.

Our common stock is quoted on the NASDAQ Global Select Market and trading volumes have been modest. The limited trading market for our common stock may cause fluctuations in the market value of our common stock to be exaggerated, leading to price volatility in excess of that which would occur in a more active trading market of our common stock. In addition, even if a more active market in our common stock develops, we cannot assure you that such a market will continue or that shareholders will be able to sell their shares.

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Anti-takeover provisions and federal law may limit the ability of another party to acquire us, which could cause our stock price to decline.

Various provisions of our articles of incorporation and bylaws could delay or prevent a third party from acquiring us, even if doing so might be beneficial to our shareholders. These provisions provide for, among other things:

specified actions that the Board of Directors shall or may take when an offer to merge, an offer to acquire all assets or a tender offer is received,

a shareholder rights plan which could deter a tender offer by requiring a potential acquiror to pay a substantial premium over the market price of our common stock,

advance notice requirements for proposals that can be acted upon at shareholder meetings, and

the authorization to issue preferred stock by action of the board of directors acting alone, thus without obtaining shareholder approval.

The BHC Act and the Change in Bank Control Act of 1978, as amended, together with federal regulations, require that, depending on the particular circumstances, either FRB approval must be obtained or notice must be furnished to the FRB and not disapproved prior to any person or entity acquiring control of a bank holding company such as TriCo. These provisions may prevent a merger or acquisition that would be attractive to shareholders and could limit the price investors would be willing to pay in the future for our common stock.

The amount of common stock owned by, and other compensation arrangements with, our officers and directors may make it more difficult to obtain shareholder approval of potential takeovers that they oppose.

As of December 31, 2012, directors and executive officers beneficially owned approximately 15.5% of our common stock and our ESOP owned approximately 8.6%. Agreements with our senior management also provide for significant payments under certain circumstances following a change in control. These compensation arrangements, together with the common stock and option ownership of our board of directors and management, could make it difficult or expensive to obtain majority support for shareholder proposals or potential acquisition proposals of us that our directors and officers oppose.

We may issue additional common stock or other equity securities in the future which could dilute the ownership interest of existing shareholders.

In order to maintain our capital at desired or regulatorily-required levels, or to fund future growth, our board of directors may decide from time to time to issue additional shares of common stock, or securities convertible into, exchangeable for or representing rights to acquire shares of our common stock. The sale of these shares may significantly dilute your ownership interest as a shareholder. New investors in the future may also have rights, preferences and privileges senior to our current shareholders which may adversely impact our current shareholders.

Holders of our junior subordinated debentures have rights that are senior to those of our common stockholders.

We have supported our continued growth through the issuance of trust preferred securities from special purpose trusts and accompanying junior subordinated debentures. At December 31, 2012, we had outstanding trust preferred securities and accompanying junior subordinated debentures totaling \$41,238,000. Payments of the principal and interest on the trust preferred securities are conditionally guaranteed by us. Further, the accompanying junior subordinated debentures we issued to the trusts are senior to our shares of common stock. As a result, we must make payments on the junior subordinated debentures before any dividends can be paid on our common stock and, in the event of our bankruptcy, dissolution or liquidation, the holders of the junior subordinated debentures must be satisfied before any distributions can be made on our common stock.

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Risks Relating to Systems, Accounting and Internal Controls

If we fail to maintain an effective system of internal and disclosure controls, we may not be able to accurately report our financial results or prevent fraud. As a result, current and potential shareholders could lose confidence in our financial reporting, which would harm our business and the trading price of our securities.

Effective internal control over financial reporting and disclosure controls and procedures are necessary for us to provide reliable financial reports and effectively prevent fraud and to operate successfully as a public company. If we cannot provide reliable financial reports or prevent fraud, our reputation and operating results would be harmed. We continually review and analyze our internal control over financial reporting for Sarbanes-Oxley Section 404 compliance. As part of that process we may discover material weaknesses or significant deficiencies in our internal control as defined under standards adopted by the Public Company Accounting Oversight Board that require remediation. Material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected in a timely basis. Significant deficiency is a deficiency or combination of deficiencies, in internal control over financial reporting that is less severe than material weakness, yet important enough to merit attention by those responsible for the oversight of the Company's financial reporting.

As a result of weaknesses that may be identified in our internal control, we may also identify certain deficiencies in some of our disclosure controls and procedures that we believe require remediation. If we discover weaknesses, we will make efforts to improve our internal and disclosure control. However, there is no assurance that we will be successful. Any failure to maintain effective controls or timely effect any necessary improvement of our internal and disclosure controls could harm operating results or cause us to fail to meet our reporting obligations, which could affect our ability to remain listed with The NASDAQ Global Select Market. Ineffective internal and disclosure controls could also cause investors to lose confidence in our reported financial information, which would likely have a negative effect on the trading price of our securities.

We rely on communications, information, operating and financial control systems technology and we may suffer an interruption in or breach of the security of those systems.

We rely heavily on our communications, information, operating and financial control systems technology to conduct our business. We rely on third party services providers to provide many of these systems. Any failure, interruption or breach in security of these systems could result in failures or interruptions in our customer relationship management, general ledger, deposit, servicing and loan origination systems. We cannot assure you that such failures, interruptions or security breaches will not occur or, if they do occur, that they will be adequately addressed by us or the third parties service providers on which we rely. The occurrence of any failures, interruptions or security breaches could damage our reputation, result in a loss of customers, expose us to possible financial liability, lead to additional regulatory scrutiny or require that we make expenditures for remediation or prevention. Any of these circumstances could have a material adverse effect on our business, financial condition, results of operations and cash flows.

A failure to implement technological advances could negatively impact our business.

The banking industry is undergoing technological changes with frequent introductions of new technology-driven products and services. In addition to improving customer services, the effective use of technology increases efficiency and enables financial institutions to reduce costs. Our future success will depend, in part, on our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands for convenience as well as to create additional efficiencies in our operations. Many of our competitors have substantially greater resources than we do to invest in technological improvements. We may not be able to effectively implement new technology-driven products and services or successfully market such products and services to our customers.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

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ITEM 2. PROPERTIES

The Company is engaged in the banking business through 66 offices in 23 counties in Northern and Central California including ten offices in Shasta County, nine in Butte County, seven in Sacramento and Nevada Counties, six in Placer County, four in Stanislaus County, three each in Siskiyou, Sutter and Kern Counties, two each in Glenn and Yolo Counties, and one each in Contra Costa, Del Norte, Fresno, Lake, Lassen, Madera, Mendocino, Merced, Napa, Tehama, Tulare, and Yuba Counties. All offices are constructed and equipped to meet prescribed security requirements.

The Company owns eighteen branch office locations, four administrative buildings, and two other buildings that it leases out. The Company leases forty-eight branch office locations, and three administrative buildings. Most of the leases contain multiple renewal options and provisions for rental increases, principally for changes in the cost of living index, property taxes and maintenance.

ITEM 3. LEGAL PROCEEDINGS

The Bank owns 10,214 shares of Class B common stock of Visa Inc. which are convertible into Class A common stock at a conversion ratio of 0.4206 per Class A share. As of December 31, 2012, the value of the Class A shares was \$151.58 per share. Utilizing the conversion ratio, the value of unredeemed Class A equivalent shares owned by the Bank was \$651,000 as of December 31, 2012, and has not been reflected in the accompanying financial statements. The shares of Visa Class B common stock are restricted and may not be transferred. Visa Member Banks are required to fund an escrow account to cover settlements, resolution of pending litigation and related claims. If the funds in the escrow account are insufficient to settle all the covered litigation, Visa may sell additional Class A shares, use the proceeds to settle litigation, and further reduce the conversion ratio. If funds remain in the escrow account after all litigation is settled, the Class B conversion ratio will be increased to reflect that surplus.

On September 27, 2012, the Company announced that the Bank entered into a tentative settlement with a former employee who filed a class action lawsuit against the Bank in the Superior Court of California, Kern County on behalf of herself and a putative class of current and former Bank employees serving as assistant branch managers seeking undisclosed damages, alleging that the Bank improperly classified its assistant branch managers as exempt employees under California laws. The lawsuit alleges claims for: failure to pay overtime compensation; failure to provide meal periods; failure to provide rest periods; failure to provide accurate wage statements; failure to provide suitable seating; declaratory relief; accounting; and unfair business practices in violation of California Business and Professions Code section 17200.

On September 26, 2012, after efforts to mediate the claim, the Bank and the former employee agreed to settle the case in an amount ranging from \$2,039,500 to \$2,500,000, depending primarily on the number of class participants who file claims, and pending approval by the court, including determination of the method to allocate settlement payments among current and former employees who are members of the defined settlement class, and the portion of the total settlement allocable to attorney's fees and costs to plaintiff's counsel. On September 26, 2012, the Bank recorded a \$2,090,000 expense and accrued liability in anticipation of approval of this settlement by the court and estimated related payroll taxes.

Neither the Company nor its subsidiaries, are party to any other material pending legal proceeding, nor is their property the subject of any material pending legal proceeding, except routine legal proceedings arising in the ordinary course of their business. None of these proceedings is expected to have a material adverse impact upon the Company's business, consolidated financial position or results of operations.

ITEM 4. MINE SAFETY DISCLOSURES

Inapplicable.

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The Company's common stock is traded on the NASDAQ Global Select Market System (NASDAQ) under the symbol TCBK. The following table shows the high and the low closing sale prices for the common stock for each quarter in the past two years, as reported by NASDAQ:

2012:	High	Low
Fourth quarter	\$ 17.14	\$ 14.73
Third quarter	\$ 16.81	\$ 14.76
Second quarter	\$ 17.71	\$ 14.84
First quarter	\$ 17.67	\$ 14.22
2011:		
Fourth quarter	\$ 15.32	\$ 11.58
Third quarter	\$ 15.50	\$ 11.75
Second quarter	\$ 16.58	\$ 13.18
First quarter	\$ 16.76	\$ 14.53

As of March 1, 2013 there were approximately 1,459 shareholders of record of the Company's common stock. On March 1, 2013, the closing sales price was \$17.01.

The Company has paid cash dividends on its common stock in every quarter since March 1990, and it is currently the intention of the Board of Directors of the Company to continue payment of cash dividends on a quarterly basis. There is no assurance, however, that any dividends will be paid since they are dependent upon earnings, financial condition and capital requirements of the Company and the Bank. As of December 31, 2012, \$23,568,000 was available for payment of dividends by the Bank to the Company, under applicable laws and regulations. The Company paid cash dividends of \$0.09 per common share in each of the quarters ended December 31, 2012, September 30, 2012, June 30, 2012, March 31, 2012, December 31, 2011, September 30, 2011, June 30, 2011, and March 31, 2011.

Stock Repurchase Plan

The Company adopted a stock repurchase plan on August 21, 2007 for the repurchase of up to 500,000 shares of the Company's common stock from time to time as market conditions allow. The 500,000 shares authorized for repurchase under this plan represented approximately 3.2% of the Company's approximately 15,815,000 common shares outstanding as of August 21, 2007. This plan has no stated expiration date for the repurchases. As of December 31, 2012, the Company had purchased 166,600 shares under this plan. The following table shows the repurchases made by the Company or any affiliated purchaser (as defined in Rule 10b-18(a)(3) under the Exchange Act) during the fourth quarter of 2012:

Period	(a) Total number of shares purchased	(b) Average price paid per share	(c) Total number of shares purchased as of part of publicly announced plans or programs	(d) Maximum number shares that may yet be purchased under the plans or programs
Oct. 1-31, 2012				333,400
Nov. 1-30, 2012				333,400
Dec. 1-31, 2012				333,400

Total

333,400

20

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The following graph presents the cumulative total yearly shareholder return from investing \$100 on December 31, 2007, in each of TriCo common stock, the Russell 3000 Index, and the SNL Western Bank Index. The SNL Western Bank Index compiled by SNL Financial includes banks located in California, Oregon, Washington, Montana, Hawaii and Alaska with market capitalization similar to that of TriCo's. The amounts shown assume that any dividends were reinvested.

TriCo Bancshares

Index	Period Ending					
	12/31/07	12/31/08	12/31/09	12/31/10	12/31/11	12/31/12
TriCo Bancshares	100.00	133.14	91.73	91.15	82.34	99.17
Russell 3000	100.00	62.69	80.46	94.08	95.05	110.65
SNL Western Bank	100.00	97.37	89.41	101.31	91.53	115.50

Equity Compensation Plans

The following table shows shares reserved for issuance for outstanding options, stock appreciation rights and warrants granted under our equity compensation plans as of December 31, 2012. All of our equity compensation plans have been approved by shareholders.

Plan category	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights	(b) Weighted average exercise price of outstanding options, warrants and rights	(c) Number of securities remaining available for issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans not approved by shareholders			
Equity compensation plans approved by shareholders	1,393,935	\$ 17.07	72,000
Total	1,393,935	\$ 17.07	72,000

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The following selected consolidated financial data are derived from our consolidated financial statements. This data should be read in connection with our consolidated financial statements and the related notes located at Item 8 of this report.

TRICO BANCSHARES**Financial Summary**

(in thousands, except per share amounts)

Year ended December 31,	2012	2011	2010	2009	2008
Interest income	\$ 108,716	\$ 102,982	\$ 104,572	\$ 112,333	\$ 121,112
Interest expense	7,344	10,238	14,133	20,615	31,552
Net interest income	101,372	92,744	90,439	91,718	89,560
Provision for loan losses	9,423	23,060	37,458	31,450	20,950
Noninterest income	37,980	42,813	32,695	30,329	27,087
Noninterest expense	97,998	82,715	77,205	75,450	68,738
Income before income taxes	31,931	29,782	8,471	15,147	26,959
Provision for income taxes	12,937	11,192	2,466	5,185	10,161
Net income	\$ 18,994	\$ 18,590	\$ 6,005	\$ 9,962	\$ 16,798
Earnings per share:					
Basic	\$ 1.19	\$ 1.17	\$ 0.38	\$ 0.63	\$ 1.07
Diluted	\$ 1.18	\$ 1.16	\$ 0.37	\$ 0.62	\$ 1.05
Per share:					
Dividends paid	\$ 0.36	\$ 0.36	\$ 0.40	\$ 0.52	\$ 0.52
Book value at December 31	\$ 14.33	\$ 13.55	\$ 12.64	\$ 12.71	\$ 12.56
Tangible book value at December 31	\$ 13.30	\$ 12.49	\$ 11.62	\$ 11.71	\$ 11.54
Average common shares outstanding	15,988	15,935	15,860	15,783	15,771
Average diluted common shares outstanding	16,052	16,000	16,010	16,011	16,050
Shares outstanding at December 31	16,001	15,979	15,860	15,787	15,756
At December 31:					
Loans, net of allowance	\$ 1,522,175	\$ 1,505,118	\$ 1,377,000	\$ 1,460,097	\$ 1,563,259
Total assets	2,609,269	2,555,597	2,189,789	2,170,520	2,043,190
Total deposits	2,289,702	2,190,536	1,852,173	1,828,512	1,669,270
Debt financing and notes payable	9,197	72,541	62,020	66,753	102,005
Junior subordinated debt	41,238	41,238	41,238	41,238	41,238
Shareholders' equity	229,359	216,441	200,397	200,649	197,932
Financial Ratios:					
For the year:					
Return on average assets	0.75%	0.82%	0.27%	0.48%	0.85%
Return on average equity	8.44%	8.93%	2.94%	4.89%	8.70%
Net interest margin ¹	4.32%	4.43%	4.45%	4.77%	4.96%
Net loan losses to average loans	0.82%	1.37%	2.07%	1.53%	0.69%
Efficiency ratio ¹	70.19%	60.88%	62.49%	61.53%	58.59%
Average equity to average assets	8.91%	9.15%	9.25%	9.73%	9.72%

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At December 31:					
Equity to assets	8.79%	8.47%	9.15%	9.24%	9.69%
Total capital to risk-adjusted assets	14.53%	13.94%	14.20%	13.36%	12.42%

¹ Fully taxable equivalent

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As TriCo Bancshares (referred to in this report as we, our or the Company) has not commenced any business operations independent of Tri Counties Bank (the Bank), the following discussion pertains primarily to the Bank. Average balances, including such balances used in calculating certain financial ratios, are generally comprised of average daily balances for the Company. Within Management's Discussion and Analysis of Financial Condition and Results of Operations, interest income and net interest income are generally presented on a fully tax-equivalent (FTE) basis. The presentation of interest income and net interest income on a FTE basis is a common practice within the banking industry. Interest income and net interest income are shown on a non-FTE basis in the Part I Financial Information section of this Form 10-Q, and a reconciliation of the FTE and non-FTE presentations is provided below in the discussion of net interest income.

Critical Accounting Policies and Estimates

The Company's discussion and analysis of its financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates, including those that materially affect the financial statements and are related to the adequacy of the allowance for loan losses, investments, mortgage servicing rights, fair value measurements, retirement plans and intangible assets. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. The Company's policies related to estimates on the allowance for loan losses, other than temporary impairment of investments and impairment of intangible assets, can be found in Note 1 in the financial statements at Item 8 of this report.

As the Company has not commenced any business operations independent of the Bank, the following discussion pertains primarily to the Bank. Average balances, including balances used in calculating certain financial ratios, are generally comprised of average daily balances for the Company. Within Management's Discussion and Analysis of Financial Condition and Results of Operations, certain performance measures including interest income, net interest income, net interest yield, and efficiency ratio are generally presented on a fully tax-equivalent (FTE) basis. The Company believes the use of these non-generally accepted accounting principles (non-GAAP) measures provides additional clarity in assessing its results.

On September 23, 2011, the California Department of Financial Institutions closed Citizens Bank of Northern California (Citizens), Nevada City, California and appointed the FDIC as receiver. That same date, the Bank assumed the banking operations of Citizens from the FDIC under a whole bank purchase and assumption agreement without loss sharing. With this agreement, the Bank added seven traditional bank branches including two in Grass Valley, and one in each of Nevada City, Penn Valley, Lake of the Pines, Truckee, and Auburn, California. This acquisition is consistent with the Bank's community banking expansion strategy and provides further opportunity to fill in the Bank's market presence in the Northern California market.

On May 28, 2010, the Office of the Comptroller of the Currency closed Granite Community Bank (Granite), Granite Bay, California and appointed the FDIC as receiver. That same date, the Bank assumed the banking operations of Granite from the FDIC under a whole bank purchase and assumption agreement with loss sharing. Under the terms of the loss sharing agreement, the FDIC will cover a substantial portion of any future losses on loans, related unfunded loan commitments, other real estate owned (OREO)/foreclosed assets and accrued interest on loans for up to 90 days. The FDIC will absorb 80% of losses and share in 80% of loss recoveries on the covered assets acquired from Granite. The loss sharing arrangements for non-single family residential and single family residential loans are in effect for 5 years and 10 years, respectively, and the loss recovery provisions are in effect for 8 years and 10 years, respectively, from the acquisition date. With this agreement, the Bank added one traditional bank branch in each of Granite Bay and Auburn, California. This acquisition is consistent with the Bank's community banking expansion strategy and provides further opportunity to fill in the Bank's market presence in the greater Sacramento, California market.

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The Company refers to loans and foreclosed assets that are covered by loss sharing agreements as covered loans and covered foreclosed assets, respectively. In addition, the Company refers to loans purchased or obtained in a business combination as purchased credit impaired (PCI) loans, or purchased non-credit impaired (PNCI) loans. The Company refers to loans that it originates as originated loans. Additional information regarding the Citizens and Granite Bank acquisitions can be found in Note 2 in the financial statements at Item 8 of this report. Additional information regarding the definitions and accounting for originated, PNCI and PCI loans can be found in Notes 1, 2, 4 and 5 in the financial statements at Item 8 of this report, and under the heading *Asset Quality and Non-Performing Assets* below.

Geographical Descriptions

For the purpose of describing the geographical location of the Company's loans, the Company has defined northern California as that area of California north of, and including, Stockton; central California as that area of the State south of Stockton, to and including, Bakersfield; and southern California as that area of the State south of Bakersfield.

Results of Operations**Overview**

The following discussion and analysis is designed to provide a better understanding of the significant changes and trends related to the Company and the Bank's financial condition, operating results, asset and liability management, liquidity and capital resources and should be read in conjunction with the consolidated financial statements of the Company and the related notes at Item 8 of this report.

Following is a summary of the components of net income for the periods indicated (dollars in thousands):

Components of Net Income	Year ended December 31,		
	2012	2011	2010
Net interest income	\$ 101,372	\$ 92,744	\$ 90,439
Provision for loan losses	(9,423)	(23,060)	(37,458)
Noninterest income	37,980	42,813	32,695
Noninterest expense	(97,998)	(82,715)	(77,205)
Taxes	(12,937)	(11,192)	(2,466)
Net income	\$ 18,994	\$ 18,590	\$ 6,005
Net income per average fully-diluted share	\$ 1.18	\$ 1.16	\$ 0.37
Net income as a percentage of average shareholders' equity	8.44%	8.93%	2.94%
Net income as a percentage of average total assets	0.75%	0.82%	0.27%

Net Interest Income

The Company's primary source of revenue is net interest income, which is the difference between interest income on earning assets and interest expense on interest-bearing liabilities.

Following is a summary of the Company's net interest income for the periods indicated (dollars in thousands):

Components of Net Interest Income	Year ended December 31,		
	2012	2011	2010
Interest income	\$ 108,716	\$ 102,982	\$ 104,572
Interest expense	(7,344)	(10,238)	(14,133)
Net interest income	101,372	92,744	90,439

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FTE adjustment	257	309	413
Net interest income (FTE)	\$ 101,629	\$ 93,053	\$ 90,852
Net interest margin (FTE)	4.32%	4.43%	4.45%

Net interest income (FTE) for the year ended December 31, 2012 was \$101,629,000, an increase of \$8,576,000 or 9.2% compared to the year ended December 31, 2011. The increase in net interest income during 2012 when compared to 2011 is mainly due to the acquisition of Citizens on September 23, 2011 and its associated net interest income of \$17,852,000 during 2012 compared to \$6,117,000 from September 23, 2011 to December 31, 2011. Included in the net interest income associated with the Citizens acquisition is \$7,572,000 and \$3,146,000 from the accretion of loan purchase discounts during 2012 and 2011, respectively. Also contributing to the increase in net interest income was a reduction in deposit rates, the flow of deposits from relatively higher paying time deposits to lower paying non-maturity deposits, and the reduction of relatively high cost other borrowings. During 2012, investment opportunities continued to be unattractive given their low market yields and interest rate risk profile. The Yield and Volume/Rate tables shown below are useful in illustrating and quantifying the developments that affected net interest income during 2012.

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Net interest income (FTE) for the year ended December 31, 2011 was \$93,053,000, an increase of \$2,201,000 or 2.4% compared to the year ended December 31, 2010. The increase in net interest income during 2011 when compared to 2010 is mainly due to the acquisition of Citizens on September 23, 2011 and its associated net interest income of \$6,117,000 from September 23, 2011 to December 31, 2011. Included in the net interest income associated with the Citizens acquisition is \$3,146,000 from the accretion of loan purchase discounts. Also contributing to the increase in net interest income was a reduction in deposit rates and the flow of deposits from relatively higher paying time deposits to lower paying non-maturity deposits. Partially offsetting the increase in net interest income related to the Citizens acquisition and the deposit rate and volume changes were organic loan payoffs in excess of loan production during 2011. These loan payoffs in excess of loan production and deposit growth during 2011 were deployed into lower yielding short-term interest-earning balances at the Federal Reserve Bank. During 2011, investment opportunities continued to be unattractive given their low market yields and interest rate risk profile.

Summary of Average Balances, Yields/Rates and Interest Differential Yield Tables

The following tables present, for the periods indicated, information regarding the Company's consolidated average assets, liabilities and shareholders' equity, the amounts of interest income from average earning assets and resulting yields, and the amount of interest expense paid on interest-bearing liabilities. Average loan balances include nonperforming loans. Interest income includes proceeds from loans on nonaccrual loans only to the extent cash payments have been received and applied to interest income. Yields on securities and certain loans have been adjusted upward to reflect the effect of income thereon exempt from federal income taxation at the current statutory tax rate (dollars in thousands):

	Year ended December 31, 2012		
	Average balance	Interest income/expense	Rates earned/paid
Assets			
Loans	\$ 1,552,540	\$ 100,496	6.47%
Investment securities - taxable	200,958	6,177	3.07%
Investment securities - nontaxable	9,529	685	7.19%
Cash at Federal Reserve and other banks	587,118	1,615	0.28%
Total earning assets	2,350,145	108,973	4.64%
Other assets	176,927		
Total assets	\$ 2,527,072		
Liabilities and shareholders' equity			
Interest-bearing demand deposits	\$ 471,747	784	0.17%
Savings deposits	763,065	1,212	0.16%
Time deposits	372,698	2,420	0.65%
Other borrowings	45,753	1,604	3.51%
Junior subordinated debt	41,238	1,324	3.21%
Total interest-bearing liabilities	1,694,501	7,344	0.43%
Noninterest-bearing demand	572,568		
Other liabilities	34,852		
Shareholders' equity	225,151		
Total liabilities and shareholders' equity	\$ 2,527,072		
Net interest spread ⁽¹⁾			4.21%
Net interest income and interest margin ⁽²⁾		\$ 101,629	4.32%

- (1) Net interest spread represents the average yield earned on interest-earning assets less the average rate paid on interest-bearing liabilities.
- (2) Net interest margin is computed by dividing net interest income by total average earning assets.

Table of Contents**Summary of Average Balances, Yields/Rates and Interest Differential Yield Tables (continued)**

	Year ended December 31, 2011		
	Average balance	Interest income/expense	Rates earned/paid
Assets			
Loans	\$ 1,442,821	\$ 92,691	6.42%
Investment securities taxable	262,306	8,760	3.34%
Investment securities nontaxable	11,403	833	7.31%
Cash at Federal Reserve and other banks	386,067	1,007	0.26%
Total earning assets	2,102,597	103,291	4.91%
Other assets	173,311		
Total assets	\$ 2,275,908		
Liabilities and shareholders' equity			
Interest-bearing demand deposits	\$ 410,870	\$ 1,217	0.30%
Savings deposits	661,480	1,421	0.21%
Time deposits	415,319	3,921	0.94%
Other borrowings	63,602	2,420	3.80%
Junior subordinated debt	41,238	1,259	3.05%
Total interest-bearing liabilities	1,592,509	10,238	0.64%
Noninterest-bearing demand	442,174		
Other liabilities	33,005		
Shareholders' equity	208,220		
Total liabilities and shareholders' equity	\$ 2,275,908		
Net interest spread ⁽¹⁾			4.27%
Net interest income and interest margin ⁽²⁾		\$ 93,053	4.43%

	Year ended December 31, 2010		
	Average balance	Interest income/expense	Rates earned/paid
Assets			
Loans	\$ 1,464,606	\$ 93,073	6.35%
Investment securities taxable	263,059	10,039	3.82%
Investment securities nontaxable	14,717	1,113	7.56%
Cash at Federal Reserve and other banks	296,970	760	0.26%
Total earning assets	2,039,352	104,985	5.15%
Other assets	169,290		
Total assets	\$ 2,208,642		

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Liabilities and shareholders' equity			
Interest-bearing demand deposits	\$ 384,077	2,242	0.58%
Savings deposits	552,104	2,277	0.41%
Time deposits	544,018	5,928	1.09%
Other borrowings	62,110	2,412	3.88%
Junior subordinated debt	41,238	1,274	3.09%
Total interest-bearing liabilities	1,583,547	14,133	0.89%
Noninterest-bearing demand	385,704		
Other liabilities	35,196		
Shareholders' equity	204,195		
Total liabilities and shareholders' equity	\$ 2,208,642		
Net interest spread ⁽¹⁾			4.26%
Net interest income and interest margin ⁽²⁾		\$ 90,852	4.45%

- (1) Net interest spread represents the average yield earned on interest-earning assets less the average rate paid on interest-bearing liabilities.
- (2) Net interest margin is computed by dividing net interest income by total average earning assets.

Table of Contents**Summary of Changes in Interest Income and Expense due to Changes in Average Asset and Liability Balances and Yields Earned and Rates Paid Volume/Rate Tables**

The following table sets forth a summary of the changes in the Company's interest income and interest expense from changes in average asset and liability balances (volume) and changes in average interest rates for the periods indicated. The rate/volume variance has been included in the rate variance. Amounts are calculated on a fully taxable equivalent basis:

	2012 over 2011			2011 over 2010		
	Volume	Rate	Total (dollars in thousands)	Volume	Yield/ Rate	Yield/ Total
Increase (decrease) in interest income:						
Loans	\$ 7,044	\$ 761	\$ 7,805	\$ (1,383)	\$ 1,001	\$ (382)
Investments taxable	(2,049)	(534)	(2,583)	(29)	(1,250)	(1,279)
Investments nontaxable	(137)	(11)	(148)	(251)	(29)	(280)
Cash at Federal Reserve and other banks	523	85	608	232	15	247
Total	5,381	301	5,682	(1,431)	(263)	(1,694)
Increase (decrease) in interest expense:						
Demand deposits (interest-bearing)	183	(616)	(433)	155	(1,180)	(1,025)
Savings deposits	213	(422)	(209)	448	(1,304)	(856)
Time deposits	(401)	(1,100)	(1,501)	(1,403)	(604)	(2,007)
Other borrowings	(678)	(138)	(816)	58	(50)	8
Junior subordinated debt		65	65		(15)	(15)
Total	(683)	(2,211)	(2,894)	(742)	(3,153)	(3,895)
Increase (decrease) in net interest income	\$ 6,064	\$ 2,512	\$ 8,576	\$ (689)	\$ 2,890	\$ 2,201

Provision for Loan Losses

The provision for loan losses was \$9,423,000 and \$23,060,000 for the years ended December 31, 2012, and 2011, respectively. The decreases in the provision for loan losses for the year ended December 31, 2012 as compared to the year ended December 31, 2011 was primarily the result of improvement in collateral values and estimated cash flows related to nonperforming loans and purchased credit impaired loans, and a reduction in nonperforming loans.

The provision for loan losses was \$23,060,000 and \$37,458,000 for the years ended December 31, 2011, and 2010, respectively. The decreases in the provision for loan losses for the year ended December 31, 2011 as compared to the year ended December 31, 2010 was primarily the result of changes in the make-up of the originated loan portfolio and the Bank's loss factors related to the originated loan portfolio in reaction to decreased losses in the construction, commercial real estate, commercial & industrial (C&I), home equity and auto indirect loan portfolios. Included in the provision for loan losses for the year ended December 31, 2011 is \$1,562,000 related to loans acquired in the Citizens acquisition and \$1,248,000 related to loans acquired in the Granite acquisition.

Management re-evaluates the loss ratios and assumptions of its originated and PNCI loan portfolios and makes changes as appropriate based upon, among other things, changes in loss rates experienced, collateral support for underlying loans, changes and trends in the economy, and changes in the loan mix. Management also re-evaluates expected cash flows for its PCI loan portfolio quarterly and makes changes as appropriate based upon, among other things, changes in loan repayment experience, changes in loss rates experienced, and collateral support for underlying loans.

The provision for loan losses related to originated and PNCI loans is based on management's evaluation of inherent risks in these loan portfolios and a corresponding analysis of the allowance for loan losses. The provision for loan losses related to PCI loan portfolio is based on changes in estimated cash flows expected to be collected on PCI loans. Additional discussion on loan quality, our procedures to measure loan impairment, and the allowance for loan losses is provided under the heading *Asset Quality and Non-Performing Assets* below.

Table of Contents**Noninterest Income**

The following table summarizes the Company's noninterest income for the periods indicated (dollars in thousands):

	Year ended December 31,		
	2012	2011	2010
Components of Noninterest Income			
Service charges on deposit accounts	\$ 14,290	\$ 14,776	\$ 15,296
ATM fees and interchange	7,762	7,058	6,078
Other service fees	2,223	1,722	1,452
Mortgage banking service fees	1,666	1,495	1,303
Change in value of mortgage servicing rights	(2,016)	(1,107)	(1,029)
Total service charges and fees	23,925	23,944	23,100
Gain on sale of loans	6,810	3,037	3,647
Commissions on sale of nondeposit investment products	3,209	2,105	1,209
Increase in cash value of life insurance	1,820	1,885	1,847
Change in indemnification asset	(286)	2,059	1,274
Gain on disposition of foreclosed assets	786	680	562
Legal settlement			400
Bargain purchase gain		7,575	232
Gain on life insurance death benefit	675	789	
Other noninterest income	1,041	739	424
Total noninterest income	\$ 37,980	\$ 42,813	\$ 32,695

Noninterest income decreased \$4,833,000 (11.3%) to \$37,980,000 in 2012. Excluding bargain purchase gains and gain on life insurance death benefits, noninterest income would have increased \$2,856,000 (8.3%) to \$37,305,000 in 2012 from \$34,449,000 in 2011. Service charges on deposit accounts were down \$486,000 (3.3%) due to reduced customer overdrafts and a resulting decrease in non-sufficient funds fees. ATM fees and interchange income was up \$704,000 (10.0%) due to increased customer point-of-sale transactions that are the result of incentives for such usage. Overall, mortgage banking activities, which includes mortgage banking servicing fees, change in value of mortgage servicing rights, and gain on sale of loans, accounted for \$6,460,000 of noninterest income in the 2012 compared to \$3,425,000 in 2011. This \$3,035,000 (88.6%) increase in mortgage banking related revenue is mainly due to historically low mortgage rates, an associated level of mortgage refinance activity, and the Bank's focus of resources in this area. Commissions on sale of nondeposit investment products increased \$1,104,000 (52.4%) in 2012 due to the Bank's focus of resources in this area. The change in indemnification asset from \$2,059,000 in 2011 to (\$286,000) in 2012 primarily due to a decrease in estimated loan losses from the loan portfolio and foreclosed assets acquired in the Granite acquisition on May 28, 2010, and the fact that such losses are generally covered at the rate of 80% by the FDIC. The actual decrease in estimated losses is reflected in increased interest income, decreased provision for loan losses and/or decreased provision for foreclosed asset losses. The operations of Citizens during 2012 added \$2,585,000 to noninterest income.

Noninterest income increased \$10,118,000 (30.9%) to \$42,813,000 in 2011. Service charges on deposit accounts were down \$520,000 (3.4%) due to new overdraft regulations that became effective on July 1, 2010 and caused a decrease in non-sufficient funds fees. ATM fees and interchange income was up \$980,000 (16.1%) due to increased customer point-of-sale transactions that are the result of incentives for such usage. Overall, mortgage banking activities, which includes mortgage banking servicing fees, change in value of mortgage servicing rights, and gain on sale of loans, accounted for \$3,425,000 of noninterest income in the 2011 compared to \$3,921,000 in 2010. Commissions on sale of nondeposit investment products increased \$896,000 (74.1%) in 2011 due to increased focus and resources deployed in that area. The change in indemnification asset of \$2,059,000 recorded in 2011 is primarily due to an increase in estimated loan losses from the loan portfolio and foreclosed assets acquired in the Granite acquisition on May 28, 2010, and the fact that such losses are generally covered at the rate of 80% by the FDIC. The actual increase in estimated losses is reflected in decreased interest income, increased provision for loan losses and/or increased provision for foreclosed asset losses. The September 23, 2011 acquisition of Citizens added noninterest income totaling \$8,029,000 through December 31, 2011 including a bargain purchase gain of \$7,575,000. Also during 2011, the Company recorded a \$789,000 gain on life insurance death benefit due to the passing of an insured former employee.

Table of Contents**Noninterest Expense**

The following table summarizes the Company's other noninterest expense for the periods indicated (dollars in thousands):

	Year ended December 31,		
	2012	2011	2010
Components of Noninterest Expense			
Salaries and related benefits:			
Base salaries, net of deferred loan origination costs	\$ 33,093	\$ 29,753	\$ 28,255
Incentive compensation	5,138	3,735	1,844
Benefits and other compensation costs	11,721	10,715	10,006
Total salaries and related benefits	49,952	44,203	40,105
Other noninterest expense:			
Occupancy	7,263	6,198	5,717
Equipment	4,444	3,770	3,975
Data processing and software	4,793	3,980	3,163
Assessments	2,393	2,491	3,253
ATM network charges	2,390	1,939	1,851
Advertising	2,876	2,649	2,340
Professional fees	2,709	2,004	2,478
Telecommunications	2,250	1,875	1,817
Postage	920	935	1,037
Courier service	1,013	953	826
Foreclosed asset expense	1,474	755	625
Intangible amortization	209	177	307
Operational losses	787	600	394
Provision for foreclosed asset losses	1,728	1,984	1,522
Change in reserve for unfunded commitments	875	100	(1,000)
Legal settlement	2,090		
Other	9,832	8,102	8,795
Total other noninterest expenses	48,046	38,512	37,100
Total noninterest expense	\$ 97,998	\$ 82,715	\$ 77,205
Average full time equivalent staff	737	687	667
Noninterest expense to revenue (FTE)	70.2%	60.9%	62.5%

Salary and benefit expenses increased \$5,749,000 (13.0%) to \$49,952,000 in 2012 compared to 2011. Base salaries increased \$3,340,000 (11.2%) to \$33,093,000 in 2012. The increase in base salaries was mainly due to a 50 FTE (7.3%) increase in average full time equivalent staff to 737 during 2012, and annual merit increases. Incentive and commission related salary expenses increased \$1,403,000 (37.6%) to \$5,138,000 in 2012 due primarily to increases in commissions related to loan production and nondeposit investment product fee production. Benefits expense, including retirement, medical and workers' compensation insurance, and taxes, increased \$1,006,000 (9.4%) to \$11,721,000 during 2012. The operations of Citizens added \$2,452,000 and \$751,000 to salaries and benefits expense for the year ended December 31, 2012, and the period from September 23, 2011 to December 31, 2011, respectively.

Salary and benefit expenses increased \$4,098,000 (10.2%) to \$44,203,000 in 2011 compared to 2010. Base salaries increased \$1,498,000 (5.3%) to \$29,753,000 in 2011. The increase in base salaries was mainly due to 3.0% increase in average full time equivalent staff and annual merit increases. Incentive and commission related salary expenses increased \$1,891,000 (103%) to \$3,735,000 in 2011 due primarily to increases in management bonuses and other incentives tied to net income. Benefits expense, including retirement, medical and workers' compensation insurance, and taxes, increased \$709,000 (7.1%) to \$10,715,000 during 2011. Included in benefits expense in 2011 was employee stock option expense of \$636,000 compared to \$550,000 in 2010.

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Other noninterest expenses increased \$9,534,000 (24.8%) to \$48,046,000 in 2012. The operations of Citizens added \$3,333,000 to other noninterest expense during 2012, compared to \$1,114,000 from September 23, 2011 to December 31, 2011. Changes in the various categories of other noninterest expense are reflected in the table above. The changes are indicative of the economic environment which has lead to increases in professional loan collection expenses, provision for foreclosed asset losses, and foreclosed asset expenses. Occupancy expense increased primarily due to seven branches and one admin facility acquired in the Citizens acquisition on September 23, 2011. The increase in change in reserve for unfunded commitments during 2012 is primarily due to increased unfunded construction loan commitments during the three months ended December 31, 2012. The legal settlement expense of \$2,090,000 noted for 2012 was previously disclosed on September 27, 2012, and is further described at Item 3 Legal Proceedings of this report.

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Other noninterest expenses increased \$1,412,000 (3.8%) to \$38,512,000 in 2011. The operations of Citizens from September 23, 2011 to December 31, 2011 added \$1,114,000 to other noninterest expense. Changes in the various categories of other noninterest expense are reflected in the table above. The changes are indicative of the economic environment which has led to increases in professional loan collection expenses, provision for foreclosed asset losses, and foreclosed asset expenses. Occupancy expense increased primarily due to seven branches and one admin facility acquired in the Citizens acquisition on September 23, 2011, and two branches acquired in the Granite acquisition on May 28, 2010. Included in the \$1,114,000 of Citizens related other noninterest expense were \$296,000 of provision for foreclosed assets expense and \$271,000 of information systems expense including system conversion expense as the Company has begun work to convert the Citizens systems to the Company's systems. Partially offsetting these increases was a \$762,000 decrease in regulatory and deposit insurance assessments.

Income Taxes

The effective tax rate on income was 40.5%, 37.6%, and 29.1% in 2012, 2011, and 2010, respectively. The effective tax rate was greater than the federal statutory tax rate due to state tax expense of \$3,277,000, \$2,845,000, and \$543,000, respectively, in these years. Tax-exempt income of \$428,000, \$514,000, and \$700,000, respectively, from investment securities, and \$2,495,000, \$2,674,000, and \$1,847,000, respectively, from increase in cash value and gain on death benefit of life insurance in these years helped to reduce the effective tax rate.

Financial Condition**Investment Securities**

During 2012 the Company did not sell any investment securities. During 2012 the Company received proceeds from maturities of securities totaling \$76,764,000, and used \$13,815,000 to purchase securities. During 2011 the Company did not sell any investment securities. During 2011 the Company received proceeds from maturities of securities totaling \$84,016,000, and used \$25,456,000 to purchase securities. The following table shows the Company's investment securities balances at the dates indicated:

(dollars in thousands)	Year ended December 31,				
	2012	2011	2010	2009	2008
Securities Available-for-sale:					
Obligations of US government corporations and agencies	\$ 151,701	\$ 217,384	\$ 264,181	\$ 193,130	\$ 242,977
Obligations of states and political subdivisions	9,421	10,028	12,541	17,953	22,665
Corporate bonds	1,905	1,811	549	539	919
Total investment securities	\$ 163,027	\$ 229,223	\$ 277,271	\$ 211,622	\$ 266,561

Additional information about the investment portfolio is provided in Note 3 in the financial statements at Item 8 of this report.

Restricted Equity Securities

Restricted equity securities were \$9,647,000 at December 31, 2012 and \$10,610,000 at December 31, 2011. The entire balance of restricted equity securities at December 31, 2012 and December 31, 2011 represents the Bank's investment in the Federal Home Loan Bank of San Francisco (FHLB). The decrease of \$963,000 is attributable to the redemption of \$963,000 of FHLB stock.

FHLB stock is carried at par and does not have a readily determinable fair value. While technically these are considered equity securities, there is no market for the FHLB stock. Therefore, the shares are considered as restricted investment securities. Management periodically evaluates FHLB stock for other-than-temporary impairment. Management's determination of whether these investments are impaired is based on its assessment of the ultimate recoverability of cost rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability of cost is influenced by criteria such as (1) the significance of any decline in net assets of the FHLB as compared to the capital stock amount for the FHLB and the length of time this situation has persisted, (2) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB, (3) the impact of legislative and regulatory changes on institutions and, accordingly, the customer base of the FHLB, and (4) the liquidity position of the FHLB.

As a member of the FHLB system, the Company is required to maintain a minimum level of investment in FHLB stock based on specific percentages of its outstanding mortgages, total assets, or FHLB advances. The Company may request redemption at par value of any stock in excess of the minimum required investment. Stock redemptions are at the discretion of the FHLB.

Table of Contents**Loans**

The Bank concentrates its lending activities in four principal areas: real estate mortgage loans (residential and commercial loans), consumer loans, commercial loans (including agricultural loans), and real estate construction loans. The interest rates charged for the loans made by the Bank vary with the degree of risk, the size and maturity of the loans, the borrower's relationship with the Bank and prevailing money market rates indicative of the Bank's cost of funds.

The majority of the Bank's loans are direct loans made to individuals, farmers and local businesses. The Bank relies substantially on local promotional activity and personal contacts by bank officers, directors and employees to compete with other financial institutions. The Bank makes loans to borrowers whose applications include a sound purpose, a viable repayment source and a plan of repayment established at inception and generally backed by a secondary source of repayment.

Loan Portfolio Composite

The following table shows the Company's loan balances, including net deferred loan costs, at the dates indicated:

(dollars in thousands)	Year ended December 31,				
	2012	2011	2010	2009	2008
Real estate mortgage	\$ 1,010,130	\$ 965,922	\$ 835,471	\$ 844,053	\$ 839,687
Consumer	386,111	406,330	395,771	428,722	477,435
Commercial	135,528	139,131	143,413	164,094	190,295
Real estate construction	33,054	39,649	44,916	58,701	83,432
Total loans	\$ 1,564,823	\$ 1,551,032	\$ 1,419,571	\$ 1,495,570	\$ 1,590,849

The following table shows the Company's loan balances, including net deferred loan costs, as a percentage of total loans at the dates indicated:

	Year ended December 31,				
	2012	2011	2010	2009	2008
Real estate mortgage	64.5%	62.2%	58.8%	56.4%	52.8%
Consumer	24.7%	26.2%	27.9%	28.7%	30.0%
Commercial	8.7%	9.0%	10.1%	11.0%	12.0%
Real estate construction	2.1%	2.6%	3.2%	3.9%	5.2%
Total loans	100.0%	100.0%	100.0%	100.0%	100.0%

At December 31, 2012 loans, including net deferred loan costs, totaled \$1,564,823,000 which was a 0.9% (\$13,791,000) increase over the balances at the end of 2011. Demand for commercial real estate (real estate mortgage) loans was weak to modest during 2012. Demand for home equity loans and lines of credit were weak during 2012. Real estate construction loans declined during 2012 as did auto dealer loans.

At December 31, 2011 loans, including net deferred loan costs, totaled \$1,551,032,000 which was a 9.3% (\$131,461,000) increase over the balances at the end of 2010. This increase in loans during 2011 included \$167,484,000 of loans acquired in the Citizens acquisition on September 23, 2011. Demand for commercial real estate (real estate mortgage) loans was weak during 2011. Demand for home equity loans and lines of credit was weak to modest during 2011. Real estate construction loans declined during 2011 as did auto dealer loans.

Asset Quality and Nonperforming Assets**Nonperforming Assets**

Loans originated by the Company, i.e., not purchased or acquired in a business combination, are referred to as originated loans. Originated loans are reported at the principal amount outstanding, net of deferred loan fees and costs. Loan origination and commitment fees and certain direct

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loan origination costs are deferred, and the net amount is amortized as an adjustment of the related loan's yield over the actual life of the loan. Originated loans on which the accrual of interest has been discontinued are designated as nonaccrual loans.

Originated loans are placed in nonaccrual status when reasonable doubt exists as to the full, timely collection of interest or principal, or a loan becomes contractually past due by 90 days or more with respect to interest or principal and is not well secured and in the process of collection. When an originated loan is placed on nonaccrual status, all interest previously accrued but not collected is reversed. Income on such loans is then recognized only to the extent that cash is received and where the future collection of principal is probable. Interest accruals are resumed on such loans only when they are brought fully current with respect to interest and principal and when, in the judgment of Management, the loan is estimated to be fully collectible as to both principal and interest.

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An allowance for loan losses for originated loans is established through a provision for loan losses charged to expense. Originated loans and deposit related overdrafts are charged against the allowance for loan losses when Management believes that the collectability of the principal is unlikely or, with respect to consumer installment loans, according to an established delinquency schedule. The allowance is an amount that Management believes will be adequate to absorb probable losses inherent in existing loans and leases, based on evaluations of the collectability, impairment and prior loss experience of loans and leases. The evaluations take into consideration such factors as changes in the nature and size of the portfolio, overall portfolio quality, loan concentrations, specific problem loans, and current economic conditions that may affect the borrower's ability to pay. The Company defines an originated loan as impaired when it is probable the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Impaired originated loans are measured based on the present value of expected future cash flows discounted at the loan's original effective interest rate. As a practical expedient, impairment may be measured based on the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. When the measure of the impaired loan is less than the recorded investment in the loan, the impairment is recorded through a valuation allowance.

In situations related to originated loans where, for economic or legal reasons related to a borrower's financial difficulties, the Company grants a concession for other than an insignificant period of time to the borrower that the Company would not otherwise consider, the related loan is classified as a troubled debt restructuring (TDR). The Company strives to identify borrowers in financial difficulty early and work with them to modify to more affordable terms before their loan reaches nonaccrual status. These modified terms may include rate reductions, principal forgiveness, payment forbearance and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. In cases where the Company grants the borrower new terms that result in the loan being classified as a TDR, the Company measures any impairment on the restructuring as noted above for impaired loans. TDR loans are classified as impaired until they are fully paid off or charged off. Loans that are in nonaccrual status at the time they become TDR loans, remain in nonaccrual status until the borrower demonstrates a sustained period of performance which the Company generally believes to be six consecutive months of payments, or equivalent. Otherwise, TDR loans are subject to the same nonaccrual and charge-off policies as noted above with respect to their restructured principal balance.

Credit risk is inherent in the business of lending. As a result, the Company maintains an allowance for loan losses to absorb losses inherent in the Company's originated loan portfolio. This is maintained through periodic charges to earnings. These charges are included in the Consolidated Statements of Income as provision for loan losses. All specifically identifiable and quantifiable losses are immediately charged off against the allowance. However, for a variety of reasons, not all losses are immediately known to the Company and, of those that are known, the full extent of the loss may not be quantifiable at that point in time. The balance of the Company's allowance for originated loan losses is meant to be an estimate of these unknown but probable losses inherent in the portfolio.

The Company formally assesses the adequacy of the allowance for originated loan losses on a quarterly basis. Determination of the adequacy is based on ongoing assessments of the probable risk in the outstanding originated loan portfolio, and to a lesser extent the Company's originated loan commitments. These assessments include the periodic re-grading of credits based on changes in their individual credit characteristics including delinquency, seasoning, recent financial performance of the borrower, economic factors, changes in the interest rate environment, growth of the portfolio as a whole or by segment, and other factors as warranted. Loans are initially graded when originated. They are re-graded as they are renewed, when there is a new loan to the same borrower, when identified facts demonstrate heightened risk of nonpayment, or if they become delinquent. Re-grading of larger problem loans occurs at least quarterly. Confirmation of the quality of the grading process is obtained by independent credit reviews conducted by consultants specifically hired for this purpose and by various bank regulatory agencies.

The Company's method for assessing the appropriateness of the allowance for originated loan losses includes specific allowances for impaired originated loans and leases, formula allowance factors for pools of credits, and allowances for changing environmental factors (e.g., interest rates, growth, economic conditions, etc.). Allowance factors for loan pools were based on historical loss experience by product type and prior risk rating. During the three months ended March 31, 2012, management changed some of the assumptions utilized in the Allowance for Loan Losses estimate calculation. These changes were intended to more accurately reflect the current risk in the loan portfolio and to better estimate the losses inherent but not yet quantifiable. These changes included the conversion to a historical loss migration analysis intended to better determine the appropriate formula reserve ratio by loan category and risk rating, the addition of an environmental factor related to the delinquency rate of loans not classified as impaired by loan category, the elimination of an unspecified reserve allocation previously intended to account for imprecision inherent in the overall calculation, and the reclassification of risk rating of certain consumer loans based on current credit score in an attempt to better identify the risk in the portfolio. The financial effect of these changes resulted in a net reduction in the calculated Allowance for Loan Losses of \$1,388,000 during the three months ended March 31, 2012. Allowances for impaired loans are based on analysis of individual credits. Allowances for changing environmental factors are Management's best estimate of the probable impact these changes have had on the originated loan portfolio as a whole. The allowance for originated loans is included in the allowance for loan losses.

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Loans purchased or acquired in a business combination are referred to as acquired loans. Acquired loans are valued as of acquisition date in accordance with Financial Accounting Standards Board Accounting Standards Codification (FASB ASC) Topic 805, *Business Combinations*. Loans acquired with evidence of credit deterioration since origination for which it is probable that all contractually required payments will not be collected are referred to as purchased credit impaired (PCI) loans. PCI loans are accounted for under FASB ASC Topic 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*. Under FASB ASC Topic 805 and FASB ASC Topic 310-30, PCI loans are recorded at fair value at acquisition date, factoring in credit losses expected to be incurred over the life of the loan. Accordingly, an allowance for loan losses is not carried over or recorded as of the acquisition date. Fair value is defined as the present value of the future estimated principal and interest payments of the loan, with the discount rate used in the present value calculation representing the estimated effective yield of the loan. Default rates, loss severity, and prepayment speed assumptions are periodically reassessed and our estimate of future payments is adjusted accordingly. The difference between contractual future payments and estimated future payments is referred to as the nonaccretable difference. The difference between estimated future payments and the present value of the estimated future payments is referred to as the accretable yield. The accretable yield represents the amount that is expected to be recorded as interest income over the remaining life of the loan. If after acquisition, the Company determines that the estimated future cash flows of a PCI loan are expected to be more than the originally estimated, an increase in the discount rate (effective yield) would be made such that the newly increased accretable yield would be recognized, on a level yield basis, over the remaining estimated life of the loan. If, after acquisition, the Company determines that the estimated future cash flows of a PCI loan are expected to be less than the previously estimated, the discount rate would first be reduced until the present value of the reduced cash flow estimate equals the previous present value however, the discount rate may not be lowered below its original level at acquisition. If the discount rate has been lowered to its original level and the present value has not been sufficiently lowered, an allowance for loan loss would be established through a provision for loan losses charged to expense to decrease the present value to the required level. If the estimated cash flows improve after an allowance has been established for a loan, the allowance may be partially or fully reversed depending on the improvement in the estimated cash flows. Only after the allowance has been fully reversed may the discount rate be increased. PCI loans are put on nonaccrual status when cash flows cannot be reasonably estimated. PCI loans on nonaccrual status are accounted for using the cost recovery method or cash basis method of income recognition. PCI loans are charged off when evidence suggests cash flows are not recoverable. Foreclosed assets from PCI loans are recorded in foreclosed assets at fair value with the fair value at time of foreclosure representing cash flow from the loan. ASC 310-30 allows PCI loans with similar risk characteristics and acquisition time frame to be pooled and have their cash flows aggregated as if they were one loan. The Company elected to use the pooled method of ASC 310-30 for PCI other loans in the acquisition of certain assets and liabilities of Granite Community Bank (Granite) and Citizens Bank of Northern California (Citizens).

Acquired loans that are not PCI loans are referred to as purchased not credit impaired (PNCI) loans. PNCI loans are accounted for under FASB ASC Topic 310-20, *Receivables - Nonrefundable Fees and Other Costs*, in which interest income is accrued on a level-yield basis for performing loans. For income recognition purposes, this method assumes that all contractual cash flows will be collected, and no allowance for loan losses is established at the time of acquisition. Post-acquisition date, an allowance for loan losses may need to be established for acquired loans through a provision charged to earnings for credit losses incurred subsequent to acquisition. Under ASC 310-20, the loss would be measured based on the probable shortfall in relation to the contractual note requirements, consistent with our allowance for loan loss policy for similar loans.

When referring to PNCI and PCI loans we will use the terms nonaccretable difference , accretable yield , or purchase discount . Nonaccretable difference is the difference between undiscounted contractual cash flows due and undiscounted cash flows we expect to collect, or put another way, it is the undiscounted contractual cash flows we do not expect to collect. Accretable yield is the difference between undiscounted cash flows we expect to collect and the value at which we have recorded the loan on our financial statements. On the date of acquisition, all purchased loans are recorded on our consolidated financial statements at estimated fair value. Purchase discount is the difference between the estimated fair value of loans on the date of acquisition and the principal amount owed by the borrower, net of charge offs, on the date of acquisition. We may also refer to discounts to principal balance of loans owed, net of charge-offs . Discounts to principal balance of loans owed, net of charge-offs is the difference between principal balance of loans owed, net of charge-offs, and loans as recorded on our financial statements. Discounts to principal balance of loans owed, net of charge-offs arise from purchase discounts, and equal the purchase discount on the acquisition date.

Loans are also categorized as covered or noncovered . Covered loans refer to loans covered by a Federal Deposit Insurance Corporation (FDIC) loss sharing agreement. Noncovered loans refer to loans not covered by a FDIC loss sharing agreement.

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Originated loans and PNCI loans are reviewed on an individual basis for reclassification to nonaccrual status when any one of the following occurs: the loan becomes 90 days past due as to interest or principal, the full and timely collection of additional interest or principal becomes uncertain, the loan is classified as doubtful by internal credit review or bank regulatory agencies, a portion of the principal balance has been charged off, or the Company takes possession of the collateral. Loans that are placed on nonaccrual even though the borrowers continue to repay the loans as scheduled are classified as performing nonaccrual and are included in total nonperforming loans. The reclassification of loans as nonaccrual does not necessarily reflect Management's judgment as to whether they are collectible.

Interest income on originated nonaccrual loans that would have been recognized during the years ended December 31, 2012, 2011 and 2010, if all such loans had been current in accordance with their original terms, totaled \$5,281,000, \$5,422,000, and \$5,169,000, respectively. Interest income actually recognized on these originated loans during the years ended December 31, 2012, 2011 and 2010 was \$936,000, \$1,497,000 and \$1,956,000, respectively. Interest income on PNCI nonaccrual loans that would have been recognized during the years ended December 31, 2012 and 2011, if all such loans had been current in accordance with their original terms, totaled \$284,000 and \$4,000, respectively. Interest income actually recognized on these PNCI loans during the years ended December 31, 2012 and 2011 was \$136,000 and \$5,000, respectively. The Company had no PNCI loans during 2010.

The Company's policy is to place originated loans and PNCI loans 90 days or more past due on nonaccrual status. In some instances when an originated loan is 90 days past due Management does not place it on nonaccrual status because the loan is well secured and in the process of collection. A loan is considered to be in the process of collection if, based on a probable specific event, it is expected that the loan will be repaid or brought current. Generally, this collection period would not exceed 30 days. Loans where the collateral has been repossessed are classified as foreclosed assets.

Management considers both the adequacy of the collateral and the other resources of the borrower in determining the steps to be taken to collect nonaccrual loans. Alternatives that are considered are foreclosure, collecting on guarantees, restructuring the loan or collection lawsuits.

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The following tables set forth the amount of the Bank's nonperforming assets as of the dates indicated. For purposes of the following table, PCI other loans that are 90 days past due and still accruing are not considered nonperforming loans:

Performing nonaccrual loans are loans that may be current for both principal and interest payments, or are less than 90 days past due, but for which payment in full of both principal and interest is not expected, and are not well secured and in the process of collection:

(dollars in thousands)	December 31,				
	2012	2011	2010	2009	2008
Performing nonaccrual loans	\$ 49,045	\$ 61,164	\$ 36,518	\$ 22,870	\$ 22,600
Nonperforming nonaccrual loans	23,471	23,647	39,224	26,301	9,994
Total nonaccrual loans	72,516	84,811	75,742	49,171	32,594
Originated and PNCI loans 90 days past due and still accruing		920	245	700	187
Total nonperforming loans	72,516	85,731	75,987	49,871	32,781
Noncovered foreclosed assets	5,957	13,268	5,000	3,726	1,185
Covered foreclosed assets	1,541	3,064	4,913		
Total nonperforming assets	\$ 80,014	\$ 102,063	\$ 85,900	\$ 53,597	\$ 33,966
U.S. government, including its agencies and its government-sponsored agencies, guaranteed portion of nonperforming loans	\$ 131	\$ 3,061	\$ 3,937	\$ 4,975	\$ 5,256
Indemnified portion of covered foreclosed assets	\$ 1,233	\$ 2,451	\$ 3,930		
Nonperforming assets to total assets	3.07%	3.99%	3.92%	2.24%	1.41%
Nonperforming loans to total loans	4.63%	5.53%	5.35%	2.99%	1.73%
Allowance for loan losses to nonperforming loans	59%	54%	56%	79%	100%
Allowance for loan losses, unamortized loan fees, and discounts to loan principal balances owed	5.30%	6.34%	3.74%	2.48%	1.79%

(dollars in thousands)	December 31, 2012				
	Originated	PNCI	PCI - cash basis	PCI - other	Total
Performing nonaccrual loans	\$ 38,646	\$ 1,428	\$ 8,971		\$ 49,045
Nonperforming nonaccrual loans	23,123	348			23,471
Total nonaccrual loans	61,769	1,776	8,971		72,516
Originated loans 90 days past due and still accruing					
Total nonperforming loans	61,769	1,776	8,971		72,516
Noncovered foreclosed assets	5,172			785	5,957
Covered foreclosed assets				1,541	1,541
Total nonperforming assets	\$ 66,941	\$ 1,776	\$ 8,971	\$ 2,326	\$ 80,014
U.S. government, including its agencies and its government-sponsored agencies, guaranteed portion of nonperforming loans	\$ 131				\$ 131
Indemnified portion of covered foreclosed assets				\$ 1,233	\$ 1,233
Nonperforming assets to total assets					3.07%
Nonperforming loans to total loans	4.42%	1.81%	100.00%		4.63%

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Allowance for loan losses to nonperforming loans	58%	111%	12%	n/m	59%
Allowance for loan losses, unamortized loan fees, and discounts to loan principal balances owed	2.76%	13.78%	61.60%	24.63%	5.30%
n/m not meaningful					

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(dollars in thousands)	December 31, 2011				
	Originated	PNCI	PCI - cash basis	PCI - other	Total
Performing nonaccrual loans	\$ 52,208	\$ 97	\$ 8,859		\$ 61,164
Nonperforming nonaccrual loans	23,067	13	567		23,647
Total nonaccrual loans	75,275	110	9,426		84,811
Originated and PNCI loans 90 days past due and still accruing	500	420			920
Total nonperforming loans	75,775	530	9,426		85,731
Noncovered foreclosed assets	6,209			7,059	13,268
Covered foreclosed assets				3,064	3,064
Total nonperforming assets	\$ 81,984	\$ 530	\$ 9,426	\$ 10,123	\$ 102,063
U.S. government, including its agencies and its government-sponsored agencies, guaranteed portion of nonperforming loans	\$ 3,061				\$ 3,061
Indemnified portion of covered foreclosed assets				\$ 2,451	\$ 2,451
Nonperforming assets to total assets					3.99%
Nonperforming loans to total loans	5.67%	0.39%	100.00%		5.53%
Allowance for loan losses to nonperforming loans	55%	46%	11%	n/m	54%
Allowance for loan losses, unamortized loan fees, and discounts to loan principal balances owed	3.27%	12.13%	62.09%	27.37%	6.34%
n/m not meaningful					

The following table shows the activity in the balance of nonperforming assets for the year ended December 31, 2012:

(dollars in thousands):	Balance at December 31, 2012	New NPA	Advances/ Capitalized Costs	Pay-downs/		Transfers to Foreclosed Assets	Category Changes	Balance at December 31, 2011
				Sales/ Upgrades	Charge-offs/ Write-downs			
Real estate mortgage:								
Residential	\$ 4,894	\$ 2,912	\$ 60	\$ (3,817)	\$ (1,558)	\$ (1,228)		\$ 8,525
Commercial	39,727	20,056	582	(18,789)	(3,457)	(4,505)	\$ 1,155	44,685
Consumer								
Home equity lines	16,500	11,702	749	(2,951)	(8,042)	(1,845)	(96)	16,983
Home equity loans	514	464	45	(238)	(385)	(26)	96	558
Auto indirect	174	132	1	(384)	(83)			508
Other consumer	92	418		(102)	(334)			110
Commercial	6,771	3,948	1,673	(4,258)	(1,251)	(254)	(1,155)	8,068
Construction:								
Residential	3,312	496	12	(1,893)	(406)	(524)		5,627
Commercial	532	152		(187)	(100)			667
Total nonperforming loans	72,516	40,280	3,122	(32,619)	(15,616)	(8,382)		85,731
Noncovered foreclosed assets	5,957		758	(14,776)	(1,267)	7,974		13,268
Covered foreclosed assets	1,541		225	(1,695)	(461)	408		3,064
Total nonperforming assets	\$ 80,014	\$ 40,280	\$ 4,105	\$ (49,090)	\$ (17,344)			\$ 102,063

The table above does not include deposit overdraft charge-offs.

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The following tables and narratives describe the activity in the balance of nonperforming assets during each of the three-month periods ending March 31, June 30, September 30, and December 31, 2012. These tables and narratives are presented in chronological order:

Changes in nonperforming assets during the three months ended December 31, 2012

(In thousands):	Balance at December 31, 2012	New NPA	Advances/ Capitalized Costs	Pay-downs/ Sales/ Upgrades	Charge-offs/ Write-downs	Transfers to Foreclosed Assets	Category Changes	Balance at September 30, 2012
Real estate mortgage:								
Residential	\$ 4,894	165		(1,614)	(640)	(438)		\$ 7,421
Commercial	39,727	9,285		(9,994)	(1,449)	(1,374)		43,259
Consumer								
Home equity lines	16,500	2,184	13	(752)	(1,303)	(501)		16,859
Home equity loans	514	80	45	(65)	(215)			669
Auto indirect	174	5		(56)				225
Other consumer	92	70		(19)	(65)			106
Commercial	6,771	810		(2,461)	(49)	(254)		8,725
Construction:								
Residential	3,312	53		(495)	(44)			3,798
Commercial	532	152		(137)	(32)			549
Total nonperforming loans	72,516	12,804	58	(15,593)	(3,797)	(2,567)		81,611
Noncovered foreclosed assets	5,957		508	(4,703)	(208)	2,567		7,793
Covered foreclosed assets	1,541			(851)				2,392
Total nonperforming assets	\$ 80,014	\$ 12,804	\$ 566	\$ (21,147)	\$ (4,005)			\$ 91,796

Nonperforming assets decreased during the fourth quarter of 2012 by \$11,782,000 (12.83%) to \$80,014,000 at December 31, 2012 compared to \$91,796,000 at September 30, 2012. The decrease in nonperforming assets during the fourth quarter of 2012 was primarily the result of new nonperforming loans of \$12,804,000, advances on existing nonperforming loans and capitalized costs on foreclosed assets of \$566,000, less pay-downs, sales or upgrades of nonperforming loans to performing status totaling \$15,593,000, less dispositions of foreclosed assets totaling \$5,554,000, less loan charge-offs of \$3,797,000, and less write-downs of foreclosed assets of \$208,000. Included in the \$15,593,000 of pay-downs, sales or upgrades of nonperforming loans were sales of \$9,739,000. The loan sales of \$9,739,000 were comprised of \$190,000 of residential real estate secured loans in central California, \$201,000 of residential real estate secured loans in northern California, \$3,537,000 of commercial real estate secured loans in central California, \$5,280,000 of commercial real estate secured loans in northern California, \$227,000 in Home Equity Lines of Credit located in northern California, \$173,000 in residential construction loans in northern California and \$129,000 in commercial construction loans in central California. Proceeds net of selling costs in the amount of \$9,810,000 were received on the sale resulting in a net gain on sale of \$71,000.

The \$12,804,000 in new nonperforming loans during the fourth quarter of 2012 was comprised of increases of \$165,000 on two residential real estate loans, \$9,285,000 on 10 commercial real estate loans, \$2,264,000 on 25 home equity lines and loans, \$5,000 on three indirect auto loans, \$70,000 on 24 consumer loans, \$810,000 on 14 C&I loans, \$53,000 on two residential construction loans, and \$152,000 on a single commercial construction loan.

The \$9,285,000 in new nonperforming commercial real estate loans was primarily made up of a single loan in the amount of \$379,000 secured by a commercial retail building in northern California, a single loan in the amount of \$3,597,000 secured by a commercial retail building in central California, and a single loan in the amount of \$4,563,000 secured by a commercial office building central California. Related charge-offs are discussed below.

The \$810,000 in new nonperforming C&I loans was primarily made up of a single loan in the amount of \$544,000 secured by an assignment of a note receivable and deed of trust northern California. Related charge-offs are discussed below.

Loan charge-offs during the three months ended December 31, 2012

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In the fourth quarter of 2012, the Company recorded \$3,797,000 in loan charge-offs and \$209,000 in deposit overdraft charge-offs less \$801,000 in loan recoveries and \$183,000 in deposit overdraft recoveries resulting in \$3,023,000 of net charge-offs. Primary causes of the loan charges taken in the fourth quarter of 2012 were gross charge-offs of \$640,000 on nine residential real estate loans, \$1,449,000 on 14 commercial real estate loans, \$1,518,000 on 36 home equity lines and loans, \$66,000 on 23 other consumer loans, \$49,000 on eight C&I loans, \$44,000 on two residential construction loans, and \$32,000 on a single commercial construction loan.

The \$1,425,000 in charge-offs the bank took in its commercial real estate portfolio was primarily comprised of a \$510,000 charge on a loan secured by a commercial warehouse in central California. The remaining \$915,000 was spread over 12 loans spread throughout the Company's footprint.

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Differences between the amounts explained in this section and the total charge-offs listed for a particular category are generally made up of individual charges of less than \$250,000 each. Generally losses are triggered by non-performance by the borrower and calculated based on any difference between the current loan amount and the current value of the underlying collateral less any estimated costs associated with the disposition of the collateral.

Changes in nonperforming assets during the three months ended September 30, 2012

(In thousands):	Balance at September 30, 2012	New NPA	Advances/ Capitalized Costs	Pay-downs/ Sales	Charge-offs/ Write-downs	Transfers to Foreclosed Assets	Category Changes	Balance at June 30, 2012
Real estate mortgage:								
Residential	\$ 7,421	\$ 1,270	\$ 1	\$ (989)	\$ (370)	\$ (292)		\$ 7,801
Commercial	43,259	1,399	193	(1,488)	(340)	(233)	\$ 19	43,709
Consumer								
Home equity lines	16,859	2,923	324	(976)	(1,635)	(171)	(18)	16,412
Home equity loans	669	164		(32)	(13)		18	532
Auto indirect	225	22		(66)	(11)			280
Other consumer	106	26		(32)	(37)			149
Commercial	8,725	298	1,267	(1,269)	(625)		\$ (19)	9,073
Construction:								
Residential	3,798	96		(559)	(93)			4,354
Commercial	549			(18)				567
Total nonperforming loans	81,611	6,198	1,785	(5,429)	(3,124)	(696)		82,877
Noncovered foreclosed assets	7,793		86	(2,702)	(433)	\$ 696		10,146
Covered foreclosed assets	2,392			(205)				2,597
Total nonperforming assets	\$ 91,796	\$ 6,198	\$ 1,871	\$ (8,336)	\$ (3,557)			\$ 95,620

Nonperforming assets decreased during the third quarter of 2012 by \$3,824,000 (4.0%) to \$91,796,000 at September 30, 2012 compared to \$95,620,000 at June 30, 2012. The decrease in nonperforming assets during the third quarter of 2012 was primarily the result of new nonperforming loans of \$6,198,000, advances on existing nonperforming loans and capitalized costs on foreclosed assets of \$1,871,000, less pay-downs or upgrades of nonperforming loans to performing status totaling \$5,429,000, less dispositions of foreclosed assets totaling \$2,907,000, less loan charge-offs of \$3,124,000, and less write-downs of foreclosed assets of \$433,000.

The primary causes of the \$6,198,000 in new nonperforming loans during the third quarter of 2012 were increases of \$1,270,000 on 11 residential real estate loans, \$1,399,000 on nine commercial real estate loans, \$3,087,000 on 37 home equity lines and loans, \$22,000 on eight indirect auto loans, \$26,000 on 17 consumer loans, \$298,000 on 10 C&I loans, and \$96,000 on one residential construction loan.

The \$1,399,000 in new nonperforming commercial real estate loans was primarily comprised of one loan totaling \$318,000 secured by a commercial retail building in northern California and a \$559,000 loan secured by a gas station in central California.

Loan charge-offs during the three months ended September 30, 2012

In the third quarter of 2012, the Company recorded \$3,124,000 in loan charge-offs and \$243,000 in deposit overdraft charge-offs less \$947,000 in loan recoveries and \$188,000 in deposit overdraft recoveries resulting in \$2,233,000 of net charge-offs. Primary causes of the charges taken in the first quarter of 2012 were gross charge-offs of \$370,000 on eight residential real estate loans, \$340,000 on 10 commercial real estate loans, \$1,648,000 on 31 home equity lines and loans, \$11,000 on five auto indirect loans, \$37,000 on 16 other consumer loans, \$625,000 on 11 C&I loans, and \$93,000 on two residential construction loans.

During the third quarter of 2012, there were no individual charges greater than \$250,000. Generally losses are triggered by non-performance by the borrower and calculated based on any difference between the current loan amount and the current value of the underlying collateral less any estimated costs associated with the disposition of the collateral.

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Activity in the balance of nonperforming assets for the periods indicated (continued):

Changes in nonperforming assets during the three months ended June 30, 2012

(In thousands):	Balance at June 30, 2012	New NPA	Advances/ Capitalized Costs	Pay-downs/ Sales	Charge-offs/ Write-downs	Transfers to Foreclosed Assets	Category Changes	Balance at March 31, 2012
Real estate mortgage:								
Residential	\$ 7,801	\$ 703	\$ 44	\$ (622)	\$ (325)	\$ (295)		\$ 8,296
Commercial	43,709	5,322	389	(3,330)	(363)	(2,206)	\$ 1,136	42,761
Consumer								
Home equity lines	16,412	4,128	25	(717)	(2,477)	(374)	(78)	15,905
Home equity loans	532	175		(112)	(117)	(26)	78	534
Auto indirect	280	37		(73)	(32)			348
Other consumer	149	120		(21)	(97)			147
Commercial	9,073	2,383		(165)	(295)		(1,136)	8,286
Construction:								
Residential	4,354	78	12	(658)	(201)	(524)		5,647
Commercial	567			(16)	(68)			651
Total nonperforming loans	82,877	12,946	470	(5,714)	(3,975)	(3,425)		82,575
Noncovered foreclosed assets	10,146		164	(3,992)	(543)	3,017		11,500
Covered foreclosed assets	2,597			(639)	(461)	408		3,289
Total nonperforming assets	\$ 95,620	\$ 12,946	\$ 634	\$ (10,345)	\$ (4,979)			\$ 97,364

Nonperforming assets decreased during the second quarter of 2012 by \$1,744,000 (1.8%) to \$95,620,000 at June 30, 2012 compared to \$97,364,000 at March 31, 2012. The decrease in nonperforming assets during the second quarter of 2012 was primarily the result of new nonperforming loans of \$12,946,000, advances on existing nonperforming loans and capitalized costs on foreclosed assets of \$634,000, less pay-downs or upgrades of nonperforming loans to performing status totaling \$5,714,000, less dispositions of foreclosed assets totaling \$4,631,000, less loan charge-offs of \$3,975,000, and less write-downs of foreclosed assets of \$1,004,000.

The primary causes of the \$12,946,000 in new nonperforming loans during the second quarter of 2012 were increases of \$703,000 on eight residential real estate loans, \$5,322,000 on 15 commercial real estate loans, \$4,303,000 on 44 home equity lines and loans, \$37,000 on seven indirect auto loans, \$120,000 on 20 consumer loans, \$2,383,000 on 21 C&I loans, and \$78,000 on one residential construction loan.

The \$5,322,000 in new nonperforming commercial real estate loans was primarily comprised of three loans totaling \$1,262,000 secured by commercial retail buildings in northern California, a \$1,906,000 loan secured by a commercial warehouse in northern California, two loans totaling \$733,000 secured by light industrial commercial property in northern California and a \$462,000 loan secured by mixed-use commercial property in northern California.

The \$2,383,000 in new nonperforming C&I loans was primarily comprised of a \$818,000 loan secured by equipment in northern California and two loans totaling \$882,000 secured by accounts receivable, inventory and equipment in northern California.

Loan charge-offs during the three months ended June 30, 2012

In the second quarter of 2012, the Company recorded \$3,976,000 in loan charge-offs and \$212,000 in deposit overdraft charge-offs less \$1,025,000 in loan recoveries and \$188,000 in deposit overdraft recoveries resulting in \$2,975,000 of net charge-offs. Primary causes of the charges taken in the first quarter of 2012 were gross charge-offs of \$325,000 on seven residential real estate loans, \$363,000 on five commercial real estate loans, \$2,595,000 on 42 home equity lines and loans, \$32,000 on eight auto indirect loans, \$97,000 on 25 other consumer loans, \$295,000 on 14 C&I loans, \$201,000 on three residential construction loans and \$68,000 on one commercial construction loan.

The \$363,000 in gross charge-offs the bank recorded in its commercial real estate portfolio was primarily comprised of a single loan secured by a commercial warehouse in central California in the amount of \$290,000.

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Differences between the amounts explained in this section and the total charge-offs listed for a particular category are generally made up of individual charges of less than \$250,000 each. Generally losses are triggered by non-performance by the borrower and calculated based on any difference between the current loan amount and the current value of the underlying collateral less any estimated costs associated with the disposition of the collateral.

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Activity in the balance of nonperforming assets for the periods indicated (continued):

Changes in nonperforming assets during the three months ended March 31, 2012

(In thousands):	Balance at March 31, 2012	New NPA	Advances/ Capitalized Costs	Pay-downs/ Sales	Charge-offs/ Write-downs	Transfers to Foreclosed Assets	Category Changes	Balance at December 31, 2011
Real estate mortgage:								
Residential	\$ 8,296	\$ 774	\$ 15	\$ (592)	\$ (223)	\$ (203)		\$ 8,525
Commercial	42,761	4,050		(3,977)	(1,305)	(692)		44,685
Consumer								
Home equity lines	15,905	2,467	387	(508)	(2,625)	(799)		16,983
Home equity loans	534	45		(28)	(41)			558
Auto indirect	348	68	1	(189)	(40)			508
Other consumer	147	202		(30)	(135)			110
Commercial	8,286	457	406	(364)	(281)			8,068
Construction:								
Residential	5,647	269		(181)	(68)			5,627
Commercial	651			(16)				667
Total nonperforming loans	82,575	8,332	809	(5,885)	(4,718)	(1,694)		85,731
Noncovered foreclosed assets	11,500			(3,379)	(83)	1,694		13,268
Covered foreclosed assets	3,289		225					3,064
Total nonperforming assets	\$ 97,364	\$ 8,332	\$ 1,034	\$ (9,264)	\$ (4,801)			\$ 102,063

Nonperforming assets decreased during the first quarter of 2012 by \$4,699,000 (4.6%) to \$97,364,000 at March 31, 2012 compared to \$102,063,000 at December 31, 2011. The decrease in nonperforming assets during the first quarter of 2012 was primarily the result of new nonperforming loans of \$8,332,000, advances on existing nonperforming loans and capitalized costs on foreclosed assets of \$1,034,000, less pay-downs or upgrades of nonperforming loans to performing status totaling \$5,885,000, less dispositions of foreclosed assets totaling \$3,379,000, less loan charge-offs of \$4,718,000, and less write-downs of foreclosed assets of \$83,000.

The primary causes of the \$8,332,000 in new nonperforming loans during the first quarter of 2012 were increases of \$774,000 on six residential real estate loans, \$4,050,000 on 12 commercial real estate loans, \$2,512,000 on 42 home equity lines and loans, \$68,000 on 16 indirect auto loans, \$202,000 on 20 consumer loans, \$457,000 on 10 C&I loans, and \$269,000 on four residential construction loans.

The \$4,050,000 in new nonperforming commercial real estate loans was primarily comprised of four loans totaling \$1,913,000 secured by commercial office buildings in northern California, a \$962,000 loan secured by a commercial retail building in northern California and a \$470,000 loan secured by a commercial warehouse in northern California.

Loan charge-offs during the three months ended March 31, 2012

In the first quarter of 2012, the Company recorded \$4,718,000 in loan charge-offs and \$204,000 in deposit overdraft charge-offs less \$244,000 in loan recoveries and \$220,000 in deposit overdraft recoveries resulting in \$4,458,000 of net charge-offs. Primary causes of the charges taken in the first quarter of 2012 were gross charge-offs of \$223,000 on nine residential real estate loans, \$1,305,000 on six commercial real estate loans, \$2,666,000 on 47 home equity lines and loans, \$40,000 on 13 auto indirect loans, \$135,000 on 17 other consumer loans, \$281,000 on 15 C&I loans, and \$2,000 on two residential construction loans.

The \$1,305,000 in charge-offs the bank took in its commercial real estate portfolio was primarily the result of a \$607,000 charge on a loan secured by a commercial warehouse in northern California and a \$541,000 charge on a loan secured by an industrial plant facility in northern California. The remaining \$157,000 was spread over four loans spread throughout the Company's footprint.

Differences between the amounts explained in this section and the total charge-offs listed for a particular category are generally made up of individual charges of less than \$250,000 each. Generally losses are triggered by non-performance by the borrower and calculated based on any

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difference between the current loan amount and the current value of the underlying collateral less any estimated costs associated with the disposition of the collateral.

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The Company's allowance for loan losses is comprised of allowances for originated, PNCI and PCI loans. All such allowances are established through a provision for loan losses charged to expense.

Originated and PNCI loans, and deposit related overdrafts are charged against the allowance for originated loan losses when Management believes that the collectability of the principal is unlikely or, with respect to consumer installment loans, according to an established delinquency schedule. The allowances for originated and PNCI loan losses are amounts that Management believes will be adequate to absorb probable losses inherent in existing originated loans, based on evaluations of the collectability, impairment and prior loss experience of those loans and leases. The evaluations take into consideration such factors as changes in the nature and size of the portfolio, overall portfolio quality, loan concentrations, specific problem loans, and current economic conditions that may affect the borrower's ability to pay. The Company defines an originated or PNCI loan as impaired when it is probable the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Impaired originated and PNCI loans are measured based on the present value of expected future cash flows discounted at the loan's original effective interest rate. As a practical expedient, impairment may be measured based on the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. When the measure of the impaired loan is less than the recorded investment in the loan, the impairment is recorded through a valuation allowance.

In situations related to originated and PNCI loans where, for economic or legal reasons related to a borrower's financial difficulties, the Company grants a concession for other than an insignificant period of time to the borrower that the Company would not otherwise consider, the related loan is classified as a troubled debt restructuring (TDR). The Company strives to identify borrowers in financial difficulty early and work with them to modify to more affordable terms before their loan reaches nonaccrual status. These modified terms may include rate reductions, principal forgiveness, payment forbearance and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. In cases where the Company grants the borrower new terms that provide for a reduction of either interest or principal, the Company measures any impairment on the restructuring as noted above for impaired loans. TDR loans are classified as impaired until they are fully paid off or charged off. Loans that are in nonaccrual status at the time they become TDR loans, remain in nonaccrual status until the borrower demonstrates a sustained period of performance which the Company generally believes to be six consecutive months of payments, or equivalent. Otherwise, TDR loans are subject to the same nonaccrual and charge-off policies as noted above with respect to their restructured principal balance.

Credit risk is inherent in the business of lending. As a result, the Company maintains an allowance for loan losses to absorb losses inherent in the Company's originated and PNCI loan portfolios. These are maintained through periodic charges to earnings. These charges are included in the Consolidated Income Statements as provision for loan losses. All specifically identifiable and quantifiable losses are immediately charged off against the allowance. However, for a variety of reasons, not all losses are immediately known to the Company and, of those that are known, the full extent of the loss may not be quantifiable at that point in time. The balance of the Company's allowances for originated and PNCI loan losses are meant to be an estimate of these unknown but probable losses inherent in these portfolios.

The Company formally assesses the adequacy of the allowance for originated and PNCI loan losses on a quarterly basis. Determination of the adequacy is based on ongoing assessments of the probable risk in the outstanding originated and PNCI loan portfolios, and to a lesser extent the Company's originated and PNCI loan commitments. These assessments include the periodic re-grading of credits based on changes in their individual credit characteristics including delinquency, seasoning, recent financial performance of the borrower, economic factors, changes in the interest rate environment, growth of the portfolio as a whole or by segment, and other factors as warranted. Loans are initially graded when originated or acquired. They are re-graded as they are renewed, when there is a new loan to the same borrower, when identified facts demonstrate heightened risk of nonpayment, or if they become delinquent. Re-grading of larger problem loans occurs at least quarterly. Confirmation of the quality of the grading process is obtained by independent credit reviews conducted by consultants specifically hired for this purpose and by various bank regulatory agencies.

The Company's method for assessing the appropriateness of the allowance for originated and PNCI loan losses includes specific allowances for impaired loans and leases, formula allowance factors for pools of credits, and allowances for changing environmental factors (e.g., interest rates, growth, economic conditions, etc.). Allowance factors for loan pools are based on historical loss experience by product type and prior risk rating. Allowances for impaired loans are based on analysis of individual credits. Allowances for changing environmental factors are Management's best estimate of the probable impact these changes have had on the originated or PNCI loan portfolio as a whole. The allowances for originated and PNCI loans are included in the allowance for loan losses.

As noted above, the allowances for originated and PNCI loan losses consists of a specific allowance, a formula allowance, and an allowance for environmental factors. The first component, the specific allowance, results from the analysis of identified credits that meet management's criteria for specific evaluation. These loans are reviewed individually to determine if such loans are considered impaired. Impaired loans are those where management has concluded that it is probable that the borrower will be unable to pay all amounts due under the contractual terms. Impaired

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loans are specifically reviewed and evaluated individually by management for loss potential by evaluating sources of repayment, including collateral as applicable, and a specified allowance for loan losses is established where necessary.

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The second component of the allowance for originated and PNCI loan losses, the formula allowance, is an estimate of the probable losses that have occurred across the major loan categories in the Company's originated and PNCI loan portfolios. This analysis is based on loan grades by pool and the loss history of these pools. This analysis covers the Company's entire originated and PNCI loan portfolios including unused commitments but excludes any loans that were analyzed individually and assigned a specific allowance as discussed above. The total amount allocated for this component is determined by applying loss estimation factors to outstanding loans and loan commitments. The loss factors were previously based primarily on the Company's historical loss experience tracked over a five-year period and adjusted as appropriate for the input of current trends and events. Because historical loss experience varies for the different categories of originated loans, the loss factors applied to each category also differed. In addition, there is a greater chance that the Company would suffer a loss from a loan that was risk rated less than satisfactory than if the loan was last graded satisfactory. Therefore, for any given category, a larger loss estimation factor was applied to less than satisfactory loans than to those that the Company last graded as satisfactory. The resulting formula allowance was the sum of the allocations determined in this manner.

During the three month period ended March 31, 2012, the Company converted to a loss migration analysis to determine the formula allowance. Under this method, the Company reviewed the loss experience of each quarter over the previous three years and determined an annualized loss rate by loan category as well as risk rating at the beginning of each period reviewed. A weighted average was then applied to arrive at the average annualized loss rate for each loan category and risk rating, which was then applied against the net recorded investment for all loans by category and risk rating not classified as impaired. The effect of this change in methodology resulted in a net reduction in formula allowance required of \$3,296,000. This loss migration approach was promoted by regulatory agencies and implemented by the Company during the three month period ended March 31, 2012 as this was the first period in which sufficient historical data could be compiled to support the analysis.

In addition to updating the method by which the estimated formula allowance required is calculated, management also improved the monitoring and risk recognition within its consumer portfolio. Previously, consumer loans with no identified credit weakness had a risk rating of "Pass" assigned, and this would generally only change if the loan went 90 days past due, at which time the risk rating was systematically downgraded to "Substandard" and the loan was placed in nonaccrual. For the period ended March 31, 2012, management has chosen to monitor consumer loans based on current credit score and assign a risk rating of "Special Mention" for those scores below a certain threshold. This change is primarily intended to more effectively monitor and manage the risk in the Company's portfolio of consumer loans and lines of credit secured by junior liens on 1-4 family residential properties. The current credit score allows us to better account for increasing default risk in these types of loans. It is also the only reasonably available tool that can be used to attempt to monitor the performance of the senior lien on the associated properties, as the Company does not generally service both the 1st and 2nd loans in these instances. The result of this change in methodology resulted in an additional required formula allowance of \$1,874,000. \$1,596,000 of this additional requirement is specifically related to loans and lines of credit secured by junior liens on 1-4 family residential properties.

The third component of the allowances for originated and PNCI loan losses, the environmental factor allowance, is a component that is not allocated to specific loans or groups of loans, but rather is intended to absorb losses that may not be provided for by the other components.

There are several primary reasons that the other components discussed above might not be sufficient to absorb the losses present in the originated and PNCI loan portfolios, and the environmental factor allowance is used to provide for the losses that have occurred because of them.

The first reason is that there are limitations to any credit risk grading process. The volume of originated and PNCI loans makes it impractical to re-grade every loan every quarter. Therefore, it is possible that some currently performing originated or PNCI loans not recently graded will not be as strong as their last grading and an insufficient portion of the allowance will have been allocated to them. Grading and loan review often must be done without knowing whether all relevant facts are at hand. Troubled borrowers may deliberately or inadvertently omit important information from reports or conversations with lending officers regarding their financial condition and the diminished strength of repayment sources.

The second reason is that the loss estimation factors are based primarily on historical loss totals. As such, the factors may not give sufficient weight to such considerations as the current general economic and business conditions that affect the Company's borrowers and specific industry conditions that affect borrowers in that industry. The factors might also not give sufficient weight to other environmental factors such as changing economic conditions and interest rates, portfolio growth, entrance into new markets or products, and other characteristics as may be determined by Management.

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Specifically, in assessing how much environmental factor allowance needed to be provided, management considered the following:

with respect to the economy, management considered the effects of changes in GDP, unemployment, CPI, debt statistics, housing starts, housing sales, auto sales, agricultural prices, and other economic factors which serve as indicators of economic health and trends and which may have an impact on the performance of our borrowers, and

with respect to changes in the interest rate environment, management considered the recent changes in interest rates and the resultant economic impact it may have had on borrowers with high leverage and/or low profitability; and

with respect to changes in energy prices, management considered the effect that increases, decreases or volatility may have on the performance of our borrowers, and

with respect to loans to borrowers in new markets and growth in general, management considered the relatively short seasoning of such loans and the lack of experience with such borrowers, and

with respect to the potential imprecision in the total Allowance for Loan Losses calculation, management previously included an unspecified reserve equal to 1.00% of the total allowance and reserve for unfunded commitments calculated. For the period ended March 31, 2012, this unspecified reserve was eliminated resulting in a reduction in allowances required of \$425,000, and

with respect to loans that have not yet been identified as impaired, management considered the volume and severity of past due loans. This environmental consideration was added to the Company's Allowance for Loan Losses methodology for the period ended March 31, 2012 and resulted in additional allowances required of \$459,000.

Each of these considerations was assigned a factor and applied to a portion or the entire originated and PNCI loan portfolios. Since these factors are not derived from experience and are applied to large non-homogeneous groups of loans, they are available for use across the portfolio as a whole.

Acquired loans are valued as of acquisition date in accordance with Financial Accounting Standards Board Accounting Standards Codification (FASB ASC) Topic 805, *Business Combinations*. Loans purchased with evidence of credit deterioration since origination for which it is probable that all contractually required payments will not be collected are referred to as purchased credit impaired (PCI) loans. PCI loans are accounted for under FASB ASC Topic 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*. In addition, because of the significant credit discounts associated with the loans acquired in the Granite acquisition, the Company elected to account for all loans acquired in the Granite acquisition under FASB ASC Topic 310-30, and classify them all as PCI loans. Under FASB ASC Topic 805 and FASB ASC Topic 310-30, PCI loans are recorded at fair value at acquisition date, factoring in credit losses expected to be incurred over the life of the loan. Accordingly, an allowance for loan losses is not carried over or recorded as of the acquisition date. Fair value is defined as the present value of the future estimated principal and interest payments of the loan, with the discount rate used in the present value calculation representing the estimated effective yield of the loan. The difference between contractual future payments and estimated future payments is referred to as the nonaccretable difference. The difference between estimated future payments and the present value of the estimated future payments is referred to as the accretable yield. The accretable yield represents the amount that is expected to be recorded as interest income over the remaining life of the loan. If after acquisition, the Company determines that the future cash flows of a PCI loan are expected to be more than the originally estimated, an increase in the discount rate (effective yield) would be made such that the newly increased accretable yield would be recognized, on a level yield basis, over the remaining estimated life of the loan. If after acquisition, the Company determines that the future cash flows of a PCI loan are expected to be less than the previously estimated, the discount rate would first be reduced until the present value of the reduced cash flow estimate equals the previous present value however, the discount rate may not be lowered below its original level. If the discount rate has been lowered to its original level and the present value has not been sufficiently lowered, an allowance for loan loss would be established through a provision for loan losses charged to expense to decrease the present value to the required level. If the estimated cash flows improve after an allowance has been established for a loan, the allowance may be partially or fully reversed depending on the improvement in the estimated cash flows. Only after the allowance has been fully reversed may the discount rate be increased. PCI loans are put on nonaccrual status when cash flows cannot be reasonably estimated. PCI loans are charged off when evidence suggests cash flows are not recoverable. Foreclosed

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assets from PCI loans are recorded in foreclosed assets at fair value with the fair value at time of foreclosure representing cash flow from the loan. ASC 310-30 allows PCI loans with similar risk characteristics and acquisition time frame to be pooled and have their cash flows aggregated as if they were one loan.

Table of Contents**The Components of the Allowance for Loan Losses**

The following table sets forth the Bank's allowance for loan losses as of the dates indicated (dollars in thousands):

	2012	2011	December 31, 2010	2009	2008
Allowance for originated and PNCI loan losses:					
Specific allowance	\$ 4,505	\$ 5,993	\$ 6,945	\$ 8,627	\$ 5,850
Formula allowance	29,314	32,023	31,070	23,361	17,989
Environmental factors allowance	3,919	3,687	2,948	3,485	3,751
Allowance for originated and PNCI loan losses	37,738	41,703	40,963	35,473	27,590
Allowance for PCI loan losses	4,910	4,211	1,608		
Allowance for loan losses	\$ 42,648	\$ 45,914	\$ 42,571	\$ 35,473	\$ 27,590

Allowance for loan losses to loans 2.73% 2.96% 3.00% 2.37% 1.73%

Based on the current conditions of the loan portfolio, management believes that the \$42,648,000 allowance for loan losses at December 31, 2012 is adequate to absorb probable losses inherent in the Bank's loan portfolio. No assurance can be given, however, that adverse economic conditions or other circumstances will not result in increased losses in the portfolio.

The following table summarizes the allocation of the allowance for loan losses between loan types:

(dollars in thousands)	2012	2011	December 31, 2010	2009	2008
Real estate mortgage	\$ 12,305	\$ 15,621	\$ 15,707	\$ 7,689	\$ 10,967
Consumer	23,461	20,506	17,779	17,026	8,470
Commercial	4,703	6,545	5,991	6,958	7,002
Real estate construction	2,179	3,242	3,094	3,800	1,151
Total allowance for loan losses	\$ 42,648	\$ 45,914	\$ 42,571	\$ 35,473	\$ 27,590

The following table summarizes the allocation of the allowance for loan losses between loan types as a percentage of the total allowance for loan losses:

	2012	2011	December 31, 2010	2009	2008
Real estate mortgage	28.9%	34.0%	36.9%	21.7%	50.5%
Consumer	55.0%	44.7%	41.8%	48.0%	32.3%
Commercial	11.0%	14.2%	14.1%	19.6%	11.9%
Real estate construction	5.1%	7.1%	7.2%	10.7%	5.3%
Total allowance for loan losses	100.0%	100.0%	100.0%	100.0%	100.0%

The following table summarizes the allocation of the allowance for loan losses between loan types as a percentage of the total loans:

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	2012	2011	December 31,		
			2010	2009	2008
Real estate mortgage	1.22%	1.62%	1.88%	0.91%	1.31%
Consumer	6.08%	5.05%	4.49%	3.97%	1.77%
Commercial	3.47%	4.70%	4.18%	4.24%	3.68%
Real estate construction	6.59%	8.18%	6.89%	6.47%	1.38%
Total allowance for loan losses	2.73%	2.96%	3.00%	2.37%	1.73%

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The following tables summarize the activity in the allowance for loan losses, reserve for unfunded commitments, and allowance for losses (which is comprised of the allowance for loan losses and the reserve for unfunded commitments) for the years indicated (dollars in thousands):

	Year ended December 31,				
	2012	2011	2010	2009	2008
Allowance for loan losses:					
Balance at beginning of period	\$ 45,914	\$ 42,571	\$ 35,473	\$ 27,590	\$ 17,331
Provision for loan losses	9,423	23,060	37,458	31,450	20,950
Loans charged off:					
Real estate mortgage:					
Residential	(1,558)	(1,655)	(1,498)	(583)	(691)
Commercial	(3,457)	(4,451)	(8,281)	(1,223)	(18)
Consumer:					
Home equity lines	(8,042)	(9,746)	(11,221)	(7,487)	(2,942)
Home equity loans	(385)	(789)	(1,339)	(656)	(409)
Auto indirect	(83)	(427)	(1,403)	(2,806)	(2,710)
Other consumer	(1,202)	(1,158)	(1,687)	(1,238)	(1,237)
Commercial	(1,251)	(2,534)	(3,539)	(3,219)	(709)
Construction:					
Residential	(406)	(634)	(4,666)	(7,737)	(3,203)
Commercial	(100)	(653)	(94)	(89)	
Total loans charged off	(16,484)	(22,047)	(33,728)	(25,038)	(11,919)
Recoveries of previously charged-off loans:					
Real estate mortgage:					
Residential	147	126	2	40	
Commercial	1,020	127	1,456	71	58
Consumer:					
Home equity lines	398	573	138	98	13
Home equity loans	100	45	15		
Auto indirect	215	379	505	484	441
Other consumer	860	839	816	677	685
Commercial	643	173	205	71	31
Construction:					
Residential	412	28	231	30	
Commercial		40			
Total recoveries of previously charged off loans	3,795	2,330	3,368	1,471	1,228
Net charge-offs	(12,689)	(19,717)	(30,360)	(23,567)	(10,691)
Balance at end of period	\$ 42,648	\$ 45,914	\$ 42,571	\$ 35,473	\$ 27,590
Reserve for unfunded commitments:					
Balance at beginning of period	\$ 2,740	\$ 2,640	\$ 3,640	\$ 2,565	\$ 2,090
Provision for losses - unfunded commitments	875	100	(1,000)	1,075	475
Balance at end of period	\$ 3,615	\$ 2,740	\$ 2,640	\$ 3,640	\$ 2,565
Balance at end of period:					
Allowance for loan losses	\$ 42,648	\$ 45,914	\$ 42,571	\$ 35,473	\$ 27,590
Reserve for unfunded commitments	3,615	2,740	2,640	3,640	2,565
Allowance for loan losses and reserve for unfunded commitments	\$ 46,263	\$ 48,654	\$ 45,211	\$ 39,113	\$ 30,155
As a percentage of total loans at end of period:					
Allowance for loan losses	2.73%	2.96%	3.00%	2.37%	1.73%
Reserve for unfunded commitments	0.23%	0.18%	0.18%	0.24%	0.16%

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Allowance for loan losses and reserve for unfunded commitments	2.96%	3.14%	3.18%	2.61%	1.89%
Average total loans	\$ 1,552,540	\$ 1,442,821	\$ 1,464,606	\$ 1,542,147	\$ 1,549,014
Ratios:					
Net charge-offs during period to average loans outstanding during period	0.82%	1.37%	2.07%	1.53%	0.69%
Provision for loan losses to average loans outstanding	0.61%	1.60%	2.56%	2.04%	1.35%
Allowance for loan losses to loans at year end	2.73%	2.96%	3.00%	2.37%	1.73%

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The following tables detail the components and summarize the activity in foreclosed assets, net of allowances for losses for the years indicated (dollars in thousands):

(dollars in thousands):	Balance at December 31, 2012	New NPA	Advances/ Capitalized Costs	Sales	Valuation Adjustments	Transfers from Loans	Category Changes	Balance at December 31, 2011
Noncovered:								
Land & Construction	\$ 1,676			\$ (3,549)	\$ (587)	\$ 778		\$ 5,034
Residential real estate	1,742		\$ 833	(5,452)	(336)	3,507		3,190
Commercial real estate	2,539		(75)	(5,775)	(344)	3,689		5,044
Total noncovered	5,957		758	(14,776)	(1,267)	7,974		13,268
Covered:								
Land & Construction	712			(779)	(308)			1,799
Residential real estate				(121)	(59)			180
Commercial real estate	829		225	(795)	(94)	408		1,085
Total covered	1,541		225	(1,695)	(461)	408		3,064
Total foreclosed assets	\$ 7,498		\$ 983	\$ (16,471)	\$ (1,728)	\$ 8,382		\$ 16,332

(dollars in thousands):	Balance at December 31, 2011	New NPA	Advances/ Capitalized Costs	Sales	Valuation Adjustments	Transfers from Loans	Category Changes	Balance at December 31, 2010
Noncovered:								
Land & Construction	\$ 5,034	\$ 4,027		\$ (735)	\$ (802)	\$ 333		\$ 2,211
Residential real estate	3,190	442		(3,816)	(318)	4,433		2,449
Commercial real estate	5,044	3,943		(1,243)	(139)	2,143		340
Total noncovered	13,268	8,412		(5,794)	(1,259)	6,909		5,000
Covered:								
Land & Construction	1,799		9	(917)	(334)	25		3,016
Residential real estate	180				(6)			186
Commercial real estate	1,085			(241)	(385)			1,711
Total covered	3,064		9	(1,158)	(725)	25		4,913
Total foreclosed assets	\$ 16,332	\$ 8,412	\$ 9	\$ (6,952)	\$ (1,984)	\$ 6,934		\$ 9,913

Premises and Equipment

Premises and equipment were comprised of:

December 31, 2012 December 31, 2011
(In thousands)

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Land & land improvements	\$ 5,929	\$ 4,400
Buildings	23,090	20,251
Furniture and equipment	25,877	24,291
	54,896	48,942
Less: Accumulated depreciation	(32,101)	(30,241)
	22,795	18,701
Construction in progress	4,190	1,192
Total premises and equipment	\$ 26,985	\$ 19,893

During the year ended December 31, 2012, premises and equipment increased \$7,092,000 due to purchases of \$10,792,000, that were partially offset by depreciation of \$3,250,000 and disposals of premises and equipment with net book value of \$450,000. Included in the \$10,792,000 of purchases during the year ended December 31, 2012 is \$4,408,000 related to the Company's new campus and operations center in Chico, CA. As of December 31, 2012 the campus and operations center had a cost basis, included in construction in progress, as follows: land & land improvements \$427,000, building \$4,987,000, and furniture and equipment \$186,000. Upon its estimated completion in the second quarter of 2013, the campus and operations center is expected to have an approximate cost basis as follows: land & land improvements \$427,000, building \$6,816,000, and furniture and equipment \$2,075,000.

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Intangible Assets

Intangible assets at December 31, 2011 and 2010 were comprised of the following:

	December 31,	
	2012	2011
	(dollars in thousands)	
Core-deposit intangible	\$ 1,092	\$ 1,301
Goodwill	15,519	15,519
Total intangible assets	\$ 16,611	\$ 16,820

The core-deposit intangible assets resulted from the Bank's acquisition of Citizens in 2011, Granite in 2010, and the 2003 acquisition of North State National Bank. The core-deposit intangible related to the North State National Bank acquisition became fully amortized in 2011. The goodwill intangible asset resulted from the North State National Bank acquisition. Amortization of core deposit intangible assets amounting to \$209,000, \$177,000, and \$307,000 was recorded in 2012, 2011, and 2010, respectively.

Deposits

Deposits at December 31, 2012 increased \$99,166,000 (4.5%) over the 2011 year-end balances to \$2,289,702,000. All categories of deposits were up in 2012 with the exception of money market accounts and time certificates. Included in the December 31, 2012 certificate of deposit balances is \$5,000,000 from the State of California.

Deposits at December 31, 2011 increased \$338,363,000 (18.3%) over the 2010 year-end balances to \$2,190,536,000. All categories of deposits were up in 2011 except time certificates. Included in the December 31, 2011 certificate of deposit balances is \$5,000,000 from the State of California. The Bank participates in a deposit program offered by the State of California whereby the State may make deposits at the Bank's request subject to collateral and creditworthiness constraints. The negotiated rates on these State deposits are generally more favorable than other wholesale funding sources available to the Bank.

Long-Term Debt

See Note 16 to the consolidated financial statements at Item 8 of this report for information about the Company's other borrowings, including long-term debt.

Junior Subordinated Debt

See Note 17 to the consolidated financial statements at Item 8 of this report for information about the Company's junior subordinated debt.

Equity

See Note 19 and Note 29 in the consolidated financial statements at Item 8 of this report for a discussion of shareholders' equity and regulatory capital, respectively. Management believes that the Company's capital is adequate to support anticipated growth, meet the cash dividend requirements of the Company and meet the future risk-based capital requirements of the Bank and the Company.

Market Risk Management

Overview. The goal for managing the assets and liabilities of the Bank is to maximize shareholder value and earnings while maintaining a high quality balance sheet without exposing the Bank to undue interest rate risk. The Board of Directors has overall responsibility for the Company's interest rate risk management policies. The Bank has an Asset and Liability Management Committee (ALCO) which establishes and monitors guidelines to control the sensitivity of earnings to changes in interest rates.

Asset/Liability Management. Activities involved in asset/liability management include but are not limited to lending, accepting and placing deposits, investing in securities and issuing debt. Interest rate risk is the primary market risk associated with asset/liability management.

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Sensitivity of earnings to interest rate changes arises when yields on assets change in a different time period or in a different amount from that of interest costs on liabilities. To mitigate interest rate risk, the structure of the balance sheet is managed with the goal that movements of interest rates on assets and liabilities are correlated and contribute to earnings even in periods of volatile interest rates. The asset/liability management policy sets limits on the acceptable amount of variance in net interest margin and market value of equity under changing interest environments. Market value of equity is the net present value of estimated cash flows from the Bank's assets, liabilities and off-balance sheet items. The Bank uses simulation models to forecast net interest margin and market value of equity.

Simulation of net interest margin and market value of equity under various interest rate scenarios is the primary tool used to measure interest rate risk. Using computer-modeling techniques, the Bank is able to estimate the potential impact of changing interest rates on net interest margin and market value of equity. A balance sheet forecast is prepared using inputs of actual loan, securities and interest-bearing liability (i.e. deposits/borrowings) positions as the beginning base.

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In the simulation of net interest income, the forecast balance sheet is processed against various interest rate scenarios. These various interest rate scenarios include a flat rate scenario, which assumes interest rates are unchanged in the future, and rate ramp scenarios including -100, +100, and +200 basis points around the flat scenario. These ramp scenarios assume that interest rates increase or decrease evenly (in a ramp fashion) over a twelve-month period and remain at the new levels beyond twelve months.

The following table summarizes the projected effect on net interest income and net income due to changing interest rates as measured against a flat rate (no interest rate change) scenario over the succeeding twelve month period. The simulation results shown below assume no changes in the structure of the Company's balance sheet over the twelve months being measured (a flat balance sheet scenario), and that deposit rates will track general interest rate changes by approximately 50%:

Interest Rate Risk Simulation of Net Interest Income and Net Income as of December 31, 2012

Change in Interest Rates (Basis Points)	Estimated Change in Net Interest Income (NII) (as % of flat NII)
+200 (ramp)	3.39%
+100 (ramp)	1.54%
+ 0 (flat)	
-100 (ramp)	(1.08%)

In the simulation of market value of equity, the forecast balance sheet is processed against various interest rate scenarios. These various interest rate scenarios include a flat rate scenario, which assumes interest rates are unchanged in the future, and rate shock scenarios including -100, +100, and +200 basis points around the flat scenario. These rate shock scenarios assume that interest rates increase or decrease immediately (in a shock fashion) and remain at the new level in the future.

The following table summarizes the effect on market value of equity due to changing interest rates as measured against a flat rate (no change) scenario:

Interest Rate Risk Simulation of Market Value of Equity as of December 31, 2012

Change in Interest Rates (Basis Points)	Estimated Change in Market Value of Equity (MVE) (as % of flat MVE)
+200 (shock)	13.05%
+100 (shock)	7.46%
+ 0 (flat)	
-100 (shock)	(18.74%)

These results indicate that given a flat balance sheet scenario, and if deposit rates track general interest rate changes by approximately 50%, the Company's balance sheet is neutral to slightly asset sensitive over a twelve month time horizon. Neutral sensitivity implies that net interest income does not change when interest rates change. Asset sensitive implies that net interest income increases when interest rates rise, and decrease when interest rates decrease. The asset liability management policy limits aggregate market risk, as measured in this fashion, to an acceptable level within the context of risk-return trade-offs.

The simulation results noted above do not incorporate any management actions that might moderate the negative consequences of interest rate deviations. In addition, the simulation results noted above contain various assumptions such as a flat balance sheet, and the rate that deposit interest rates change as general interest rates change. Therefore, they do not reflect likely actual results, but serve as estimates of interest rate risk.

As with any method of measuring interest rate risk, certain shortcomings are inherent in the method of analysis presented in the preceding tables. For example, although certain of the Bank's assets and liabilities may have similar maturities or repricing time frames, they may react in different degrees to changes in market interest rates. In addition, the interest rates on certain of the Bank's asset and liability categories may precede, or lag behind, changes in market interest rates. Also, the actual rates of prepayments on loans and investments could vary significantly from the assumptions utilized in deriving the results as presented in the preceding tables. Further, a change in U.S. Treasury rates accompanied by a

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change in the shape of the treasury yield curve could result in different estimations from those presented herein. Accordingly, the results in the preceding tables should not be relied upon as indicative of actual results in the event of changing market interest rates. Additionally, the resulting estimates of changes in market value of equity are not intended to represent, and should not be construed to represent, estimates of changes in the underlying value of the Bank.

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Interest rate sensitivity is a function of the repricing characteristics of the Bank's portfolio of assets and liabilities. One aspect of these repricing characteristics is the time frame within which the interest-bearing assets and liabilities are subject to change in interest rates either at replacement, repricing or maturity. An analysis of the repricing time frames of interest-bearing assets and liabilities is sometimes called a gap analysis because it shows the gap between assets and liabilities repricing or maturing in each of a number of periods. Another aspect of these repricing characteristics is the relative magnitude of the repricing for each category of interest earning asset and interest-bearing liability given various changes in market interest rates. Gap analysis gives no indication of the relative magnitude of repricing given various changes in interest rates. Interest rate sensitivity management focuses on the maturity of assets and liabilities and their repricing during periods of changes in market interest rates. Interest rate sensitivity gaps are measured as the difference between the volumes of assets and liabilities in the Bank's current portfolio that are subject to repricing at various time horizons.

The following interest rate sensitivity table shows the Bank's repricing gaps as of December 31, 2012. In this table transaction deposits, which may be repriced at will by the Bank, have been included in the less than 3-month category. The inclusion of all of the transaction deposits in the less than 3-month repricing category causes the Bank to appear liability sensitive. Because the Bank may reprice its transaction deposits at will, transaction deposits may or may not reprice immediately with changes in interest rates.

Due to the limitations of gap analysis, as described above, the Bank does not actively use gap analysis in managing interest rate risk. Instead, the Bank relies on the more sophisticated interest rate risk simulation model described above as its primary tool in measuring and managing interest rate risk.

Interest Rate Sensitivity December 31, 2012

(dollars in thousands)	Repricing within:				
	Less than 3 months	3 - 6 months	6 - 12 months	1 - 5 years	Over 5 years
Interest-earning assets:					
Cash at Federal Reserve and other banks	\$ 667,813				
Securities	17,033	\$ 14,837	\$ 27,361	\$ 76,088	\$ 27,708
Loans	504,818	86,607	139,620	675,299	158,479
Total interest-earning assets	1,189,664	101,444	166,981	751,387	\$ 186,187
Interest-bearing liabilities					
Transaction deposits	1,266,389				
Time	118,426	69,687	70,594	79,773	
Other borrowings	9,197				
Junior subordinated debt	41,238				
Total interest-bearing liabilities	\$ 1,435,250	\$ 69,687	\$ 70,594	\$ 79,773	
Interest sensitivity gap	\$ (245,586)	\$ 31,757	\$ 96,387	\$ 671,614	\$ 186,187
Cumulative sensitivity gap	\$ (245,586)	\$ (213,829)	\$ (117,442)	\$ 554,172	\$ 740,359
As a percentage of earning assets:					
Interest sensitivity gap	(10.3%)	1.3%	4.0%	28.0%	7.8%
Cumulative sensitivity gap	(10.3%)	(8.9%)	(4.9%)	23.1%	30.9%

Liquidity

Liquidity refers to the Bank's ability to provide funds at an acceptable cost to meet loan demand and deposit withdrawals, as well as contingency plans to meet unanticipated funding needs or loss of funding sources. These objectives can be met from either the asset or liability side of the balance sheet. Asset liquidity sources consist of the repayments and maturities of loans, selling of loans, short-term money market investments, maturities of securities and sales of securities from the available-for-sale portfolio. These activities are generally summarized as investing activities in the Consolidated Statement of Cash Flows. Net cash provided by investing activities totaled approximately \$24,823,000 in 2012. A net decrease in investment balances and proceeds from the sale of other real estate owned were the major sources of funds in this category.

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Liquidity may also be generated from liabilities through deposit growth and borrowings. These activities are included under financing activities in the Consolidated Statement of Cash Flows. In 2012, financing activities provide funds totaling \$30,315,000 due mainly to a \$99,166,000 increase in deposit balances. Dividends paid and a decrease in short-term other borrowings used \$5,757,000 and \$63,344,000 of funds, respectively. The Bank also had available correspondent banking lines of credit totaling \$5,000,000 at December 31, 2012. In addition, at December 31, 2012, the Company had loans and securities available to pledge towards future borrowings from the Federal Home Loan Bank and the Federal Reserve Bank of up to \$507,404,000 and \$88,050,000, respectively. As of December 31, 2012, the Company had \$9,197,000 of other borrowings as described in Note 16 of the consolidated financial statements of the Company and the related notes at Item 8 of this report. While these sources are expected to continue to provide significant amounts of funds in the future, their mix, as well as the possible use of other sources, will depend on future economic and market conditions. Liquidity is also provided or used through the results of operating activities. In 2012, operating activities provided cash of \$56,486,000.

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The Bank classifies its entire investment portfolio as available for sale (AFS). The AFS securities plus cash and cash equivalents in excess of reserve requirements totaled \$880,332,000 at December 31, 2012, which was 33.7% of total assets at that time. This was up from \$846,355,000 and 33.1% at the end of 2011.

It is anticipated that loan demand may remain weak during 2013, although such demand will be dictated by economic and competitive conditions. The Company aggressively solicits non-interest bearing demand deposits and money market checking deposits, which are the least sensitive to interest rates. The growth of deposit balances is subject to heightened competition, the success of the Company's sales efforts, delivery of superior customer service and market conditions. The reduction in the federal funds rate and various Federal Reserve interest rate manipulation efforts have resulted in historic low short-term and long-term interest rates, which could impact deposit volumes in the future. Depending on economic conditions, interest rate levels, and a variety of other conditions, deposit growth may be used to fund loans, to reduce short-term borrowings or purchase investment securities. However, due to concerns such as uncertainty in the general economic environment, competition and political uncertainty, loan demand and levels of customer deposits are not certain.

The principal cash requirements of the Company are dividends on common stock when declared. The Company is dependent upon the payment of cash dividends by the Bank to service its commitments. Shareholder dividends are expected to continue subject to the Board's discretion and continuing evaluation of capital levels, earnings, asset quality and other factors. The Company expects that the cash dividends paid by the Bank to the Company will be sufficient to meet this payment schedule. Dividends from the Bank are subject to certain regulatory restrictions.

The maturity distribution of certificates of deposit in denominations of \$100,000 or more is set forth in the following table. These deposits are generally more rate sensitive than other deposits and, therefore, are more likely to be withdrawn to obtain higher yields elsewhere if available. The Bank participates in a program wherein the State of California places time deposits with the Bank at the Bank's option. At December 31, 2012, 2011 and 2010, the Bank had \$5,000,000, \$5,000,000 and \$5,000,000, respectively, of these State deposits.

Certificates of Deposit in Denominations of \$100,000 or More

(dollars in thousands)	Amounts as of December 31,		
	2012	2011	2010
Time remaining until maturity:			
Less than 3 months	\$ 73,180	\$ 82,497	\$ 91,208
3 months to 6 months	32,384	49,613	49,976
6 months to 12 months	34,311	46,446	54,316
More than 12 months	40,320	41,818	40,491
Total	\$ 180,195	\$ 220,374	\$ 235,991

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Loan demand also affects the Bank's liquidity position. The following table presents the maturities of loans, net of deferred loan costs, at December 31, 2012:

	Within One Year	After One But Within 5 Years	After 5 Years	Total
(dollars in thousands)				
Loans with predetermined interest rates:				
Real estate mortgage	\$ 50,582	\$ 115,439	\$ 158,386	\$ 324,407
Consumer	13,304	31,418	30,143	74,865
Commercial	11,499	26,735	2,388	40,622
Real estate construction	7,790	2,539	8,722	19,051
	\$ 83,175	\$ 176,131	\$ 199,639	\$ 458,945
Loans with floating interest rates:				
Real estate mortgage	\$ 47,686	\$ 173,515	\$ 464,522	\$ 685,723
Consumer	1,627	7,534	302,085	311,246
Commercial	66,173	22,170	6,563	94,906
Real estate construction	3,031	7,558	3,414	14,003
	\$ 118,517	\$ 210,777	\$ 776,584	\$ 1,105,878
Total loans	\$ 201,692	\$ 386,908	\$ 976,223	\$ 1,564,823

The maturity distribution and yields of the investment portfolio at December 31, 2012 is presented in the following table. The timing of the maturities indicated in the table below is based on final contractual maturities. Most mortgage-backed securities return principal throughout their contractual lives. As such, the weighted average life of mortgage-backed securities based on outstanding principal balance is usually significantly shorter than the final contractual maturity indicated below. Yields on tax exempt securities are shown on a tax equivalent basis. At December 31, 2012, the Bank had no held-to-maturity securities.

	Within One Year		After One Year but Through Five Years		After Five Years but Through Ten Years		After Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
(dollars in thousands)										
Securities Available-for-Sale										
Obligations of US government corporations and agencies	\$ 1,046	4.55%	\$ 4,117	4.33%	\$ 44,843	2.75%	\$ 101,695	3.94%	\$ 151,701	3.60%
Obligations of states and political subdivisions	2,236	7.66%			5,613	7.10%	1,572	6.70%	9,421	7.16%
Corporate bonds			1,905	1.84%					1,905	1.84%
Total securities available-for-sale	\$ 3,282	6.67%	\$ 6,022	3.52%	\$ 50,456	3.24%	\$ 103,267	3.98%	\$ 163,027	3.63%

Off-Balance Sheet Items

The Bank has certain ongoing commitments under operating and capital leases. See Note 18 of the financial statements at Item 8 of this report for the terms. These commitments do not significantly impact operating results. As of December 31, 2012 commitments to extend credit and commitments related to the Bank's deposit overdraft privilege product were the Bank's only financial instruments with off-balance sheet risk. The Bank has not entered into any material contracts for financial derivative instruments such as futures, swaps, options, etc. Commitments to extend

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credit were \$560,159,000 and \$534,370,000 at December 31, 2012 and 2011, respectively, and represent 35.8% of the total loans outstanding at year-end 2012 versus 34.5% at December 31, 2011. Commitments related to the Bank's deposit overdraft privilege product totaled \$69,675,000 and \$61,623,000 at December 31, 2012 and 2011, respectively.

Table of Contents**Certain Contractual Obligations**

The following chart summarizes certain contractual obligations of the Company as of December 31, 2012:

(dollars in thousands)	Total	Less than one year	1-3 years	3-5 years	More than 5 years
Other collateralized borrowings, fixed rate of 0.05% payable on January 2, 2013	\$ 9,197	\$ 9,197			
Junior subordinated debt ⁽²⁾	20,619				20,619
Junior subordinated debt ⁽³⁾	20,619				20,619
Operating lease obligations	9,608	2,772	3,953	1,571	1,312
Deferred compensation ⁽¹⁾	8,442	1,096	2,125	1,682	3,539
Supplemental retirement plans ⁽¹⁾	3,450	472	772	690	1,516
Construction contract ⁽⁴⁾	4,154	4,154			
Total contractual obligations	\$ 76,089	\$ 17,691	\$ 6,850	\$ 3,943	\$ 47,605

- (1) These amounts represent known certain payments to participants under the Company's deferred compensation and supplemental retirement plans. See Note 25 in the financial statements at Item 8 of this report for additional information related to the Company's deferred compensation and supplemental retirement plan liabilities.
- (2) Junior subordinated debt, adjustable rate of three-month LIBOR plus 3.05%, callable in whole or in part by the Company on a quarterly basis beginning October 7, 2008, matures October 7, 2033.
- (3) Junior subordinated debt, adjustable rate of three-month LIBOR plus 2.55%, callable in whole or in part by the Company on a quarterly basis beginning July 23, 2009, matures July 23, 2034.
- (4) This amount represents estimated amounts to be paid under a contract to construct the Company's new campus and operations facility. See Premises and Equipment under Item 7 of this report and Note 18 in the financial statements at Item 8 of this report for additional information related to the contractual commitment related to the construction of the Company's new campus and operations facility.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See Market Risk Management under Item 7 of this report which is incorporated herein.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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TRICO BANCSHARES
CONSOLIDATED BALANCE SHEETS

	At December 31,	
	2012	2011
	(in thousands, except share data)	
Assets:		
Cash and due from banks	\$ 81,086	\$ 73,652
Cash at Federal Reserve and other banks	667,813	563,623
Cash and cash equivalents	748,899	637,275
Securities available-for-sale	163,027	229,223
Restricted equity securities	9,647	10,610
Loans held for sale	12,053	10,219
Loans	1,564,823	1,551,032
Allowance for loan losses	(42,648)	(45,914)
Total loans, net	1,522,175	1,505,118
Foreclosed assets, net	7,498	16,332
Premises and equipment, net	26,985	19,893
Cash value of life insurance	50,582	50,403
Accrued interest receivable	6,636	7,312
Goodwill	15,519	15,519
Other intangible assets, net	1,092	1,301
Mortgage servicing rights	4,552	4,603
Indemnification asset	1,997	4,405
Other assets	38,607	43,384
Total assets	\$ 2,609,269	\$ 2,555,597
Liabilities and Shareholders' Equity:		
Liabilities:		
Deposits:		
Noninterest-bearing demand	\$ 684,833	\$ 541,276
Interest-bearing	1,604,869	1,649,260
Total deposits	2,289,702	2,190,536
Accrued interest payable	1,036	1,674
Reserve for unfunded commitments	3,615	2,740
Other liabilities	35,122	30,427
Other borrowings	9,197	72,541
Junior subordinated debt	41,238	41,238
Total liabilities	2,379,910	2,339,156
Commitments and contingencies (Note 18)		
Shareholders' equity:		
Common stock, no par value: 50,000,000 shares authorized; issued and outstanding: 16,000,838 at December 31, 2012	85,561	

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15,978,958 at December 31, 2011		84,079
Retained earnings	141,639	128,551
Accumulated other comprehensive income, net of tax	2,159	3,811
Total shareholders' equity	229,359	216,441
Total liabilities and shareholders' equity	\$ 2,609,269	\$ 2,555,597

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents**TRICO BANCSHARES****CONSOLIDATED STATEMENTS OF INCOME**

	Years ended December 31,		
	2012	2011	2010
	(in thousands, except per share data)		
Interest and dividend income:			
Loans, including fees	\$ 100,496	\$ 92,691	\$ 93,073
Debt securities:			
Taxable	6,072	8,733	10,007
Tax exempt	428	524	700
Dividends	105	27	32
Interest bearing cash at Federal Reserve and other banks	1,615	1,007	760
Total interest and dividend income	108,716	102,982	104,572
Interest expense:			
Deposits	4,416	6,559	10,447
Other borrowings	1,604	2,420	2,412
Junior subordinated debt	1,324	1,259	1,274
Total interest expense	7,344	10,238	14,133
Net interest income	101,372	92,744	90,439
Provision for loan losses	9,423	23,060	37,458
Net interest income after provision for loan losses	91,949	69,684	52,981
Noninterest income:			
Service charges and fees	23,925	23,944	23,100
Gain on sale of loans	6,810	3,037	3,647
Commissions on sale of non-deposit investment products	3,209	2,105	1,209
Increase in cash value of life insurance	1,820	1,885	1,847
Bargain purchase gain		7,575	232
Other	2,216	4,267	2,660
Total noninterest income	37,980	42,813	32,695
Noninterest expense:			
Salaries and related benefits	49,952	44,203	40,105
Other	48,046	38,512	37,100
Total noninterest expense	97,998	82,715	77,205
Income before income taxes	31,931	29,782	8,471

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Provision for income taxes	12,937	11,192	2,466
Net income	\$ 18,994	\$ 18,590	\$ 6,005
Earnings per share:			
Basic	\$ 1.19	\$ 1.17	\$ 0.38
Diluted	\$ 1.18	\$ 1.16	\$ 0.37

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents**TRICO BANCSHARES****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

	Years ended December 31,		
	2012	2011	2010
	(in thousands, except per share data)		
Net income	\$ 18,994	\$ 18,590	\$ 6,005
Other comprehensive (loss) income, net of tax:			
Unrealized holding (losses) gains on securities arising during the period	(1,216)	1,504	(24)
Change in minimum pension liability	(2)	1,140	(943)
Change in joint beneficiary agreement liability	(434)	(143)	(1)
Other comprehensive (loss) income	(1,652)	2,501	(968)
Comprehensive income	\$ 17,342	\$ 21,091	\$ 5,037

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

TRICO BANCSHARES**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY****Years Ended December 31, 2011, 2010 and 2009**

	Shares of Common Stock	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income	Total
	(in thousands, except share data)				
Balance at December 31, 2009	15,787,753	\$ 79,508	\$ 118,863	\$ 2,278	\$ 200,649
Net income			6,005		6,005
Other comprehensive loss				(968)	(968)
Stock option vesting		800			800
Stock options exercised	146,403	1,229			1,229
Tax benefit of stock options exercised		390			390
Repurchase of common stock	(74,018)	(373)	(991)		(1,364)
Dividends paid (\$0.40 per share)			(6,344)		(6,344)
Balance at December 31, 2010	15,860,138	\$ 81,554	\$ 117,533	\$ 1,310	\$ 200,397
Net income			18,590		18,590
Other comprehensive income				2,501	2,501
Stock option vesting		830			830
Stock option forfeiture		(114)			(114)
Stock options exercised	296,250	2,428			2,428
Tax benefit of stock options exercised		296			296
Repurchase of common stock	(177,430)	(915)	(1,830)		(2,745)
Dividends paid (\$0.36 per share)			(5,742)		(5,742)
Balance at December 31, 2011	15,978,958	\$ 84,079	\$ 128,551	\$ 3,811	\$ 216,441

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Net income	18,994	18,994
Other comprehensive loss		(1,652)
Stock option vesting	1,083	1,083
Stock options exercised		