

FIRST PACTRUST BANCORP INC

Form 10-Q

April 29, 2011

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2011

**FIRST PACTRUST BANCORP, INC.**

(Exact name of registrant as specified in its charter)

**000-49806**

(Commission File Number)

**Maryland**

(State of incorporation)

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**04-3639825**

**(IRS Employer Identification No.)**

**610 Bay Boulevard, Chula Vista, California**

**(Address of Principal Executive Offices)**

**91910**

**(ZIP Code)**

**(619) 691-1519**

**(Registrant's telephone number, including area code)**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  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 (p232.405) 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 whether the Registrant is a large accelerated filer; an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of accelerated filer and large accelerated filer in Rule 12B-2 of the Exchange Act.

Large accelerated Filer  Accelerated Filer  Non-accelerated Filer  Smaller reporting company   
Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.) Yes  No

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

As of April 27, 2010 the Registrant had 9,729,066 outstanding shares of common stock.

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**FIRST PACTRUST BANCORP, INC.**

Form 10-Q Quarterly Report

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**Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995**

This report contains certain forward-looking statements within the meaning of Section 27a of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. First PacTrust Bancorp, Inc. (the Company) and Pacific Trust Bank (the Bank) intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Reform Act of 1995, as amended, and are including this statement for purposes of these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies, and expectations of the Company and the Bank, are generally identifiable by use of the words such as believe, expect, intend, anticipate, estimate, project, or similar expressions. The ability of the Company and the Bank to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors that could have a material adverse effect on the operations and future prospects of the Company, the Bank, and the Bank's wholly owned subsidiaries include, but are not limited to, changes in: interest rates; the economic health of the local real estate market; general economic conditions; legislative/regulatory provisions; monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Federal Reserve Board; the quality or composition of the loan and securities portfolios; demand for loan products; deposit flows; competition; demand for financial services in the Bank's market area; and impact of new accounting pronouncements. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements.

**Table of Contents****ITEM 1 FINANCIAL STATEMENTS****First PacTrust Bancorp, Inc.****Consolidated Statements of Financial Condition****(In thousands of dollars except share data)****(Unaudited)**

|  | March 31,<br>2011 | December 31,<br>2010 |
|--|-------------------|----------------------|
| <b>ASSETS</b>  |                   |                      |
| Cash and due from banks  | \$ 5,090          | \$ 5,371             |
| Interest-bearing deposits  | 23,593            | 53,729               |
| Total cash and cash equivalents  | 28,683            | 59,100               |
| Securities available-for-sale  | 73,689            | 64,790               |
| Federal Home Loan Bank stock, at cost  | 7,993             | 8,323                |
| Loans, net of allowance of \$11,905 at March 31, 2011 and \$14,637 at December 31, 2010  | 670,579           | 678,175              |
| Accrued interest receivable  | 3,465             | 3,531                |
| Real estate owned, net   | 6,433             | 6,562                |
| Premises and equipment, net  | 8,249             | 6,344                |
| Bank owned life insurance investment   | 18,215            | 18,151               |
| Prepaid FDIC assessment  | 3,156             | 3,521                |
| Other assets   | 14,521            | 13,124               |
| Total assets   | \$ 834,983        | \$ 861,621           |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>   |                   |                      |
| Deposits   |                   |                      |
| Noninterest-bearing  | \$ 18,066         | \$ 15,171            |
| Interest-bearing   | 47,381            | 44,860               |
| Money market accounts  | 88,287            | 89,708               |
| Savings accounts   | 135,064           | 124,620              |
| Certificates of deposit  | 345,612           | 371,949              |
| Total deposits   | 634,410           | 646,308              |
| Advances from Federal Home Loan Bank   | 60,000            | 75,000               |
| Accrued expenses and other liabilities   | 4,923             | 4,304                |
| Total liabilities  | 699,333           | 725,612              |
| Commitments and contingent liabilities   |                   |                      |
| <b>SHAREHOLDERS EQUITY</b>   |                   |                      |
| Preferred stock, \$.01 par value per share, \$1,000 per share liquidation preference, 5,000,000 shares authorized, 19,300 shares issued and outstanding at December 31, 2010   |                   |                      |
| Common stock, \$.01 par value per share, 17,163,844 shares authorized; 9,863,390 shares issued and 9,729,066 shares outstanding at March 31, 2011; 9,863,390 shares issued and 8,693,228 shares outstanding at December 31, 2010 | 99                | 99                   |
| Class B non-voting non-convertible Common stock, \$.01 par value per share, 2,836,156 shares authorized; 1,036,156 shares issued and outstanding at March 31, 2011 and December 31, 2010   | 10                | 10                   |
| Additional paid-in capital   | 119,497           | 119,998              |
| Additional paid-in capital-warrants  | 3,172             | 3,172                |
| Retained earnings  | 35,448            | 35,773               |

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|  |                   |                   |
|--|-------------------|-------------------|
| Treasury stock, at cost (March 31, 2011 1,170,480 shares, December 31, 2010 1,170,162 shares,)                       | (25,139)          | (25,135)          |
| Unearned Employee Stock Ownership Plan (ESOP) shares (March 31, 2011 31,740 shares, December 31, 2010 42,320 shares) | (381)             | (507)             |
| Accumulated other comprehensive income   | 2,944             | 2,599             |
| <b>Total shareholders equity</b>   | <b>135,650</b>    | <b>136,009</b>    |
| <b>Total liabilities and shareholders equity</b>   | <b>\$ 834,983</b> | <b>\$ 861,621</b> |

See accompanying notes to consolidated financial statements.

**Table of Contents****First PacTrust Bancorp, Inc.****Consolidated Statements of Income (Loss)****(In thousands of dollars except per share data)****(Unaudited)**

|  | <b>Three months ended<br/>March 31,</b> |               |
|--|---|---------------|
|  | <b>2011</b>                             | <b>2010</b>   |
| Interest and dividend income                               |   |               |
| Loans, including fees                                      | \$ 7,666                                | \$ 9,165      |
| Securities   | 1,244                                   | 1,330         |
| Dividends and other interest-earning assets                | 39                                      | 24            |
| <b>Total interest and dividend income</b>                  | <b>8,949</b>                            | <b>10,519</b> |
| Interest expense   |   |               |
| Savings  | 90                                      | 242           |
| NOW  | 16                                      | 32            |
| Money market   | 66                                      | 173           |
| Certificates of deposit                                    | 1,105                                   | 1,844         |
| Federal Home Loan Bank advances                            | 517                                     | 888           |
| <b>Total interest expense</b>                              | <b>1,794</b>                            | <b>3,179</b>  |
| <b>Net interest income</b>                                 | <b>7,155</b>                            | <b>7,340</b>  |
| Provision for loan losses                                  |   | 2,214         |
| <b>Net interest income after provision for loan losses</b> | <b>7,155</b>                            | <b>5,126</b>  |
| Noninterest income   |   |               |
| Customer service fees                                      | 338                                     | 314           |
| Income from bank owned life insurance                      | 64                                      | 47            |
| Net gain on sales of securities available-for-sale         | 319                                     |               |
| Other  | 46                                      | 6             |
| <b>Total noninterest income</b>                            | <b>767</b>                              | <b>367</b>    |
| Noninterest expense  |   |               |
| Salaries and employee benefits                             | 3,381                                   | 1,628         |
| Occupancy and equipment                                    | 664                                     | 488           |
| Advertising  | 60                                      | 110           |
| Professional fees  | 335                                     | 168           |
| Stationery paper, supplies, and postage                    | 115                                     | 86            |
| Data processing  | 293                                     | 280           |
| ATM costs  | 64                                      | 73            |
| FDIC expense   | 383                                     | 380           |
| Loan servicing and foreclosure                             | (76)                                    | 568           |
| Operating loss on equity investment                        | 78                                      | 82            |
| Valuation allowance for OREO                               | 421                                     |               |
| Loss on sale of other real estate owned                    | 768                                     |               |
| Other general and administrative                           | 330                                     | 396           |
| <b>Total noninterest expense</b>                           | <b>6,816</b>                            | <b>4,259</b>  |

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|  |               |               |
|--|---------------|---------------|
| <b>Income before income taxes</b>                  | 1,106         | 1,234         |
| Income tax expense                                 | 413           | 359           |
| <b>Net income</b>                                  | 693           | 875           |
| Preferred stock dividends and discount accretion   |               | 250           |
| <b>Net income available to common shareholders</b> | <b>\$ 693</b> | <b>\$ 625</b> |
| Basic earnings per share                           | \$ .07        | \$ .15        |
| Diluted earnings per share                         | \$ .07        | \$ .15        |

See accompanying notes to consolidated financial statements.

**Table of Contents****First PacTrust Bancorp, Inc.****Consolidated Statements of Cash Flows****(In thousands of dollars)****(Unaudited)**

|  | <b>Three months ended<br/>March 31,</b> |             |
|--|---|-------------|
|  | <b>2011</b>                             | <b>2010</b> |
| <b>Cash flows from operating activities</b>  |   |             |
| Net income   | \$ 693                                  | \$ 875      |
| Adjustments to reconcile net income to net cash provided by operating activities           |   |             |
| Provision for loan losses  |   | 2,214       |
| Net accretion of securities  | (240)                                   | (518)       |
| Depreciation and amortization  | 130                                     | 97          |
| Employee stock ownership plan compensation expense   | 183                                     | 71          |
| Stock option compensation expense  | 164                                     | 3           |
| Stock award compensation expense   | 32                                      | 6           |
| Bank owned life insurance income   | (64)                                    | (47)        |
| Operating loss on equity investment  | 78                                      | 82          |
| Gain on sale of securities available-for-sale  | (319)                                   |             |
| Loss on sale of real estate owned  | 768                                     | 340         |
| Deferred income tax (benefit)/expense  | (1,018)                                 | 314         |
| Decrease in valuation allowances on other real estate owned                                | (170)                                   |             |
| Net change in:   |   |             |
| Deferred loan costs  | 60                                      | 72          |
| Accrued interest receivable  | 66                                      | 276         |
| Other assets   | 2,749                                   | 2,778       |
| Accrued interest payable and other liabilities   | 1,584                                   | 231         |
| Net cash provided by operating activities  | 4,696                                   | 6,794       |
| <b>Cash flows from investing activities</b>  |   |             |
| Proceeds from sales of securities available-for-sale                                       | 6,478                                   |             |
| Proceeds from maturities, calls, and principal repayments of securities available-for-sale | 4,826                                   | 3,299       |
| Purchases of securities available-for-sale   | (20,342)                                | (20,455)    |
| Loan originations and principal collections, net   | 1,787                                   | 9,734       |
| Redemption of Federal Home Loan Bank stock   | 330                                     |             |
| Proceeds from sale of real estate owned  | 2,517                                   | 2784        |
| Additions to premises and equipment  | (2,035)                                 | (18)        |
| Net cash from investing activities   | (6,439)                                 | (4,656)     |
| <b>Cash flows from financing activities</b>  |   |             |
| Repurchase of Warrants, TARP   | (1,003)                                 |             |
| Net increase/(decrease) in deposits  | (11,898)                                | 33,218      |
| Repayments of Federal Home Loan Bank advances  | (15,000)                                | (25,000)    |
| Net proceeds from stock issuance   | (45)                                    |             |
| Purchase of treasury stock   | (4)                                     | (3)         |
| Tax benefit/(loss) from RRP shares vesting   | (1)                                     | (4)         |
| Tax Effect of ESOP   | 148                                     |             |
| Tax Effect of Options redeemed   | 147                                     |             |
| Dividends paid on preferred stock  |   | (241)       |
| Dividends paid on common stock   | (1,018)                                 | (208)       |

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|  |                  |                  |
|--|------------------|------------------|
| Net cash from financing activities   | (28,674)         | 7,762            |
| Net change in cash and cash equivalents                                    | (30,417)         | 9,900            |
| Cash and cash equivalents at beginning of year                             | 59,100           | 34,596           |
| <b>Cash and cash equivalents at end of year</b>                            | <b>\$ 28,683</b> | <b>\$ 44,496</b> |
| Supplemental cash flow information   |                  |                  |
| Interest paid on deposits and borrowed funds                               | \$ 1,824         | \$ 3,197         |
| Income taxes paid  | 0                | 0                |
| Supplemental disclosure of noncash activities                              |                  |                  |
| Transfer from loans to loans provided for sales of other real estate owned | 0                | 0                |
| Transfer from loans to real estate owned, net                              | 3,232            | 6,902            |

See accompanying notes to consolidated financial statements.

**Table of Contents****First PacTrust Bancorp, Inc.****Consolidated Statements of ShareHolder s Equity****(In thousands of dollars, except share and per share data)****(Unaudited)**

|  | Preferred<br>Stock | Common<br>Stock | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Treasury<br>Stock | Unearned<br>ESOP | Additional<br>Paid in<br>capital<br>Warrants | Accumulated<br>Other<br>Comprehensive<br>Income | Total      |
|--|--------------------|-----------------|----------------------------------|----------------------|-------------------|------------------|--|---|------------|
| Balance at January 1, 2010   | \$ 19,094          | \$ 54           | \$ 67,958                        | \$ 35,515            | \$ (25,788)       | \$ (1,015)       |  | \$ 1,667  | \$ 97,485  |
| Net Income   |                    |                 |                                  | 2,825                |                   |                  |  |   | 2,825      |
| Change in net unrealized<br>gain (losses) on securities<br>available-for-sale, net of<br>reclassification and tax<br>effects |                    |                 |                                  |                      |                   |                  |  | 932   | 932        |
| Total comprehensive income   |                    |                 |                                  |                      |                   |                  |  |   | 3,757      |
| Forfeiture and retirement of<br>stock  |                    |                 | 10                               |                      | (10)              |                  |  |   |            |
| Stock option compensation<br>expense   |                    |                 | 94                               |                      |                   |                  |  |   | 94         |
| Stock awards earned  |                    |                 | 29                               |                      |                   |                  |  |   | 29         |
| Amortization of preferred<br>stock discount  | 35                 |                 |                                  | (35)                 |                   |                  |  |   |            |
| Repurchased of Preferred<br>Stock  | (19,129)           |                 | (171)                            |                      |                   |                  |  |   | (19,300)   |
| Issuance of stock awards   |                    |                 | (668)                            |                      | 668               |                  |  |   |            |
| Issuance of warrants   |                    |                 |                                  |                      |                   |                  | 3,172  |   | 3,172      |
| Purchase of 506 shares of<br>treasury stock  |                    |                 |                                  |                      | (5)               |                  |  |   | (5)        |
| Employee stock ownership<br>plan shares earned   |                    |                 | (53)                             |                      |                   | 508              |  |   | 455        |
| Tax benefit/(loss) of RRP<br>shares vesting  |                    |                 | (6)                              |                      |                   |                  |  |   | (6)        |
| Dividends declared (\$.25 per<br>common share)   |                    |                 |                                  | (1,503)              |                   |                  |  |   | (1,503)    |
| Preferred stock dividends  |                    |                 |                                  | (925)                |                   |                  |  |   | (925)      |
| Warrant dividends  |                    |                 |                                  | (104)                |                   |                  |  |   | (104)      |
| Net proceeds from stock<br>issuance  |                    | 55              | 52,805                           |                      |                   |                  |  |   | 52,860     |
| Balance at December 31,<br>2010  | \$                 | \$ 109          | \$ 119,998                       | \$ 35,773            | \$ (25,135)       | \$ (507)         | \$ 3,172                                     | \$ 2,599  | \$ 136,009 |
| Net Income   |                    |                 |                                  | 693                  |                   |                  |  |   | 693        |
| Change in net unrealized<br>gain (losses) on securities<br>available-for-sale, net of<br>reclassification and tax            |                    |                 |                                  |                      |                   |                  |  | 345   | 345        |

effects

|                            |       |
|----------------------------|-------|
| Total comprehensive income | 1,038 |
|----------------------------|-------|

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|  | Preferred<br>Stock | Common<br>Stock | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Treasury<br>Stock | Unearned<br>ESOP | Additional<br>Paid in<br>capital<br>Warrants | Accumulated<br>Other<br>Comprehensive<br>Income | Total      |
|--|--------------------|-----------------|----------------------------------|----------------------|-------------------|------------------|--|---|------------|
| Stock option compensation expense            |                    |                 | 164                              |                      |                   |                  |  |   | 164        |
| Stock awards earned                          |                    |                 | 32                               |                      |                   |                  |  |   | 32         |
| Purchase of 318 shares of treasury stock     |                    |                 |                                  |                      | (4)               |                  |  |   | (4)        |
| Employee stock ownership plan shares earned  |                    |                 | 57                               |                      |                   | 126              |  |   | 183        |
| Tax benefit/(loss) of RRP shares vesting     |                    |                 | (1)                              |                      |                   |                  |  |   | (1)        |
| Dividends declared (\$.105 per common share) |                    |                 |                                  | (1,018)              |                   |                  |  |   | (1,018)    |
| Repurchase of Warrants-TARP                  |                    |                 | (1,003)                          |                      |                   |                  |  |   | (1,003)    |
| Tax Effect ESOP                              |                    |                 | 148                              |                      |                   |                  |  |   | 148        |
| Tax Effect Options Redeemed                  |                    |                 | 147                              |                      |                   |                  |  |   | 147        |
| Net proceeds from stock issuance             |                    |                 | (45)                             |                      |                   |                  |  |   | (45)       |
| Balance at March 31, 2011                    | \$                 | \$ 109          | \$ 119,497                       | \$ 35,448            | \$ (25,139)       | \$ (381)         | \$ 3,172                                     | \$ 2,944  | \$ 135,650 |

See accompanying notes to consolidated financial statements.

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FIRST PACTRUST BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2011

(Amounts in thousands of dollars, except share and per share data)

NOTE 1 BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements include the accounts of First PacTrust Bancorp, Inc. (the Company) and its wholly owned subsidiary Pacific Trust Bank (the Bank) as of March 31, 2011 and December 31, 2010 and for the three month periods ended March 31, 2011 and March 31, 2010. Significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying unaudited interim consolidated financial statements have been prepared pursuant to the rules and regulations for reporting on Form 10-Q. Accordingly, certain disclosures required by U.S. generally accepted accounting principles are not included herein. These interim statements should be read in conjunction with the consolidated financial statements and notes included in the Annual Report on Form 10-K filed by the Company with the Securities and Exchange Commission. The December 31, 2010 balance sheet presented herein has been derived from the audited financial statements included in the Annual Report on Form 10-K filed with the Securities and Exchange Commission, but does not include all of the disclosures required by U.S. generally accepted accounting principles.

Interim statements are subject to possible adjustment in connection with the annual audit of the Company for the year ending December 31, 2011. In the opinion of management of the Company, the accompanying unaudited interim consolidated financial statements reflect all of the adjustments (consisting of normal recurring adjustments) necessary for a fair presentation of the consolidated financial position and consolidated results of operations for the periods presented.

The results of operations for the three month periods ended March 31, 2011 are not necessarily indicative of the results to be expected for the full year.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

*Principles of Consolidation:* The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, the Bank. All significant intercompany transactions and balances are eliminated in consolidation.

*Nature of Operations:* The principal business of the Company is the ownership of the Bank. The Bank is a federally chartered stock savings bank and a member of the Federal Home Loan Bank (FHLB) system, which maintains insurance on deposit accounts with the Federal Deposit Insurance Corporation.

The Bank is engaged in the business of retail banking, with operations conducted through its main office and eight branches located in San Diego and Riverside counties. In addition, the Bank opened a loan production office in Los Angeles, California during the first quarter of 2011. Loan production is expected to expand throughout southern California during the coming quarters. There are no significant concentrations of loans to any one industry or customer. However, the customer's ability to repay their loans is dependent on the real estate market and general economic conditions in the area.

The accounting and reporting policies of the Company are based upon U.S. generally accepted accounting principles and conform to predominant practices within the banking industry. Significant accounting policies followed by the Company are presented below.

*Use of Estimates in the Preparation of Financial Statements:* The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and disclosures provided, and actual results could differ. The allowance for loan losses, other real estate owned, realization of deferred tax assets, and the fair value of financial instruments are particularly subject to change.

*Cash Flows:* Cash and cash equivalents include cash on hand, deposits with other financial institutions under 90 days, and daily federal funds sold. Net cash flows are reported for customer loan and deposit transactions, interest bearing deposits in other financial institutions, and federal funds purchased, including overnight borrowings with the Federal Home Loan Bank.

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*Interest-bearing Deposits in Other Financial Institutions:* Interest-bearing deposits in other financial institutions mature within one year and are carried at cost.

*Securities:* Debt securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Debt securities are classified as available-for-sale when they might be sold before maturity. Equity securities with readily determinable fair values are classified as available-for-sale. Securities available-for-sale are carried at fair value with unrealized holding gains and losses, net of taxes, reported in other comprehensive income, net of tax.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized on the level-yield method without anticipating prepayments, except for mortgage backed securities where prepayments are anticipated. Gains and losses on sales are recorded on the trade date and determined using the specific identification method.

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Management evaluates securities for other-than-temporary impairment ( OTTI ) on at least a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. See further discussion in Note 2- Securities.

*Federal Home Loan Bank (FHLB) Stock:* The Bank is a member of the FHLB system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. FHLB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income.

*Affordable Housing Fund:* The Company has a 19% equity investment in an affordable housing fund originally totaling \$4.2 million for purposes of obtaining tax credits and for Community Reinvestment Act purposes. This investment is accounted for using the equity method of accounting. Under the equity method of accounting, the Company recognizes its ownership share of the profits and losses of the fund. The Company obtains tax credits from these investments which reduce income tax expense for a period of 10 years. This investment is regularly evaluated for impairment by comparing the carrying value to the remaining tax credits expected to be received. For the three months ending March 31, 2011, 2010 and 2009 our share of the fund's operating loss was \$78 thousand, \$82 thousand and \$87 thousand, respectively. The balance of the investment at March 31, 2011 and December 31, 2010 was \$1.8 million and \$1.9 million, respectively, and is included in other assets.

*Loans:* Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, net of unearned interest, deferred loan fees and costs, and an allowance for loan losses. Interest income is accrued on the unpaid principal balance and includes amortization of net deferred loan fees and costs over the loan term. Interest income on mortgage and commercial loans is discontinued at the time the loan is 91 days delinquent unless the loan is well secured and in process of collection. Consumer loans, other than those secured by real estate, are typically charged off no later than 180 days past due. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not received for loans placed on nonaccrual, is reversed against interest income. Interest received on such loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

The Company's single family residential mortgage portfolio is comprised of a combination of traditional, fully-amortizing loans and non-traditional and/or interest only loans. In 2005 the Company introduced a fully-transactional flexible mortgage product called the Green Account. The Green Account is a mortgage line of credit which is secured by a first-deed of trust and which provides an associated clearing account that allows all types of deposits and withdrawals to be performed, including direct deposit, check, debit card, ATM, ACH debits and credits, and internet banking and bill payment transactions.

*Concentration of Credit Risk:* Most of the Company's business activity is with customers located within San Diego and Riverside Counties. Therefore, the Company's exposure to credit risk is significantly affected by changes in the economy in San Diego and Riverside County area.

*Allowance for Loan Losses:* The allowance for loan losses is maintained at a level considered adequate by management to provide for probable incurred loan losses. The allowance is increased by provisions charged against income, while loan losses are charged against the allowance when management deems a loan balance to be uncollectible. Subsequent recoveries, if any, are credited to the allowance. The Company performs an analysis of the adequacy of the allowance on a monthly basis. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged off. The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired. A loan is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. The Company evaluates all impaired loans individually under the guidance of ASC 310, primarily through the evaluation of collateral values and cash flows. Loans, for which the terms have been modified, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Troubled debt restructurings are also measured at the present value of estimated future cash flows using the loan's effective rate at inception or at the fair value of collateral if repayment is expected solely from the collateral. The general component covers loans that are not impaired and is determined by portfolio segment and is based on actual loss history experienced by the Company over the most recent 12 months. This actual loss experience is supplemented with other economic factors based on the risks present for each portfolio segment. These economic factors include consideration of the following: levels of and trends in delinquencies and impaired loans; levels of and trends in charge-offs and recoveries; trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other

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changes in lending policies, procedures, and practices; experience, ability, and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; effects of changes in credit concentrations and other factors. The historical loss analysis is also combined with a comprehensive loan to value analysis to analyze the associated risks in the current loan portfolio. An updated loan to value analysis is obtained from an independent firm semi-annually, most recently in November, 2010. Management uses available information to recognize loan losses, however, future loan loss provisions may be necessary based on changes in the above mentioned factors. In addition, regulatory agencies, as an

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integral part of their examination process, periodically review the allowance for loan losses and may require the Bank to recognize additional provisions based on their judgment of information available to them at the time of their examination.

The following portfolio segments have been identified: one-to four- family-fully amortizing, one-to four- family-negatively amortizing, one-to four-family interest only, multi-family, multi-family-negative amortizing, condominium conversions, secured commercial, unsecured commercial, land, home equity lines of credit, Green account- 1<sup>st</sup> trust deeds, Green account- 2<sup>nd</sup> trust deeds, Green account- multi-family, Green account- land, Green account- commercial, auto and other consumer. The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis includes all loans delinquent over 60 days and non-homogenous loans such as commercial and commercial real estate loans. Classification of problem single-family residential loans is performed on a monthly basis while analysis of non-homogenous loans is performed on a quarterly basis.

Loans secured by multi-family and commercial real estate properties generally involve a greater degree of credit risk than one-to four- family residential mortgage loans. Because payments on loan secured by multi-family and commercial real estate properties are often dependent on the successful operation or management of the properties, repayment of these loans may be subject to adverse conditions in the real estate market or the economy. Commercial business loans are also considered to have a greater degree of credit risk due to the fact these loans are typically made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business. As a result, the availability of funds for the repayment of commercial business loans may be substantially dependent on the success of the business itself (which, in turn, is often dependent in part upon general economic conditions). Consumer and other real estate loans may entail greater risk than do one- to four- family residential mortgage loans given that collection of these loans is dependent on the borrower's continuing financial stability and, thus, are more likely to be adversely affected by job loss, divorce, illness, or personal bankruptcy. Negatively amortizing and interest only loans are also considered to carry a higher degree of credit risk due to their unique cash flows. The Green Mortgages tend to have lower levels of delinquencies as a result of the borrower's ability to meet their monthly payments obligations by increasing the level of their line. Credit risk on this asset class is also managed through the completion of regular re-appraisals of the underlying collateral. In cases where the property values have declined to levels less than the original loan-to-value, or other levels deemed prudent by the Bank, the Bank may freeze the line and/or require monthly payments or principal reductions to bring the loan in balance.

*Classified Assets:* Federal regulations provide for the classification of loans and other assets, such as debt and equity securities considered by the Office of Thrift Supervision to be of lesser quality, as substandard, doubtful or loss. An asset is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets include those characterized by the distinct possibility that the insured institution will sustain some loss if the deficiencies are not corrected. The Bank includes in its classification of Substandard Assets loans that are performing under terms of a TDR, but where the borrower has yet to make six or more payments under the TDR, as well as loans where the borrower is current in his or her payments on the subject Classified Loan but may be a guarantor on another loan that is classified as a result of weakness in the credit or collateral ( Relationship ). As of March 31, 2011, the Bank had \$6.3 million of loans classified as substandard that were performing under a TDR for less than six months, and \$7.6 million of substandard loans where the borrower was current on all payments and the underlying collateral values left the Bank well secured, but where the Relationship was rated Substandard as result of the existence of personal guarantees. These two classes of Substandard loans represented 37.5% of the Bank's substandard assets as of March 31, 2011. Assets classified as doubtful have all of the weaknesses inherent in those classified substandard, with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. Assets classified as loss are those considered uncollectible and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted.

When an insured institution classifies problem assets as either substandard or doubtful, it may establish general or specific allowances for loan losses in an amount deemed prudent by management and approved by the Board of Directors. General allowances represent loss allowances which have been established to recognize the inherent risk associated with lending activities, but, unlike specific allowances, have not been allocated to particular problem assets. When an insured institution classifies problem assets as loss, it is required either to establish a specific allowance for losses equal to 100% of that portion of the asset so classified or to charge off such amount. An institution's determination as to the classification of its assets and the amount of its valuation allowances is subject to review by the Office of Thrift Supervision and the FDIC, which may order the establishment of additional general or specific loss allowances.

In connection with the filing of our periodic reports with the Office of Thrift Supervision and in accordance with our classification of assets policy, we regularly review the problem assets in our portfolio to determine whether any assets require classification in accordance with applicable regulations.

*Premises and Equipment:* Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation and are depreciated using the straight-line method with average useful lives ranging from five to forty years.

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Building and leasehold improvements are depreciated using the straight-line method over estimated useful lives not to exceed the lease term. Lease terms range up to ten years. Furniture, fixtures, and equipment are depreciated using the straight-line method with useful lives ranging from five to seven years. Maintenance and repairs are charged to expense as incurred, and improvements that extend the useful lives of assets are capitalized.

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*Real Estate Owned:* Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. In general, the Bank assumes a 9% cost when recording fair value. If fair value declines subsequent to foreclosure, a valuation allowance is recorded through expense. Operating costs after acquisition are expensed.

*Bank Owned Life Insurance:* The Bank has purchased life insurance policies on certain key executives. Bank owned life insurance is recorded at its cash surrender value (or the amount that can be realized). Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

*Long-term Assets:* Premises and equipment and other long-term assets are reviewed for impairment when events indicate their carrying amount may not be recoverable from future undiscounted cash flows. If impaired, the assets are recorded at fair value.

*Loan Commitments and Related Financial Statements:* Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

*Stock-Based Compensation:* Compensation cost is recognized for stock options and restricted stock awards issued to employees, based on the fair value of these awards at the date of grant. A Black-Scholes model is utilized to estimate the fair value of stock options, while the market price of the Company's common stock at the date of grant is used for restricted stock awards. Compensation cost is recognized over the required service period, generally defined as the vesting period. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award.

*Income Taxes:* Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized. A tax position is recognized as a benefit only if it is more likely than not that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the more likely than not test, no tax benefit is recorded.

The Company and its subsidiaries are subject to U.S. federal income tax as well as income tax of multiple state jurisdictions. The Company is no longer subject to examination by U.S. Federal taxing authorities for years before 2007 and for all state income taxes before 2006. The Company expects the total amount of unrecognized tax benefits to be recognized in 2011.

The Company recognizes interest and/or penalties related to income tax matters in income tax expense. The Company had \$0 accrued for interest and penalties at March 31, 2011 and December 31, 2010.

*Employee Stock Ownership Plan:* The cost of shares issued to the ESOP but not yet allocated to participants is shown as a reduction of shareholders' equity. Compensation expense is based on the average market price of shares as they are committed to be released to participant accounts. Dividends on allocated ESOP shares reduces retained earnings; dividends on unearned ESOP shares reduce debt and accrued interest. There were no shares forfeited for the three months ending March 31, 2011, 2010 and 2009.

*Earnings Per Common Share:* Basic earnings per common share is net income available to common shareholders divided by the weighted average number of common shares outstanding during the period. ESOP shares are considered outstanding for this calculation unless unearned. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable under stock options and stock awards. Dividends paid, and the accretion of discount on the Company's preferred stock, reduce the earnings available to common shareholders.

*Comprehensive Income:* Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on securities available for sale, net of tax, which are also recognized as a separate component of equity.

*Loss Contingencies:* Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there now are such matters that will have a material effect on the financial statements.

*Restrictions on Cash:* Cash on hand or on deposit with the Federal Reserve Bank was required to meet regulatory reserve and clearing requirements.

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*Fair Value of Financial Instruments:* Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

*Operating Segments:* While the chief decision-makers monitor the revenue streams of the various products and services, the identifiable segments are not material and operations are managed and financial performance is evaluated on a Company-wide basis.

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Operating segments are aggregated into one as operating results for all segments are similar. Accordingly, all of the financial service operations are considered by management to be aggregated in one reportable operating segment.

*Adoption of New Accounting Standards:* In July 2010, the FASB updated disclosure requirements with respect to the credit quality of financing receivables and the allowance for credit losses. According to the guidance, there are two levels of detail at which credit information must be presented – the portfolio segment level and class level. The portfolio segment level is defined as the level where financing receivables are aggregated in developing a Company’s systematic method for calculating its allowance for credit losses. The class level is the second level at which credit information will be presented and represents the categorization of financing related receivables at a slightly less aggregated level than the portfolio segment level. Companies will now be required to provide the following disclosures as a result of this update; a rollforward of the allowance for credit losses at the portfolio segment level with the ending balances further categorized according to impairment method along with the balance reported in the related financing receivables at period end; additional disclosure of nonaccrual and impaired financing receivables by class as of period end; credit quality and past due/aging information by class as of period end; information surrounding the nature and extent of loan modifications and troubled-debt restructurings and their effect on the allowance for credit losses during the period; and detail of any significant purchases or sales of financing receivables during the period. The increased period-end disclosure requirements become effective for periods ending on or after December 15, 2010, with the exception of the additional disclosures surrounding troubled-debt restructurings which were deferred in December 2010 and will be required for annual and interim reporting periods ending on or after June 15, 2011. The increased disclosures for activity within a reporting period became effective for periods beginning on or after December 15, 2010. The provisions of this update expanded the Company’s current disclosures with respect to the credit quality of our financing receivables in addition to our allowance for loan losses.

*Newly Issued But Not Yet Effective Accounting Standards:* In April 2011, the FASB issued an accounting standard updated to amend previous guidance with respect to troubled debt restructurings. This updated guidance is designed to assist creditors with determining whether or not a restructuring constitutes a troubled debt restructuring. In particular, additional guidance has been added to help creditors determine whether a concession has been granted and whether a debtor is experiencing financial difficulties. Both of these conditions are required to be met for a restructuring to constitute a troubled debt restructuring. The amendments in the update are effective for the first interim period beginning on or after June 15, 2011, and should be applied retrospectively to the beginning of the annual period of adoption. The provisions of this update are not expected to have a material impact on the Company’s financial position, results of operations or cash flows.

**NOTE 3 EMPLOYEE STOCK COMPENSATION**

The Company has two share based compensation plans as described below. Total compensation cost that has been charged against income for both plans was \$195 and \$9 thousand for the three months ended March 31, 2011 and March 31, 2010. The total income tax benefit and/or recovery was \$1 thousand and \$4 thousand, respectively.

**Recognition and Retention Plan**

A Recognition and Retention Plan ( RRP ) provides for the issuance of shares to directors, officers, and employees. Compensation expense is recognized over the vesting period of the shares based on the market value at date of grant. Pursuant to its 2003 stock-based incentive plan, total shares issuable under the plan are 211,600. At March 31, 2011, all 211,600 shares were issued. There were 9,598 shares granted during 2010 under the RRP. These shares vest over a five-year period. There were no shares issued or forfeited in 2011. Additionally, 21,500 one-time inducement restricted shares were granted during 2010 to newly hired executive officers. Of these shares, none were exercised during 2011. These one-time inducement shares vest over a three year period. Compensation expense for the restricted stock awards and inducement awards totaled approximately \$32 thousand for the three months ended March 31, 2011 and \$6 thousand for the three months ended March 31, 2010.

A summary of changes in the Company’s nonvested shares for the quarter ending March 31, 2011 follows:

|                              | Shares | Weighted-Average<br>Grant-Date<br>Fair-Value |
|------------------------------|--------|--|
| <b>Nonvested shares</b>      |        |  |
| Nonvested at January 1, 2011 | 12,378 | \$ 17.67                                     |
| Granted                      |        |  |
| Vested                       | 860    |  |
| Forfeited/expired            |        |  |

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|                             |        |    |       |
|-----------------------------|--------|----|-------|
| Nonvested at March 31, 2011 | 11,518 | \$ | 17.67 |
|-----------------------------|--------|----|-------|

A summary of changes in the Company's nonvested shares for the quarter ending March 31, 2010 follows:

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|                              | Shares  | Weighted-Average<br>Grant-Date<br>Fair-Value |
|------------------------------|---------|--|
| <b>Nonvested shares</b>      |         |  |
| Nonvested at January 1, 2010 | 206,800 | \$ 17.96                                     |
| Granted                      |         |  |
| Vested                       |         |  |
| Forfeited/expired            |         |  |
| Nonvested at March 31, 2010  | 206,800 | \$ 17.96                                     |

During the fourth quarter of 2010, an additional 21,500 inducement shares were awarded to newly hired executives. These shares were awarded at an average fair value of \$11.57. As of March 31, 2011, there was \$186 thousand of total unrecognized compensation cost related to 21,500 nonvested inducement awards. The cost is expected to be recognized over a weighted-average period of less than 3 years.

A summary of changes related to the Company's nonvested inducement awards for the quarter ending March 31, 2011 follows:

|                              | Shares | Weighted<br>Average<br>Exercise<br>Price |
|------------------------------|--------|--|
| Nonvested at January 1, 2011 | 21,500 | \$ 11.57                                 |
| Granted                      |        |  |
| Vested                       |        |  |
| Forfeited or expired         |        |  |
| Nonvested at March 31, 2011  | 21,500 | \$ 11.57                                 |

**Stock Options**

A Stock Option Plan (SOP) provides for the issuance of options to directors, officers, and employees. The Company adopted the SOP during 2003 under the terms of which 529,000 shares of the Company's common stock may be awarded. At March 31, 2011, the number of shares available for future awards was 16,500. The options become exercisable in equal installments over a five-year period from the date of grant. The options expire ten years from the date of grant. The fair value of options granted are computed using option pricing models, using the following weighted-average assumptions as of grant date. The fair value of each option award is estimated on the date of grant using a closed form option valuation (Black-Scholes) model that uses the assumptions noted in the table below. Expected volatilities are based on historical volatilities of the Company's common stock. The Company uses historical data to estimate option exercise and post-vesting termination behavior. The expected term of options granted is based on historical data and represents the period of time that options granted are expected to be outstanding, which takes into account that the options are not transferable. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant. There were no options granted in 2011 or 2010 under the current SOP.

The following table represents stock option activity during the three months ended March 31, 2011:

|                                  | Shares    | Weighted<br>Average<br>Exercise<br>Price |
|----------------------------------|-----------|--|
| Outstanding at Beginning of year | 482,386   | \$ 18.32                                 |
| Granted                          |           |  |
| Exercised                        |           |  |
| Forfeited or expired             | (482,386) |  |
| Outstanding at end of period     |           |  |

Fully vested and expected to vest

Options exercisable at March 31, 2011

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There were 770,000 one-time inducement options issued to newly hired executive officers during 2010 at an average fair value of \$11.42. These one-time inducement options were granted outside of the existing SOP plan and are not a part of a new SOP plan. None of these options were exercised during 2011. These options have a three year vesting. As of March 31, 2011, there was \$1.7 million of total unrecognized compensation cost related to nonvested stock options. The cost is expected to be recognized over a weighted-average period of less than 3 years.

The following table represents inducement option activity during the three months ended March 31, 2011:

|                                    | Shares  | Weighted<br>Average<br>Exercise Price |
|------------------------------------|---------|---------------------------------------|
| Outstanding at Beginning of year   | 770,000 | \$ 11.42                              |
| Granted                            |         |                                       |
| Exercised                          |         |                                       |
| Forfeited or expired               |         |                                       |
| Outstanding at March 31, 2011      | 770,000 | \$ 11.42                              |
| Fully vested and expected to vest  |         |                                       |
| Options exercisable at quarter-end |         |                                       |

Information related to the stock option plan during each year follows:

|  | 2011 | 2010 | 2009 |
|--|------|------|------|
| Intrinsic value of options exercised       | \$   | \$   | \$   |
| Cash received from option exercises        |      |      |      |
| Tax benefit realized from option exercises |      |      |      |

The intrinsic value for stock options is calculated based on the exercise price of the underlying awards and the market price of our common stock as of the reporting date. ASC 718 and 505 require the recognition of stock based compensation for the number of awards that are ultimately expected to vest. As a result, recognized stock compensation expense was reduced for estimated forfeitures prior to vesting primarily based on historical annual forfeiture rates of approximately 5% for senior management and the board of directors and 45% for all other employees. Estimated forfeitures will be reassessed in subsequent periods and may change based on new facts and circumstances. The Company recorded stock compensation expense of \$164 thousand and \$3 thousand as salary and employee benefits expense during the three months ended March 31, 2011 and 2010, respectively.

**Warrants**

On November 1, 2010, the Company issued warrants to TCW Shared Opportunity Fund V, L.P. for up to 240,000 shares of non-voting common stock at an exercise price of \$11.00 per share, subject to anti-dilutive adjustments. These warrants are exercisable from the date of issuance through November 1, 2015. On November 1, 2010, the Company also issued warrants to COR Advisors LLC to purchase up to 1,395,000 shares of non-voting stock at an exercise price of \$11.00 per share, subject to anti-dilutive adjustments. These warrants are exercisable with respect to 95,000 shares on January 1, 2011 and an additional 130,000 shares on the first day of each of the next ten calendar quarterly periods beginning with April 1, 2011, subject to earlier vesting upon a change in control of the Company or in the discretion of our board of directors. These warrants are exercisable with respect to each vesting tranche for five years after the tranche's vesting date. The warrants are exercisable for voting common stock in lieu of non-voting common stock following the transfer of the warrants in a widely disbursed offering or in other limited circumstances.

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## NOTE 4 EARNINGS/(LOSS) PER SHARE

Basic earnings/(loss) per share were computed by dividing net income/(loss) by the weighted average number of shares outstanding. Diluted earnings/(loss) per share were computed by dividing net income/(loss) by the weighted average number of shares outstanding, adjusted for the dilutive effect of the outstanding stock options and restricted stock awards. Computations for basic and diluted earnings/(loss) per share are provided below.

|   | Three months ended<br>March 31, |                  |
|---|---------------------------------|------------------|
|   | 2011                            | 2010             |
| <b>Basic</b>  |                                 |                  |
| Net income/(loss)   | \$ 693                          | \$ 875           |
| Less: Dividends on preferred stock  |                                 | (241)            |
| Less: Imputed dividends   |                                 | (9)              |
| <b>Net income/(loss) available to common shareholders</b>                             | <b>\$ 693</b>                   | <b>\$ 625</b>    |
| Weighted average common shares outstanding  | 9,661,447                       | 4,181,073        |
| <b>Basic earnings/(loss) per share</b>  | <b>\$ 0.07</b>                  | <b>\$ 0.15</b>   |
| <b>Diluted</b>  |                                 |                  |
| Net income/(loss) available to common shareholders                                    | \$ 693                          | \$ 625           |
| Weighted average common shares outstanding for basic earnings/(loss) per common share | 9,661,447                       | 4,181,073        |
| Add: Dilutive effects of stock options  |                                 |                  |
| Add: Dilutive effects of stock awards   | 3,826                           |                  |
| <b>Average shares and dilutive potential common shares</b>                            | <b>9,665,273</b>                | <b>4,181,073</b> |
| <b>Diluted earnings/(loss) per common share</b>                                       | <b>\$ 0.07</b>                  | <b>\$ 0.15</b>   |

All outstanding options and 1,514 stock awards were not considered in computing diluted earnings per common share for the period ending March 31, 2011 and March 31, 2010 because they were anti-dilutive. They were anti-dilutive since the exercise prices were greater than the average market price of the common stock.

## NOTE 5 FAIR VALUES OF FINANCIAL INSTRUMENTS

**Fair Value Hierarchy.** ASC 820-10 establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The topic describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing and asset or liability.

**Investment Securities Available for Sale.** The fair values of securities available for sale are determined by matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific

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securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3). The fair values of the Company's Level 3 securities are by the Company and an independent third-party provider using a discounted cash flow methodology. The methodology uses discount rates that are based upon observed market yields for similar securities. Prepayment speeds are estimated based upon the prepayment history of each bond and a detailed analysis of the underlying collateral. Gross weighted average coupon, geographic concentrations, loan to value, FICO and seasoning are among the different loan attributes that are factored into our prepayment curve. Default rates and severity are estimated based upon geography of the collateral, delinquency, modifications, loan to value ratios, FICO scores, and past performance.

Impaired Loans. The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for

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differences between the comparable sales and income data available. Such adjustments are typically significant and result in a Level 3 classification of the inputs for determining fair value.

**Real Estate Owned Assets.** Real estate owned assets (OREO) are recorded at the lower of cost or fair value less estimated costs to sell at the time of foreclosure. The fair value of real estate owned assets is generally based on recent real estate appraisals adjusted for estimated selling costs. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a Level 3 classification of the inputs for determining fair value.

**Assets and Liabilities Measured on a Recurring and Non Recurring Basis**

Available for sale securities are measured at fair value on a recurring basis, impaired loans and real estate owned are measured at fair value on a non-recurring basis.

|  | Fair Value Measurements at March 31, 2011 Using |  |   |   |
|--|---|--|---|---|
|  | Carrying Value                                  | Quoted Prices in Active Markets for Identical Assets (Level One) | Significant Other Observable Inputs (Level Two) | Significant Unobservable Inputs (Level Three) |
| <b>Assets</b>  |   |  |   |   |
| U.S. government sponsored entities and agency securities (recurring) | \$ 16,722                                       | \$   | \$ 16,722                                       | \$  |
| Private label residential mortgage-backed securities (recurring)     | 52,097  |  |   | 52,097  |
| Federal National Mortgage Association securities (recurring)         | 3   |  | 3   |   |
| Government National Mortgage Association securities (recurring)      | 4,867   |  | 4,867   |   |
| Impaired loans (non recurring)                                       | 22,226  |  |   | 22,226  |
| Real estate owned assets (non recurring)                             | 6,433   |  |   | 6,433   |

The table below presents a reconciliation of all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the period ended March 31, 2011 :

|  | Investment Securities Available-for-sale |
|--|--|
| Balance of recurring Level 3 assets at January 1, 2011 | \$ 54,246                                |
| Total gains or losses (realized/unrealized):           |  |
| Included in earnings realized                          | 319                                      |
| Included in earnings unrealized                        |  |
| Included in other comprehensive income                 | (2,282)                                  |
| Purchases  | 20,342                                   |
| Sales, issuances and settlements                       | (20,528)                                 |
| Net transfers in and/or out of Level 3                 |  |
| Balance of recurring Level 3 assets at March 31, 2011  | \$ 52,097                                |

There were no significant transfers between Level 1 and Level 2 during the quarter ended March 31, 2011.

Impaired loans with specific valuation allowances are measured for impairment using the fair value of the collateral for collateral dependent loans. At March 31, 2011, impaired loans totaled \$22.2 million and had a carrying amount of \$18.4 million, net of a valuation allowance of \$3.9 million at March 31, 2011. At March 31, 2011, these impaired loans consisted of \$13.0 million of single-family residential loans, one land loan totaling \$738 thousand and two multi-family loan totaling \$8.5 million. Other real estate owned which is measured at the lower of carrying or fair value less costs to sell, had a net had a carrying amount of \$6.4 million, which is made up of the outstanding balance of \$6.4 million, net of a

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valuation allowance of \$5 thousand at December 31, 2010, resulting in expense of \$421 thousand for the quarter ending March 31, 2011.

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The table below presents a reconciliation of all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the period ended December 31, 2010:

|  | Fair Value Measurements at December 31, 2010 Using |  |   |   |
|--|--|--|---|---|
|  | Carrying Value                                     | Quoted Prices in Active Markets for Identical Assets (Level One) | Significant Other Observable Inputs (Level Two) | Significant Unobservable Inputs (Level Three) |
| <b>Assets</b>  |  |  |   |   |
| U.S. government sponsored entities and agency securities (recurring) | \$ 5,055   | \$   | \$ 5,055  | \$  |
| Private label residential mortgage-backed securities (recurring)     | 54,246   |  |   | 54,246  |
| Federal National Mortgage Association securities (recurring)         | 3  |  | 3   |   |
| Government National Mortgage Association securities (recurring)      | 5,485  |  | 5,485   |   |
| Impaired loans (non recurring)                                       | 23,936   |  |   | 23,936  |
| Real estate owned assets (non recurring)                             | 6,562  |  |   | 6,562   |

The table below presents a reconciliation of all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the period ended December 31, 2010:

|  | Investment Securities Available-for-sale |
|--|--|
| Balance of recurring Level 3 assets at January 1, 2010   | \$ 47,131                                |
| Total gains or losses (realized/unrealized):             |  |
| Included in earnings realized                            |  |
| Included in earnings unrealized                          |  |
| Included in other comprehensive income                   | 1,590                                    |
| Purchases  | 29,110                                   |
| Sales, issuances and settlements                         | (23,585)                                 |
| Net transfers in and/or out of Level 3                   |  |
| Balance of recurring Level 3 assets at December 31, 2010 | 54,246                                   |

There were no significant transfers between Level 1 and Level 2 during 2010.

Impaired loans, with specific valuation allowances are measured for impairment using the fair value of the collateral for collateral dependent loans totaled \$23.9 million and had a carrying amount of \$19.6 million, net of a valuation allowance of \$4.4 million at December 31, 2010. At December 31, 2010, these impaired loans consisted of \$15.3 million single-family loans, \$8.5 million multi-family loans and one HELOC totaling \$108 thousand. During the year ended December 31, 2010, a provision of \$4.4 million was made for these loans, net of charge-offs previously provided.

Other real estate owned which is measured at the lower of carrying or fair value less costs to sell, had a net had a carrying amount of \$6.5 million, which is made up of the outstanding balance of \$9.9 million, net of a valuation allowance of \$3.4 million at December 31, 2009, resulting in expense of \$2.7 million for the year ending December 31, 2010.

In accordance with ASC 825-10, the carrying amounts and estimated fair values of financial instruments, at March 31, 2011 and December 31, 2010 were as follows:

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|                               | March 31, 2011     |                            | December 31, 2010  |                            |
|-------------------------------|--------------------|----------------------------|--------------------|----------------------------|
|                               | Carrying<br>Amount | Estimated<br>Fair<br>Value | Carrying<br>Amount | Estimated<br>Fair<br>Value |
| Financial assets              |                    |                            |                    |                            |
| Cash and cash equivalents     | \$ 28,683          | \$ 28,683                  | \$ 59,100          | \$ 59,100                  |
| Securities available-for-sale | 73,689             | 73,689                     | 64,790             | 64,790                     |
| FHLB stock                    | 7,993              | N/A                        | 8,323              | N/A                        |

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|                             | March 31, 2011  |                      | December 31, 2010 |                      |
|-----------------------------|-----------------|----------------------|-------------------|----------------------|
|                             | Carrying Amount | Estimated Fair Value | Carrying Amount   | Estimated Fair Value |
| Loans receivable, net       | 670,579         | 678,615              | 678,175           | 690,229              |
| Real estate owned, net      | 6,433           | 6,433                | 6,562             | 6,562                |
| Accrued interest receivable | 3,465           | 3,465                | 3,531             | 3,531                |
| Financial liabilities       |                 |                      |                   |                      |
| Deposits                    | \$ 634,410      | \$ 636,805           | \$ 646,308        | \$ 628,319           |
| Advances from the FHLB      | 60,000          | 60,514               | 75,000            | 75,959               |
| Accrued interest payable    | 195             | 195                  | 225               | 225                  |

The methods and assumptions used to estimate fair value are described as follows:

Carrying amount is the estimated fair value for cash and cash equivalents, interest bearing deposits in other financial institutions, accrued interest receivable and payable, demand deposits, short-term debt, and variable rate loans or deposits that re-price frequently and fully. The methods for determining the fair values for securities were described previously. For fixed rate loans or deposits and for variable rate loans or deposits with infrequent re-pricing or re-pricing limits, fair value is based on discounted cash flows using current market rates applied to the estimated life and credit risk. Fair value of debt is based on current rates for similar financing. It was not practicable to determine the fair value of FHLB stock due to restrictions placed on its transferability. The fair value of off-balance-sheet items is not considered material (or is based on the current fees or cost that would be charged to enter into or terminate such arrangements).

**NOTE 6 SECURITIES**

The following table summarizes the amortized cost and fair value of the available-for-sale securities investment securities portfolio at March 31, 2011 and the corresponding amounts of gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) were as follows:

|  | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|--|----------------|------------------------|-------------------------|------------|
| <b>2011</b>  |                |                        |                         |            |
| Available-for sale                                   |                |                        |                         |            |
| U.S. government-sponsored entities and agencies      | \$ 16,752      | \$ 6                   | \$ (36)                 | \$ 16,722  |
| Private label residential mortgage-backed securities | 50,069         | 2,189                  | (161)                   | 52,097     |
| Federal National Mortgage Association                | 3              |                        |                         | 3          |
| Government National Mortgage Association             | 4,780          | 87                     |                         | 4,867      |
| Total securities available for sale                  | \$ 71,604      | \$ 2,282               | \$ (197)                | \$ 73,689  |

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|  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|--|-------------------|------------------------------|-------------------------------|---------------|
| <b>2010</b>  |                   |                              |                               |               |
| Available-for sale                                   |                   |                              |                               |               |
| U.S. government-sponsored entities and agencies      | \$ 5,036          | \$ 19                        | \$                            | \$ 5,055      |
| Private label residential mortgage-backed securities | 49,933            | 4,545                        | (232)                         | 54,246        |
| Federal National Mortgage Association                | 3                 |                              |                               | 3             |
| Government National Mortgage Association             | 5,402             | 84                           |                               | 5,486         |
| Total securities available for sale                  | \$ 60,374         | \$ 4,648                     | \$ (232)                      | \$ 64,790     |

The amortized cost and fair value of the investment securities portfolio are shown by expected maturity. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

|   | March 31, 2011    |               |
|---|-------------------|---------------|
|   | Amortized<br>Cost | Fair<br>Value |
| <b>Maturity</b>   |                   |               |
| Available-for-sale  |                   |               |
| Within one year   |                   | \$ 5,010      |
| One to five years   |                   | 11,745        |
| Five to ten years   |                   |               |
| Private label residential mortgage backed and agency securities |                   | 54,849        |
| Total   |                   | \$ 71,604     |
|   |                   | \$ 73,689     |

At quarter-ending March 31, 2011 and March 31, 2010, there were no holdings of securities of any one issuer, other than the U.S. Government and its agencies, in an amount greater than 10% of shareholders' equity.

The following table summarizes the investment securities with unrealized losses at March 31, 2011 by aggregated major security type and length of time in a continuous unrealized loss position:

|  | Less Than 12 Months |                      | 12 Months or Longer |                      | Total         |                      |
|--|---------------------|----------------------|---------------------|----------------------|---------------|----------------------|
|  | Fair<br>Value       | Unrealized<br>Losses | Fair<br>Value       | Unrealized<br>Losses | Fair<br>Value | Unrealized<br>Losses |
| <b>Available-for-sale</b>                            |                     |                      |                     |                      |               |                      |
| U.S. government-sponsored entities and agencies      | \$ 11,706           | \$ (36)              | \$                  | \$                   | \$ 11,706     | \$ (36)              |
| Private label residential mortgage-backed securities | 8,035               | (106)                | 40,515              | (55)                 | 12,086        | (161)                |
| Total available-for-sale                             | \$ 19,741           | \$ (142)             | \$ 40,515           | \$ (55)              | \$ 23,792     | \$ (197)             |

The following table summarizes the investment securities with unrealized losses at December 31, 2010 by aggregated major security type and length of time in a continuous unrealized loss position:

|  | Less Than 12 Months |                      | 12 Months or Longer |                      | Total         |                      |
|--|---------------------|----------------------|---------------------|----------------------|---------------|----------------------|
|  | Fair<br>Value       | Unrealized<br>Losses | Fair<br>Value       | Unrealized<br>Losses | Fair<br>Value | Unrealized<br>Losses |
| <b>Available-for-sale</b>                            |                     |                      |                     |                      |               |                      |
| Private label residential mortgage-backed securities | \$ 11,547           | \$ (232)             | \$                  | \$                   | \$ 11,547     | \$ (232)             |

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|                          |           |          |    |    |           |          |
|--------------------------|-----------|----------|----|----|-----------|----------|
| Total available-for-sale | \$ 11,547 | \$ (232) | \$ | \$ | \$ 11,547 | \$ (232) |
|--------------------------|-----------|----------|----|----|-----------|----------|

*Other-Than-Temporary-Impairment.* Management evaluates securities for other-than-temporary impairment ( OTTI ) on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. The investment securities portfolio is evaluated for OTTI by segregating the portfolio into two general segments and applying the appropriate OTTI model. Investment securities classified as available for sale or held-to-maturity are generally evaluated for OTTI under Statement of Financial Accounting Standards ASC 320, *Accounting for Certain Investments in Debt and Equity Securities*. However, certain purchased beneficial interests, including non-agency mortgage-backed securities, asset-backed securities, and collateralized debt obligations, that had credit ratings at the time of purchase of below AA are evaluated using the model outlined in ASC 325, *Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continue to be Held by a Transfer in Securitized Financial Assets*.

In determining OTTI under the ASC 320 model, management considers many factors, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the

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market decline was affected by macroeconomic conditions, and (4) whether the entity has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to management at a point in time.

The second segment of the portfolio uses the OTTI guidance provided by ASC 325 that is specific to purchased beneficial interests that, on the purchase date, were rated below AA. Under the ASC 325 model, the Company compares the present value of the remaining cash flows as estimated at the preceding evaluation date to the current expected remaining cash flows. An OTTI is deemed to have occurred if there has been an adverse change in the remaining expected future cash flows.

When OTTI occurs under either model, the amount of the OTTI recognized in earnings depends on whether an entity intends to sell the security or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss. If an entity intends to sell or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss, the OTTI shall be recognized in earnings equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. If an entity does not intend to sell the security and it is not more likely than not that the entity will be required to sell the security before recovery of its amortized cost basis less any current-period loss, the OTTI shall be separated into the amount representing the credit loss and the amount related to all other factors. The amount of the total OTTI related to the credit loss is determined based on the present value of cash flows expected to be collected and is recognized in earnings. The amount of the total OTTI related to other factors is recognized in other comprehensive income, net of applicable taxes. The previous amortized cost basis less the OTTI recognized in earnings becomes the new amortized cost basis of the investment.

As of March 31, 2011, the Company's security portfolio consisted of twenty-seven securities, six of which were in an unrealized loss position. The unrealized losses are related to the Company's private label residential mortgage-backed securities and the US government sponsored entities and agencies securities as discussed below.

The Company's private label residential mortgage-backed securities that are in a loss position had a market value of \$12.1 million with unrealized losses of approximately \$161 thousand at March 31, 2011. These non-agency private label residential mortgage-backed securities were rated AAA at purchase and are not within the scope of ASC 325. The Company monitors to insure it has adequate credit support and as of March 31, 2011, the Company believes there is no OTTI and does not have the intent to sell these securities and it is likely that it will not be required to sell the securities before their anticipated recovery. Of the \$73.7 million securities portfolio, \$55.8 million were rated AAA or AA and \$17.9 million were rated between B- to BBB based on the most recent credit rating as of March 31, 2011.

During the quarter ended March 31, 2011 and 2010, the Company determined that no securities were other-than-temporarily impaired due to current market conditions.

**NOTE 7 LOANS**

Loans receivable consist of the following:

|   | <b>2011</b> | <b>2010</b> |
|---|-------------|-------------|
| One-to four-family- fully amortizing                | \$ 189,174  | \$ 177,360  |
| One-to four-family- negatively amortizing           | 29,389      | 29,733      |
| One-to four-family- interest only                   | 122,858     | 147,914     |
| Multi-family  | 17,112      | 17,207      |
| Condominium conversions                             | 11,675      | 12,038      |
| Commercial real estate- secured                     | 34,080      | 32,820      |
| Commercial real estate- unsecured                   | 6,215       | 6,215       |
| Land  | 8,985       | 10,660      |
| Real estate secured-first trust deeds (Green acct)  | 221,168     | 214,509     |
| Real estate secured-second trust deeds (Green acct) | 9,037       | 9,260       |
| Commercial real estate secured (Green acct)         | 14,263      | 13,749      |
| Multi-family (Green acct)                           | 3,808       | 3,795       |
| Land (Green acct)                                   | 1,460       | 4,168       |
| HELOCs  | 8,994       | 9,383       |
| Other consumer                                      | 1,548       | 1,583       |

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|                            |            |            |
|----------------------------|------------|------------|
| Auto                       | 50         | 65         |
| Commercial non-real estate | 904        | 529        |
| Total                      | 680,720    | 690,988    |
| Allowance for loan losses  | (11,905)   | (14,637)   |
| Net deferred loan costs    | 1,764      | 1,824      |
| Loans receivable, net      | \$ 670,579 | \$ 678,175 |

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At March 31, 2011, the Company has a total of \$402.9 million in interest only mortgage loans (including Green Account loans) and \$31.6 million in loans with potential for negative amortization. At December 31, 2010, the Company has a total of \$423.4 million in interest only mortgage loans (including Green Account loans) and \$29.7 million in loans with potential for negative amortization. These loans pose a potentially higher credit risk because of the lack of principal amortization and potential for negative amortization. However, management believes the risk is mitigated through the Company's loan terms and underwriting standards, including its policies on loan-to-value ratios.

Activity in the allowance for loan losses is summarized as follows:

|  | <b>2011</b>      | <b>2010</b>      | <b>2009</b>      |
|--|------------------|------------------|------------------|
| Balance at beginning of year               | \$ 14,637        | \$ 13,079        | \$ 18,286        |
| Loans charged off                          | (2,735)          | (7,531)          | (22,505)         |
| Recoveries of loans previously charged off | 3                | 132              | 2                |
| Provision for loan losses                  |                  | 8,957            | 17,296           |
| <b>Balance at end of year</b>              | <b>\$ 11,905</b> | <b>\$ 14,637</b> | <b>\$ 13,079</b> |

Loans charged off in 2011 primarily included specific valuation charge offs for various one to-four- family properties and one land loan totaling \$2.7 million.

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The following table presents the activity in the allowance for loan losses and the recorded investment in loans by portfolio segment and is based on impairment method as of March 31, 2011:

|   | One-to<br>four-<br>Family<br>Fully<br>Amortizing | Negatively<br>Amortizing<br>One-to<br>four-<br>Family | Interest<br>Only<br>One-to<br>four-<br>Family | Multi-<br>Family | Condominium<br>Conversions | Commercial | Unsecured<br>Commercial | Land     |
|---|--|---|---|------------------|----------------------------|------------|-------------------------|----------|
| Allowance for loan losses:                  |  |   |   |                  |                            |            |                         |          |
| Balance as of December 31, 2010             | \$ 2,445   | \$ 923  | \$ 4,164                                      | \$ 1,854         | \$ 528                     | \$ 236     | \$ 47                   | \$ 208   |
| Charge-offs                                 |  |   | 1,053   |                  |                            |            |                         | 1,674    |
| Recoveries                                  |  |   |   |                  |                            |            |                         |          |
| Provision                                   | 312  | (11)  | (421)   |                  | (33)                       | 9          |                         | 1,690    |
| Balance as of March 31, 2011                | \$ 2,757   | \$ 912  | \$ 2,690                                      | \$ 1,854         | \$ 495                     | \$ 245     | \$ 47                   | \$ 224   |
| Individually evaluated for impairment       | 560  | 70  | 842   | 1,811            | 272                        |            |                         | 169      |
| Collectively evaluated for impairment       | 2,197  | 842   | 1,848   | 43               | 223                        | 245        | 47                      | 55       |
| Total ending allowance balance              | \$ 2,757   | \$ 912  | \$ 2,690                                      | \$ 1,854         | \$ 495                     | \$ 245     | \$ 47                   | \$ 224   |
| Loans:                                      |  |   |   |                  |                            |            |                         |          |
| Loans individually evaluated for impairment | \$ 5,068   | \$ 2,279  | \$ 14,592                                     | \$               | \$ 10,458                  | \$ 1,385   | \$                      | \$ 4,373 |
| Loans collectively evaluated for impairment | 184,106  | 27,110  | 108,267                                       | 17,112           | 1,217                      | 32,694     | 6,215                   | 4,612    |
| Total ending loans balance                  | \$ 189,174                                       | \$ 29,389   | \$ 122,859                                    | \$ 17,112        | \$ 11,675                  | \$ 34,079  | \$ 6,215                | \$ 8,985 |

|  | HELOCS | Green-<br>1 <sup>st</sup> Trust<br>Deeds | Green-<br>2 <sup>nd</sup><br>Trust<br>Deeds | Green-<br>Multi-1st<br>TD s | Green-<br>Land | Green-<br>Comm-1st<br>TDs | Auto | Other<br>Consumer | Commercial-<br>non real<br>estate | TOTAL     |
|--|--------|--|---|-----------------------------|----------------|---------------------------|------|-------------------|-----------------------------------|-----------|
| Allowance for loan losses:                     |        |  |   |                             |                |                           |      |                   |                                   |           |
| Balance as of December 31, 2010                | \$ 274 | \$ 2,043                                 | \$ 258                                      | \$ 9                        | \$ 859         | \$ 96                     | \$ 3 | \$ 73             | \$ 4                              | \$ 14,024 |
| Charge-offs                                    |        |  |   |                             |                |                           |      | 8                 |                                   | 2,735     |
| Recoveries                                     | 3      |  |   |                             |                |                           |      |                   |                                   | 3         |
| Provision                                      | (119)  | (505)                                    | (70)  | 1                           | (823)          | 4                         | (1)  | 8                 | 2                                 | 43        |
| Balance as of March 31, 2011                   | \$ 158 | \$ 1,538                                 | \$ 188                                      | \$ 10                       | \$ 36          | \$ 100                    | \$ 2 | \$ 73             | \$ 6                              | \$ 11,335 |
| Allowance for loans losses:                    |        |  |   |                             |                |                           |      |                   |                                   |           |
| Ending allowance balance attributable to loans | \$     | \$                                       | \$  | \$                          | \$             | \$                        | \$   | \$                | \$                                | \$        |
| Individually evaluated for impairment          |        | 132                                      |   |                             |                |                           |      |                   |                                   | 3,856     |

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|   |          |            |          |          |          |           |       |          |        |            |
|---|----------|------------|----------|----------|----------|-----------|-------|----------|--------|------------|
| Collectively evaluated for impairment       | 158      | 1,406      | 188      | 10       | 36       | 100       | 2     | 73       | 6      | 7,479      |
| Acquired with deteriorated credit quality   |          |            |          |          |          |           |       |          |        |            |
| Total ending loans balance                  | \$ 158   | \$ 1,538   | \$ 188   | \$ 10    | \$ 36    | \$ 100    | \$ 2  | \$ 73    | \$ 6   | \$ 11,335  |
| Loans:                                      |          |            |          |          |          |           |       |          |        |            |
| Loans individually evaluated for impairment | \$ 1,101 | \$ 9,222   | \$       | \$       | \$       | \$ 901    | \$    | \$ 2     | \$ 38  | \$ 49,419  |
| Loans collectively evaluated for impairment | 7,893    | 211,946    | 9,038    | 3,808    | 1,460    | 13,361    | 50    | 1,546    | 866    | 631,301    |
| Total ending loans balance                  | \$ 8,994 | \$ 221,168 | \$ 9,038 | \$ 3,808 | \$ 1,460 | \$ 14,262 | \$ 50 | \$ 1,548 | \$ 904 | \$ 680,720 |

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The following table presents the activity in the allowance for loan losses and the recorded investment in loans by portfolio segment and is based on impairment method as of December 31, 2010:

|  | One-to<br>four-<br>Family<br>Fully<br>Amortizing | Negatively<br>Amortizing<br>One-to<br>four-<br>Family | Interest<br>Only<br>One-to<br>four-<br>Family | Multi-<br>Family | Condominium<br>Conversions | Commercial       | Unsecured<br>Commercial | Land             |
|--|--|---|---|------------------|----------------------------|------------------|-------------------------|------------------|
| <b>Allowance for loans losses:</b>             |  |   |   |                  |                            |                  |                         |                  |
| Ending allowance balance attributable to loans | \$   | \$  | \$  | \$               | \$                         | \$               | \$                      | \$               |
| Individually evaluated for impairment          | 114  | 69  | 1,677   | 1,811            | 272                        |                  |                         |                  |
| Collectively evaluated for impairment          | 2,331  | 854   | 2,487   | 43               | 256                        | 236              | 47                      | 208              |
| <b>Total ending allowance balance</b>          | <b>\$ 2,445</b>                                  | <b>\$ 923</b>   | <b>\$ 4,164</b>                               | <b>\$ 1,854</b>  | <b>\$ 528</b>              | <b>\$ 236</b>    | <b>\$ 47</b>            | <b>\$ 208</b>    |
| <b>Loans:</b>                                  |  |   |   |                  |                            |                  |                         |                  |
| Loans individually evaluated for impairment    | \$ 3,214   | \$ 2,418  | \$ 14,191                                     | \$               | \$ 10,466                  | \$ 1,394         | \$                      | \$ 9,715         |
| Loans collectively evaluated for impairment    | 174,147  | 27,315  | 133,722                                       | 17,207           | 1,572                      | 31,426           | 6,215                   | 945              |
| <b>Total ending loans balance</b>              | <b>\$ 177,361</b>                                | <b>\$ 29,733</b>                                      | <b>\$ 147,913</b>                             | <b>\$ 17,207</b> | <b>\$ 12,038</b>           | <b>\$ 32,820</b> | <b>\$ 6,215</b>         | <b>\$ 10,660</b> |

|  | HELOCS          | Green-<br>1 <sup>st</sup> Trust<br>Deeds | Green-<br>2 <sup>nd</sup><br>Trust<br>Deeds | Green-<br>Multi-1 <sup>st</sup><br>TD s | Green-<br>Land  | Green-<br>Comm-1 <sup>st</sup><br>TDs | Auto         | Other<br>Consumer | Commercial-<br>non real<br>estate | TOTAL             |
|--|-----------------|--|---|---|-----------------|---------------------------------------|--------------|-------------------|-----------------------------------|-------------------|
| <b>Allowance for loans losses:</b>             |                 |  |   |   |                 |                                       |              |                   |                                   |                   |
| Ending allowance balance attributable to loans | \$              | \$                                       | \$  | \$                                      | \$              | \$                                    | \$           | \$                | \$                                | \$                |
| Individually evaluated for impairment          | 44              | 375                                      |   |   |                 |                                       |              |                   |                                   | 4,362             |
| Collectively evaluated for impairment          | 230             | 1,668                                    | 258   | 9                                       | 859             | 96                                    | 3            | 73                | 4                                 | 9,662             |
| Acquired with deteriorated credit quality      |                 |  |   |   |                 |                                       |              |                   |                                   |                   |
| <b>Total ending allowance balance</b>          | <b>\$ 274</b>   | <b>\$ 2,043</b>                          | <b>\$ 258</b>                               | <b>\$ 9</b>                             | <b>\$ 859</b>   | <b>\$ 96</b>                          | <b>\$ 3</b>  | <b>\$ 73</b>      | <b>\$ 4</b>                       | <b>\$ 14,024</b>  |
| <b>Loans:</b>                                  |                 |  |   |   |                 |                                       |              |                   |                                   |                   |
| Loans individually evaluated for impairment    | \$ 108          | \$ 7,473                                 | \$  | \$                                      | \$              | \$ 916                                | \$           | \$ 5              | \$ 14                             | \$ 49,915         |
| Loans collectively evaluated for impairment    | 9,275           | 207,036                                  | 9,260                                       | 3,795                                   | 4,168           | 12,833                                | 65           | 1,578             | 515                               | 641,073           |
| <b>Total ending loans balance</b>              | <b>\$ 9,383</b> | <b>\$ 214,509</b>                        | <b>\$ 9,260</b>                             | <b>\$ 3,795</b>                         | <b>\$ 4,168</b> | <b>\$ 13,749</b>                      | <b>\$ 65</b> | <b>\$ 1,583</b>   | <b>\$ 529</b>                     | <b>\$ 690,988</b> |

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Individually impaired loans were as follows:

|  | March 2011    | December 2010 |
|--|---------------|---------------|
| Year-end loans with no allocated allowance for loan losses | \$ 31,598     | \$ 25,979     |
| Year-end loans with allocated allowance for loan losses    | 22,226        | 23,936        |
| <b>Total</b>   | <b>53,824</b> | <b>49,915</b> |
| Amount of the allowance for loan losses allocated          | \$ 3,857      | \$ 4,363      |

|  | 2011      | 2010      | 2009      |
|--|-----------|-----------|-----------|
| Average of individually impaired loans during the period | \$ 24,019 | \$ 33,662 | \$ 47,214 |
| Interest income recognized during impairment             | 112       | 1,785     | 820       |
| Cash-basis interest income recognized                    | 90        | 1,555     | 595       |

The following table presents loans individually evaluated for impairment by class of loans as of March 31, 2011. The recorded investment included represents customer balances net of any partial charge-offs recognized on the loans, net of any deferred fees and costs and accrued interest.

|   | Unpaid<br>Principal<br>Balance | Recorded<br>Investment | Allowance<br>for Loan<br>Losses<br>Allocated | Average<br>Recorded<br>Investment<br>YTD | Interest<br>Income<br>Recognized<br>YTD |
|---|--------------------------------|------------------------|--|--|---|
| With no related allowance recorded:                 |                                |                        |  |  |   |
| One-to four-family                                  | \$ 11,455                      | \$ 11,992              | \$   | \$ 12,676                                | \$ 41                                   |
| Multi-family  |                                |                        |  |  |   |
| Commercial real estate                              | 1,385                          | 1,385                  |  | 1,389                                    | 12                                      |
| Land  | 8,041                          | 10,306                 |  | 8,130                                    |   |
| Construction loans                                  |                                |                        |  |  |   |
| Real estate secured-first trust deeds (Green acct)  | 8,675                          | 8,693                  |  | 8,662                                    | 29                                      |
| Real estate secured-second trust deeds (Green acct) |                                |                        |  |  |   |
| Commercial real estate (Green acct)                 | 901                            | 905                    |  | 910                                      | 10                                      |
| Multi-family (Green acct)                           |                                |                        |  |  |   |
| Land (Green acct)                                   |                                |                        |  |  |   |
| Consumer  | 1,103                          | 1,120                  |  | 1,109                                    | 1                                       |
| Commercial business                                 | 38                             | 38                     |  | 47                                       |   |
| With an allowance recorded:                         |                                |                        |  |  |   |
| One-to four-family                                  | 10,483                         | 9,258                  | 1,472  | 10,509                                   |   |
| Multi-family  | 10,458                         | 8,523                  | 2,084  | 10,552                                   | 19                                      |
| Commercial real estate                              |                                |                        |  |  |   |
| Land  | 738                            | 580                    | 169  | 741                                      |   |
| Construction loans                                  |                                |                        |  |  |   |
| Real estate secured-first trust deeds (Green acct)  | 547                            | 415                    | 132  | 548                                      |   |
| Real estate secured-second trust deeds (Green acct) |                                |                        |  |  |   |
| Commercial real estate (Green acct)                 |                                |                        |  |  |   |
| Multi-family (Green acct)                           |                                |                        |  |  |   |
| Land (Green acct)                                   |                                |                        |  |  |   |
| Consumer  |                                |                        |  |  |   |
| Commercial business                                 |                                |                        |  |  |   |
| <b>Total</b>  | <b>\$ 53,824</b>               | <b>\$ 53,220</b>       | <b>\$ 3,857</b>                              | <b>\$ 55,273</b>                         | <b>\$ 112</b>                           |

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The following table presents loans individually evaluated for impairment by class of loans as of December 31, 2010:

|   | Unpaid<br>Principal<br>Balance | Recorded<br>Investment | Allowance<br>for Loan<br>Losses<br>Allocated | Average<br>Recorded<br>Investment<br>YTD | Interest<br>Income<br>Recognized<br>YTD |
|---|--------------------------------|------------------------|--|--|---|
| With no related allowance recorded:                 |                                |                        |  |  |   |
| One-to four-family                                  | \$ 7,807                       | \$ 8,196               | \$   | \$ 9,537                                 | \$ 131                                  |
| Multi-family  |                                |                        |  | 32                                       | 3                                       |
| Commercial real estate                              | 1,394                          | 1,398                  |  | 1,520                                    | 27                                      |
| Land  | 9,715                          | 10,625                 |  | 4,952                                    | 171                                     |
| Construction loans                                  |                                |                        |  |  |   |
| Real estate secured-first trust deeds (Green acct)  | 6,127                          | 6,447                  |  | 7,174                                    | 142                                     |
| Real estate secured-second trust deeds (Green acct) |                                |                        |  | 161                                      |   |
| Commercial real estate (Green acct)                 | 916                            | 961                    |  | 681                                      |   |
| Multi-family (Green acct)                           |                                |                        |  |  |   |
| Land (Green acct)                                   |                                |                        |  |  |   |
| Consumer  | 5                              | 5                      |  | 15                                       | 2                                       |
| Commercial business                                 | 15                             | 16                     |  | 25                                       | 1                                       |
| With an allowance recorded:                         |                                |                        |  |  |   |
| One-to four-family                                  | 12,016                         | 10,369                 | 1,860  | 14,337                                   | 196                                     |
| Multi-family  | 10,466                         | 8,421                  | 2,084  | 8,696                                    | 808                                     |
| Commercial real estate                              |                                |                        |  |  |   |
| Land  |                                |                        |  | 7,240                                    | 250                                     |
| Construction loans                                  |                                |                        |  |  |   |
| Real estate secured-first trust deeds (Green acct)  | 1,346                          | 1,046                  | 375  | 2,078                                    | 41                                      |
| Real estate secured-second trust deeds (Green acct) |                                |                        |  | 8  |   |
| Commercial real estate (Green acct)                 |                                |                        |  |  |   |
| Multi-family (Green acct)                           |                                |                        |  |  |   |
| Land (Green acct)                                   |                                |                        |  |  |   |
| Consumer  | 108                            | 74                     | 44   | 100                                      | 14                                      |
| Commercial business                                 |                                |                        |  |  |   |
| <b>Total</b>  | <b>\$ 49,915</b>               | <b>\$ 47,558</b>       | <b>\$ 4,363</b>                              | <b>\$ 56,556</b>                         | <b>\$ 1,786</b>                         |

Nonaccrual loans and loans past due 90 days still on accrual were as follows:

|  | 2011      | 2010      |
|--|-----------|-----------|
| Loans past due over 90 days still on accrual | \$        | \$        |
| Nonaccrual loans                             | \$ 38,357 | \$ 38,830 |

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Nonaccrual loans consist of the following:

|  | March 2011       | December 2010    |
|--|------------------|------------------|
| One-to-four-family                                 | \$ 17,689        | \$ 16,921        |
| Multi-family                                       | 5,450            | 8,501            |
| Land   | 8,779            | 9,715            |
| Real estate secured-first trust deeds (Green acct) | 5,446            | 3,691            |
| Consumer   | 993              | 2                |
| <b>Total</b>                                       | <b>\$ 38,357</b> | <b>\$ 38,830</b> |

Of the \$38.4 million in nonaccrual loans, \$15.5 million represents trouble debt restructured loans that are nonaccrual due to the fact that these loans are currently in the first six months of payment.

**Troubled Debt Restructurings:**

The Company has allocated \$2.4 million and \$3.1 million of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as of March 31, 2011 and December 31, 2010, respectively. The Company did not have any commitments to lend additional amounts to customers with outstanding loans that are classified as troubled debt restructurings at March 31, 2011 or December 31, 2010.

**Credit Quality Indicators:**

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company performs an historical loss analysis that is combined with a comprehensive loan to value analysis to analyze the associated risks in the current loan portfolio. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis includes all loans delinquent over 60 days and non-homogenous loans such as commercial and commercial real estate loans. Classification of problem single family residential loans is performed on a monthly basis while analysis of non-homogenous loans is performed on a quarterly basis. The Company uses the following definitions for risk ratings:

**Special Mention.** Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

**Substandard.** Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

**Doubtful.** Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. Loans not rated are evaluated based on payment history.

|                        | Pass      | Special<br>Mention | Substandard | Doubtful | Not Rated  | TOTAL      |
|------------------------|-----------|--------------------|-------------|----------|------------|------------|
| <b>Real Estate:</b>    |           |                    |             |          |            |            |
| One-to four-family     | \$ 25,563 | \$ 16,936          | \$ 16,668   | \$       | \$ 282,255 | \$ 341,422 |
| Multi-family           | 969       |                    | 10,458      |          | 17,360     | 28,787     |
| Commercial real estate | 6,977     |                    | 1,385       |          | 31,932     | 40,294     |

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|   |                  |                  |                  |           |                   |                   |
|---|------------------|------------------|------------------|-----------|-------------------|-------------------|
| Land  |                  | 334              | 4,039            |           | 4,612             | 8,985             |
| <b>Construction</b>                                 |                  |                  |                  |           |                   |                   |
| Real estate secured-first trust deeds (Green acct)  | 15,030           | 9,082            | 6,290            |           | 190,766           | 221,168           |
| Real estate secured-second trust deeds (Green acct) | 946              | 863              |                  |           | 7,228             | 9,037             |
| Commercial real estate (Green acct)                 |                  | 3,766            | 901              |           | 9,596             | 14,263            |
| Multi-family (Green acct)                           |                  |                  |                  |           | 3,808             | 3,808             |
| Land (Green acct)                                   |                  |                  |                  |           | 1,460             | 1,460             |
| Consumer  | 478              | 117              | 993              |           | 9,004             | 10,592            |
| Commercial business                                 | 9                | 523              |                  |           | 372               | 904               |
| <b>Total</b>  | <b>\$ 49,972</b> | <b>\$ 31,621</b> | <b>\$ 40,734</b> | <b>\$</b> | <b>\$ 558,393</b> | <b>\$ 680,720</b> |

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The following table presents the aging of the principal balances in past due loans as of March 31, 2011 by class of loans:

|  | 30-59 Days<br>Past Due | 60-89 Days<br>Past Due | Greater than<br>90 Days<br>Past Due | Total<br>Past Due | Current    | Total<br>Financing<br>Receivables | Total Carrying<br>Amount ><br>90<br>Days<br>and<br>Accruing | Considered<br>Current That<br>Have been<br>Modified<br>in<br>Previous Year |
|--|------------------------|------------------------|-------------------------------------|-------------------|------------|-----------------------------------|---|--|
| March 31, 2011   |                        |                        |                                     |                   |            |                                   |   |  |
| One-to four-family                                     | \$ 16,912              | \$                     | \$ 12,757                           | \$ 29,669         | \$ 311,752 | \$ 341,421                        | \$  | \$ 2,902   |
| Multi-family   | 1,956                  |                        | 5,412                               | 7,368             | 21,419     | 28,787                            |   | 3,090  |
| Non-Residential  | 659                    |                        |                                     | 659               | 39,636     | 40,295                            |   |  |
| Land   |                        |                        | 8,445                               | 8,445             | 540        | 8,985                             |   |  |
| Construction loans                                     |                        |                        |                                     |                   |            |                                   |   |  |
| Real estate secured-first trust deeds<br>(Green acct)  | 5,441                  | 1,000                  | 2,765                               | 9,206             | 211,962    | 221,168                           |   | 798  |
| Real estate secured-second trust<br>deeds (Green acct) | 698                    |                        |                                     | 698               | 8,339      | 9,037                             |   |  |
| Commercial real estate (Green acct)                    |                        | 485                    |                                     | 485               | 13,778     | 14,263                            |   |  |
| Multi-family (Green acct)                              |                        |                        |                                     |                   | 3,808      | 3,808                             |   |  |
| Land (Green acct)                                      |                        |                        |                                     |                   | 1,460      | 1,460                             |   |  |
| Consumer   | 2                      |                        | 992                                 | 995               | 9,597      | 10,592                            |   | 110  |
| Commercial business                                    |                        |                        |                                     |                   | 904        | 904                               |   |  |
| Total  | \$ 25,668              | \$ 1,485               | \$ 30,371                           | \$ 57,525         | \$ 623,195 | \$ 680,720                        |   | \$ 6,900   |

The following table displays the Company's non-performing and performing substandard loan portfolio. \*The Impaired TDR loan on accrual status has reverted back to the loans original terms and has adequate debt service coverage.

|  | # of Loans | Balance   |
|--|------------|-----------|
| Substandard Loans:                                       |            |           |
| Non-Performing   | 35         | \$ 23,213 |
| Performing:  |            |           |
| TDR on non-accrual (not yet made 6 consecutive payments) | 6          | 3,312     |
| Impaired TDR on accrual                                  | 1          | 3,014*    |
| Rated Sub due to borrower relationship to distress loan  | 13         | 7,614     |
| Total Performing:  | 20         | \$ 13,939 |

The following table presents the aging of the principal balances in past due loans as of December 31, 2010 by class of loans:

|                    | 30-59 Days<br>Past Due | 60-89 Days<br>Past Due | Greater than<br>90 Days<br>Past Due | Total<br>Past Due | Current    | Total<br>Financing<br>Receivables | Total Carrying<br>Amount ><br>90<br>Days<br>and<br>Accruing | Considered<br>Current That<br>Have been<br>Modified<br>in<br>Previous Year |
|--------------------|------------------------|------------------------|-------------------------------------|-------------------|------------|-----------------------------------|---|--|
| December 2010      |                        |                        |                                     |                   |            |                                   |   |  |
| One-to four-family | \$ 10,653              | \$ 7,189               | \$ 13,518                           | \$ 31,360         | \$ 323,647 | \$ 355,007                        | \$  | \$ 2,903   |
| Multi-family       | 540                    |                        |                                     | 540               | 28,705     | 29,245                            |   |  |

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|  |       |       |       |        |         |         |     |
|--|-------|-------|-------|--------|---------|---------|-----|
| Non-Residential  | 665   |       |       | 665    | 38,370  | 39,035  |     |
| Land   | 2,538 |       | 7,582 | 10,120 | 540     | 10,660  |     |
| Construction loans                                     |       |       |       |        |         |         |     |
| Real estate secured-first trust deeds<br>(Green acct)  | 6,472 | 2,756 |       | 9,228  | 205,281 | 214,509 | 799 |
| Real estate secured-second trust deeds<br>(Green acct) | 698   |       |       | 698    | 8,562   | 9,260   |     |
| Commercial real estate (Green acct)                    |       |       |       |        | 13,749  | 13,749  |     |
| Multi-family (Green acct)                              |       |       |       |        | 3,795   | 3,795   |     |
| Land (Green acct)                                      |       |       |       |        | 4,168   | 4,168   |     |
| Consumer   | 4     | 2     | 2     | 8      | 11,023  | 11,031  | 111 |

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|                     | 30-59 Days<br>Past Due | 60-89 Days<br>Past Due | Greater than<br>90 Days<br>Past Due | Total<br>Past Due | Current           | Total<br>Financing<br>Receivables | Total<br>Carrying<br>Amount ><br>90<br>Days<br>and<br>Accruing | Considered<br>Current That<br>Have been<br>Modified<br>in<br>Previous Year |
|---------------------|------------------------|------------------------|-------------------------------------|-------------------|-------------------|-----------------------------------|--|--|
| December 2010       |                        |                        |                                     |                   |                   |                                   |  |  |
| Commercial business |                        |                        |                                     |                   | 529               | 529                               |  | 14   |
| <b>Total</b>        | <b>\$ 21,570</b>       | <b>\$ 9,947</b>        | <b>\$ 21,102</b>                    | <b>\$ 52,619</b>  | <b>\$ 638,369</b> | <b>\$ 690,988</b>                 |  | <b>\$ 3,827</b>  |

**NOTE 8 REAL ESTATE OWNED**

Activity in the valuation allowance was as follows:

|                              | 2011     | 2010     | 2009   |
|------------------------------|----------|----------|--------|
| Beginning of year            | \$ 3,379 | \$ 700   | \$     |
| Additions charged to expense | 421      | 2,679    | 700    |
| Direct write-downs           | (3,795)  |          |        |
| End of year                  | \$ 5     | \$ 3,379 | \$ 700 |

The valuation allowance of \$421 thousand charged to expense during 2011 was expensed based on a pending sale of the underlying construction property.

Expenses related to foreclosed assets included in loan servicing and foreclosure expenses on the consolidated statement of operations are as follows:

|   | 2011     | 2010     | 2009     |
|---|----------|----------|----------|
| Net loss on sales                             | \$ 768   | \$ 332   | \$ 79    |
| Operating expenses, net of rental income      | (611)    | 841      | 877      |
|   | \$ 157   | \$ 1,173 | \$ 956   |
| Real Estate loans sold on contract            | \$ 1,146 | \$ 1,147 | \$ 1,002 |
| Deferred gain on real estate sold on contract | \$ 51    | \$ 52    | \$ 54    |

**NOTE 9 LOAN COMMITMENTS AND OTHER RELATED ACTIVITIES**

Some financial instruments such as loan commitments, credit lines, letters of credit, and overdraft protection are issued to meet customer financing needs. These are agreements to provide credit or to support the credit of others, as long as conditions established in the contract are met, and usually have expiration dates. Commitments may expire without being used. Risk of credit loss exists up to the face amount of these instruments, although material losses are not anticipated. The same credit policies are used to make such commitments as are used for loans, including obtaining collateral at exercise of the commitment.

The contractual amount of financial instruments with off-balance-sheet risk was as follows at year end:

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|  | Contract Amount                 |                                    |                                    |                                       |
|--|---------------------------------|------------------------------------|------------------------------------|---------------------------------------|
|  | March 31, 2011<br>Fixed<br>Rate | March 31, 2011<br>Variable<br>Rate | December 31, 2010<br>Fixed<br>Rate | December 31, 2010<br>Variable<br>Rate |
| Financial instruments whose contract amounts represent credit risk |                                 |                                    |                                    |                                       |
| Commitments to extend credit                                       | \$                              | \$                                 | \$                                 | \$                                    |
| Unused lines of credit   | 4,693                           | 41,731                             | 4,761                              | 44,679                                |
| Standby letters of credit  | 10                              | 10                                 | 10                                 | 10                                    |

Commitments to make loans are generally made for periods of 30 days or less.

Financial instruments that potentially subject the Bank to concentrations of credit risk include interest-bearing deposit accounts in other financial institutions, and loans. At March 31, 2011 and December 31, 2010, the Bank had deposit accounts with balances totaling approximately \$23.6 million and \$53.7 million, respectively, in other financial institutions.

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NOTE 10 PREFERRED STOCK

On December 15, 2010, the Company redeemed all \$19.3 million of Series A preferred stock issued to the U.S. Treasury under the TARP Troubled Asset Relief Program's Capital Purchase Program. During the first quarter, the Company entered into an Agreement with the U.S. Department of the Treasury for the repurchase of 280,795 warrants issued to Treasury in connection with the TARP investment. These warrants, which had a strike price of \$10.31 and were purchased for \$1.0 million.

NOTE 11 INCOME TAXES

The Company accounts for income taxes by recognizing deferred tax assets and liabilities based upon temporary differences between the financial reporting and tax basis of its assets and liabilities. Valuation allowances are established when necessary to reduce deferred tax assets when it is more-likely-than-not that a portion or all of the deferred tax assets will not be realized. Each quarter, the Company reviews its analysis of whether a valuation allowance should be recorded against its deferred tax assets. Accounting literature states that a deferred tax asset should be reduced by a valuation allowance if, based on the weight of all available evidence, it is more likely than not (a likelihood of more than 50%) that some portion or the entire deferred tax asset will not be realized. The determination of whether a deferred tax asset is realizable is based on weighting all available evidence, including both positive and negative evidence. In making such judgments, significant weight is given to evidence that can be objectively verified. Although realization is not assured, the Company believes that the realization of the recognized net deferred tax asset at March 31, 2011 is more likely than not based upon available tax planning strategies and expectations as to future taxable income. At March 31, 2011, the Company had a net deferred tax asset of \$7.9 million.

**Table of Contents****ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion compares the financial condition of First PacTrust Bancorp, Inc. (the Company or Bancorp) and Pacific Trust Bank (the Bank), at March 31, 2011, to its financial condition at December 31, 2010, and the results of operations for the three months ended March 31, 2011 to the same periods in 2010. This discussion should be read in conjunction with the interim financial statements and footnotes included herein.

The Company is a community-oriented financial institution deriving substantially all of its revenue from providing banking services to individuals within its market area, primarily San Diego County and portions of Riverside County, CA. In addition, the Company opened a loan production office in Los Angeles, California during the first quarter of 2011. The Company's assets consist primarily of loans and investment securities, which are funded by deposits, borrowings and capital. The primary source of revenue is net interest income, the difference between interest income on loans and investments, and interest expense on deposits and borrowed funds. The Company's basic strategy is to maintain and grow net interest income by the retention of its existing customer base and the expansion of its core businesses and branch offices within its current market and expects to expand further into southern California in the coming quarters. The Company's primary market risk exposure is interest rate risk and credit risk.

**Comparison of Financial Condition at March 31, 2011 and December 31, 2010**

**Assets.** The Company's total assets decreased by \$26.6 million, or 3.1%, to \$835.0 million at March 31, 2011 from \$861.6 million at December 31, 2010 primarily as a result of a planned decline of \$26.3 million of balances in certificates of deposit accounts and a \$7.6 million reduction in balances of loans receivable. The decrease in total assets was partially reduced by an increase in the balance of the available-for-sale securities portfolio in the amount of \$9.0 million and an increase in premises and equipment of \$1.9 million.

**Cash and cash equivalents.** Cash and cash equivalents decreased \$30.4 million, or 51.5%, to \$28.7 million at March 31, 2011 from \$59.1 million at December 31, 2010. The decline was primarily due to a decrease in interest bearing deposits resulting from the repayment of FHLB advances totaling \$15.0 million, a \$26.3 million decline in CD balances offset by \$14.4 of growth in core banking deposits.

**Loans.** Loans receivable, net of valuation allowances, decreased by \$7.6 million, or 1.1%, to \$670.6 million at March 31, 2011 from \$678.2 million at December 31, 2010. This decrease was the result of net loan principal repayments, charge-offs and foreclosures exceeding loan production during the three months ended March 31, 2011. During the first quarter, the Bank sold two non-performing land loans representing \$4.4 million in book value to Bancorp in connection with its effort to further reduce the levels of classified and non-performing assets held at the Bank. These assets had principal balances of \$15.5 million at origination and are expected to be resolved by Bancorp later this year. Also, during the first quarter, the Bank hired a new Chief Loan Officer and Chief Credit Officer and a commercial production team. The Bank also re-launched production for its Green Mortgage and other residential loan products with improved underwriting standards. Production from the re-launch of the Bank's residential lending programs is expected to increase during the second quarter but not hit its long term run rate until the second half of 2011.

**Investments.** Securities classified as available-for-sale of \$73.7 million at March 31, 2011 increased \$9.0 million from December 31, 2010 due to the purchase of \$20.3 million of agency and private label mortgage-backed securities during the period. In addition, the Bank sold \$6.1 million of classified securities in the open market at a gain of \$319 thousand and sold \$11.4 million (book value) in classified securities to Bancorp at a market value of \$13.2 million. The Bank recorded a \$1.8 million gain from this transaction, which was eliminated in the Company's consolidated earnings. While these securities continued to perform well and have no indication of impairment, the assets held credit ratings below investment grade and were sold or transferred to further improve the Bank's asset quality ratios.

**Premises and Equipment.** Premises and equipment increased \$1.9 million, or 30.0%, to \$8.2 million at March 31, 2011 from \$6.3 million at December 31, 2010 primarily due to a newly acquired building in San Marcos, California that will serve as an additional branch for the Company in the second quarter of 2011.

**Allowance for Loan Losses.** The allowance for loan losses at March 31, 2011 was \$11.9 million, which represented 1.8% of the loans outstanding at March 31, 2011, as compared to \$14.6 million, or 2.1%, of the loans outstanding at December 31, 2010. Of these allowances, \$3.9 million are allocated to non-performing loans and loans subject to troubled debt restructurings with \$8.0 million serving as a general reserve for loan losses. The reduction in the allowance largely resulted from the Bank recording a charge-off of \$1.7 million on a delinquent land loan that the Company expects to migrate to OREO, as well as \$222 thousand in charge-offs on 4 loans delinquent more than 90 days.

The Company maintains an allowance for loan losses to absorb probable incurred losses presently inherent in the loan portfolio. The allowance is based on ongoing assessments of the estimated probable losses presently inherent in the loan portfolio. In evaluating the level of the

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allowance for loan losses, management considers the types of loans and the amount of loans in the loan portfolio, peer group information, historical loss experience, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. The Company currently uses a rolling 12 month history of actual losses incurred, adjusted for current economic conditions and other qualitative factors, combined with a current loan to value analysis to analyze the associated risks in the current loan portfolio. The Company obtains updated loan to value amounts to use in this analysis on a semi-annual basis. The most recent analysis was done in November, 2010. The Company evaluates all impaired loans individually, primarily through the evaluation of collateral values and cash flows.

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Management assesses the allowance for loan losses monthly. While management uses available information to recognize losses on loans; future loan loss provisions may be necessary based on changes in economic conditions. In addition, regulatory agencies, as an integral part of their examination process, review the allowance for loan losses and may require the Bank to recognize additional provisions based on their judgment of information available to them at the time of their examination. The allowance for loan losses as of March 31, 2011 was maintained at a level that represented management's best estimate of incurred losses in the loan portfolio to the extent they were both probable and reasonably estimable. See further discussion in subsection entitled "Comparison of Operating Results-Provision for Loan Losses."

**Non-performing Loans.** The following table is a summary of our nonperforming assets, net of specific valuation allowances, at March 31, 2011 and December 31, 2010 (dollars in thousands):

|  | At December 31,<br>2010 | Increased(2)     | Decreases(3)      | At March 31,<br>2011 |
|--|-------------------------|------------------|-------------------|----------------------|
| Nonperforming loans(1)                 |                         |                  |                   |                      |
| One-to four-family                     | \$ 12,330               | \$ 3,553         | \$ (3,975)        | \$ 11,908            |
| Commercial and multi-family            |                         | 3,677            |                   | 3,677                |
| Home-Equity                            |                         | 992              |                   | 992                  |
| Green first trust deeds                |                         | 2,765            |                   | 2,765                |
| Real estate secured-first trust deeds  |                         |                  |                   |                      |
| Real estate secured-second trust deeds |                         |                  |                   |                      |
| Commercial                             |                         |                  |                   |                      |
| Land                                   | 7,581                   | 2,369            | (1,674)           | 8,276                |
| Consumer                               | 2                       |                  | (2)               |                      |
| <b>Total nonperforming loans</b>       | <b>\$ 19,913</b>        | <b>\$ 13,356</b> | <b>\$ (5,651)</b> | <b>\$ 27,618</b>     |
| Other real estate owned                | \$ 6,562                | \$ 3,232         | \$ (3,361)        | \$ 6,433             |
| <b>Total nonperforming assets</b>      | <b>\$ 26,475</b>        | <b>\$ 16,588</b> | <b>\$ (9,012)</b> | <b>\$ 34,051</b>     |

**Ratios**

|  |       |       |
|--|-------|-------|
| Nonperforming loans, net of specific valuation allowances, to total gross loans  | 2.88% | 4.06% |
| Nonperforming assets, net of specific valuation allowances, to total gross loans | 3.80% | 5.00% |

- (1) The Company ceases accruing interest, and therefore classifies as nonperforming, any loan as to which principal or interest has been in default for a period of greater than 90 days, or if repayment in full of interest or principal is not expected. Nonperforming loans exclude loans that have been restructured and remain on accruing status. At March 31, 2011, gross nonperforming loans totaled \$30.4 million. At December 31, 2010, gross nonperforming loans totaled \$21.1 million.
- (2) Increases in nonperforming loans are attributable to loans where we have discontinued the accrual of interest at some point during the quarter ended March 31, 2011. Increases in other real estate owned represent the value of properties that have been foreclosed upon during the quarter ended March 31, 2011.
- (3) Decreases in nonperforming loans are primarily attributable to payments we have collected from borrowers, charge-offs of recorded balances and transfers of balances to other real estate owned during 2011. Decreases in other real estate owned represent either the sale, disposition or valuation adjustment on properties which had previously been foreclosed upon.

Nonperforming loans increased \$7.7 million to \$27.6 million at March 31, 2011 compared to \$19.9 million at December 31, 2010. Loan loss reserves totaling \$3.6 million have been established for these loans. The Company utilizes estimated current market values for collateral when assessing loan loss allocations for impaired collateral dependent loans.

**Troubled Debt Restructured Loans (TDRs).** As of March 31, 2011 the Company had 31 loans with an aggregate balance of \$22.3 million classified as TDR compared to \$23.1 million at December 31, 2010. Specific valuation allowances totaling \$2.4 million have been established for these loans as of March 31, 2011 compared to \$3.1 million at December 31, 2010. When a loan becomes a TDR the Company ceases accruing interest, recognizes principal and interest payments on a cash basis and classifies it as non-accrual until the borrower has made at least six consecutive payments and in certain instances twelve consecutive payments under the modified terms. Of the 31 loans classified as TDR, 25

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loans totaling \$14.3 million are performing under their modified terms (defined as less than 90 days delinquent). Performing TDR include \$10.8 million in loans secured by single family residences, \$3.0 million reported as multi-family loans but secured by condo conversion projects, \$333 thousand million in loans secured by land, one home equity line of credit with a balance of \$108 thousand, an unsecured commercial line of credit with a balance of \$38 thousand and an unsecured consumer loan with a balance of \$2 thousand. Of the performing TDRs, \$6.8 million have been paying as agreed for more than six months and are on accrual status while \$7.5 million are performing and earning interest on a cash basis but are classified non-accrual because the borrower has yet to make six consecutive payments under the modified agreement. Six TDR loans with an aggregate balance of \$8.0 million are nonperforming (defined as over 90 days delinquent). Nonperforming TDR loans consist of one Green loan with an aggregate balance of \$1.0 million secured by a one- to four-family property, two loans totaling \$1.9 million secured by land, one loan with an aggregate balance of \$3.7 million secured by multi-family residences, and two loans totaling \$1.4 million secured by single family residences. These loans will either return to a performing TDR status or

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move through the Bank's normal collection process for non-performing loans. The Company restructured two loans during the quarter ended March 31, 2011 by providing interest rate concessions. Two TDR loans totaling \$6.4 million became delinquent greater than 90 days during the first quarter. Of these, one loan was secured by a single-family property totaling \$1.0 million and one loan totaling \$5.4 million was secured by a multi-family property.

The following table presents the seasoning of the Bank's performing restructured loans, their effective balance (principal balance minus specific valuation allowances charged-off), and their weighted average interest rates (dollars in thousands):

**Performing Restructured Loans As of March 31, 2011**

| Payments     | # of loans | Book Value       | Average Loan Size<br>(Dollars in Thousands) | Weighted<br>Average<br>Interest Rate |
|--------------|------------|------------------|---|--------------------------------------|
| 1 Payment    | 2          | \$ 1,448         | \$ 724                                      | 3.03%                                |
| 2 Payments   | N/A        |                  |   |                                      |
| 3 Payments   | N/A        |                  |   |                                      |
| 4 Payments   | 3          | 3,104            | 1,035                                       | 3.69%                                |
| 5 Payments   | N/A        |                  |   |                                      |
| 6 Payments   | 1          | 547              | 547   | 5.20%                                |
| 7 Payments   | N/A        |                  |   |                                      |
| 8 Payments   | 3          | 3,370            | 1,123                                       | 5.93%                                |
| 9 Payments   | 1          | 320              | 320   | 5.60%                                |
| 10 Payments  | 1          | 512              | 512   | 5.13%                                |
| 11 Payments  | 4          | 1,477            | 369   | 5.55%                                |
| 12 Payments  | 10         | 4,107            | 411   | 5.28%                                |
| <b>Total</b> | <b>25</b>  | <b>\$ 14,885</b> | <b>\$ 595</b>                               | <b>4.61%</b>                         |

**Other Real Estate Owned Assets - OREO.** During the quarter, the Bank sold a single family home at a net loss of \$761.6 thousand, and recorded a \$420.8 thousand write-down on a construction/land loan OREO to levels equal to net sales proceeds. This asset has now been written down to less than 20% of its original loan amount and is expected to be sold by May 30, 2011.

**Deposits.** Total deposits decreased by \$11.9 million, or 1.8%, to \$634.4 million at March 31, 2011 from \$646.3 million at December 31, 2010. Certificate of deposits decreased \$26.3 million and money market accounts decreased \$1.4 million primarily due to the maturity of institutional, single product and inter-company certificate of deposit accounts. In connection with our focus on the development of core banking relationships, savings account balances increased \$10.4 million and checking accounts increased \$2.5 million. Growth was achieved primarily from the formation of new customer relationships and the attraction of additional funds from existing customers. Total core deposits (total deposits less CDs) increased by 5.3% to \$288.8 million at March 31, 2011, compared to \$274.4 million at December 31, 2010. The Bank completed the opening of a new branch in La Jolla, California in early March and expects to open a second branch in San Marcos, California during the second quarter. The Bank is actively seeking additional production offices in core Southern California banking markets and expects to expand the Bank's branch network into Los Angeles during the third quarter.

**Federal Home Loan Bank - FHLB Advances.** \$15.0 million of long term FHLB advances matured in Q1 resulting in a 20.0% decrease, to \$60.0 million at March 31, 2011, from \$75.0 million at December 31, 2010. An additional \$40.0 million of advances have an average current yield of 3.59% and mature in 2011. These advances are expected to be replaced with low cost deposits consumer deposits, or CDs from the State of California CDs that are currently priced at six basis points over the three month Treasury Bill rate.

**Equity.** Equity decreased \$359 thousand, or 0.3% to \$135.7 million at March 31, 2011 from \$136.0 million at December 31, 2010. The net decrease was primarily due to the payment of common stock dividends of \$1.0 million and the repurchase of warrants of \$1.0 million. The decrease in equity was compensated by an increase of \$693.3 thousand in net operating income, a \$345 thousand increase in unrealized gain in securities available-for-sale, the tax effect of ESOP and options redeemed totaling \$295 thousand, and an increase of ESOP shares earned of \$183 thousand.

**Comparison of Operating Results for the Three Months Ended March 31, 2011 and 2010**

**General.** Net income for the three months ended March 31, 2011 was \$693.3 thousand, a \$182 thousand decrease over the same period of the prior year. Excluding certain non-core charges, Bancorp would have earned \$2.0 million, or \$0.20 per share for the quarter ended March 31, 2011. Non-core charges were principally composed of \$1.2 million in OREO related losses and expenses (\$0.07 per share after-tax), and \$863.5 thousand (\$0.06 per share after-tax) in non-core compensation expenses related to an accrual for Change of Control of benefits related to our 2010 private placement. There remain \$883.2 thousand of potential Change of Control payments should the contractual provisions be triggered in the future. Net of a \$0.105 dividend paid on February 24, 2011, and a \$1.0 million (\$0.10 per share) payment to the Department of Treasury in connection with the retirement of TARP related warrants, tangible book value per share declined from \$13.98 to \$13.94 per share between December 31, 2010 and March 31, 2011.

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**Interest Income.** Interest income decreased by \$1.6 million, or 14.9%, to \$8.9 million for the three months ended March 31, 2011, from \$10.5 million for the three months ended March 31, 2010 as described below.

Interest income on loans decreased \$1.5 million, or 16.4% to \$7.7 million for the three months ended March 31, 2011 from \$9.2 million for the three months ended March 31, 2010. The primary factor for the decrease was a \$64.1 million decrease in the average balances of loans receivable from \$736.6 million for the three months ended March 31, 2010 to \$672.5 million for the three months ended March 31, 2011. This was due to principal repayments, loan charge-offs and foreclosures exceeding loan production. The decrease in interest income on loans receivable was further reduced by a 42 basis point reduction in the average yield on loans receivable to 4.6% due to a general decline in market interest rates from the prior period.

Interest income on securities decreased \$86 thousand to \$1.2 million for the three months ended March 31, 2011 from \$1.3 million for the three months ended March 31, 2010. This decrease was due to the sale of four securities during the period as well as a decline on average rate paid on the securities.

**Average Balances, Net Interest Income, Yields Earned and Rates Paid**

The following table presents for the periods indicated the total dollar amount of interest income from average interest-earning assets and the resultant yields, as well as the interest expense on average interest-bearing liabilities, expressed both in dollars and rates. Also presented is the weighted average yield on interest-earning assets, rates paid on interest-bearing liabilities and the resultant spread for the three months at March 31, 2011 and March 31, 2010. No tax equivalent adjustments were made. All average balances are monthly average balances. Non-accruing loans have been included in the table as loans carrying a zero yield.

|  | Three Months Ended March 31, |          |                    |                 |          |                    |
|--|------------------------------|----------|--------------------|-----------------|----------|--------------------|
|  | 2011                         |          |                    | 2010            |          |                    |
|  | Average Balance              | Interest | Average Yield/Cost | Average Balance | Interest | Average Yield/Cost |
| <b><u>INTEREST-EARNING ASSETS</u></b>      |                              |          |                    |                 |          |                    |
| Loans receivable(1)                        | \$ 672,491                   | 7,666    | 4.56%              | \$ 736,647      | 9,165    | 4.98%              |
| Securities(2)                              | 70,073                       | 1,244    | 7.10%              | 55,175          | 1,329    | 9.63%              |
| Other interest-earning assets(3)           | 46,370                       | 39       | 0.34%              | 39,465          | 24       | 0.24%              |
| Total interest-earning assets              | 788,934                      | 8,949    | 4.52%              | 831,287         | 10,518   | 5.08%              |
| Non-interest earning assets(4)             | 62,320                       |          |                    | 61,397          |          |                    |
| Total assets                               | \$ 851,254                   |          |                    | \$ 892,684      |          |                    |
| <b><u>INTEREST-BEARING LIABILITIES</u></b> |                              |          |                    |                 |          |                    |
| NOW  | \$ 61,304                    | 16       | 0.10%              | \$ 55,159       | 32       | 0.23%              |
| Money market                               | 89,814                       | 66       | 0.29%              | 84,730          | 173      | 0.82%              |
| Savings                                    | 129,042                      | 90       | 0.28%              | 121,968         | 242      | 0.79%              |
| Certificates of deposit                    | 359,228                      | 1,105    | 1.23%              | 407,101         | 1,844    | 1.81%              |
| FHLB advances                              | 68,750                       | 517      | 3.01%              | 120,000         | 887      | 2.96%              |
| Total interest-bearing liabilities         | 708,138                      | 1,794    | 1.00%              | 788,958         | 3,178    | 1.60%              |
| Non-interest-bearing liabilities           | 7,159                        |          |                    | 5,607           |          |                    |
| Total liabilities                          | 715,297                      |          |                    | 794,565         |          |                    |
| Equity                                     | 135,957                      |          |                    | 98,120          |          |                    |
| Total liabilities and equity               | \$ 851,254                   |          |                    | \$ 892,685      |          |                    |

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|  |          |       |          |       |
|--|----------|-------|----------|-------|
| Net interest/spread  | \$ 7,155 | 3.52% | \$ 7,340 | 3.48% |
| Margin(5)  |          | 3.63% |          | 3.53% |
| Ratio of interest-earning assets to interest-bearing liabilities | 111.41%  |       | 105.37%  |       |

- (1) Calculated net of deferred fees and loss reserves.
- (2) Calculated based on amortized cost.
- (3) Includes FHLB stock at cost and term deposits with other financial institutions.
- (4) Includes BOLI investment of \$18.1 million.
- (5) Net interest income divided by interest-earning assets.

**Rate/Volume Analysis**

The following table presents the dollar amount of changes in interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities. For each category of interest-earning assets and interest-bearing liabilities,

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information is provided on changes attributable to (1) changes in volume, which are changes in volume multiplied by the old rate, and (2) changes in rate, which are changes in rate multiplied by the old volume. Changes attributable to both rate and volume which cannot be segregated have been allocated proportionately to the change due to volume and the change due to rate.

|   | Three Months Ended March 31, 2011<br>compared to March 31, 2010 |                         |                       |
|---|---|-------------------------|-----------------------|
|   | Total<br>Change   | Change Due<br>To Volume | Change Due<br>To Rate |
| (In thousands)  |   |                         |                       |
| <b><u>Income from interest earning assets:</u></b>            |   |                         |                       |
| Loans, gross  | \$ (1,499)  | \$ (3,056)              | \$ 1,557              |
| Securities  | (85)  | 1,244                   | (1,329)               |
| Interest-bearing deposits in other financial institutions     | 15  | 19                      | (4)                   |
| <b>Total interest income from interest earning assets</b>     | <b>(1,569)</b>  | <b>(1,793)</b>          | <b>224</b>            |
| <b><u>Expense on interest bearing liabilities:</u></b>        |   |                         |                       |
| Now   | \$ (16)   | \$ 13                   | \$ (29)               |
| Savings   | (152)   | 53                      | (205)                 |
| Money market  | (107)   | 39                      | (146)                 |
| Certificate of Deposit  | (739)   | (793)                   | 54                    |
| FHLB Advances   | (370)   | (1,541)                 | 1,171                 |
| <b>Total interest expense on interest-bearing liabilities</b> | <b>(1,384)</b>  | <b>(2,229)</b>          | <b>845</b>            |
| <b>Net interest income</b>                                    | <b>\$ (185)</b>   | <b>\$ 434</b>           | <b>\$ (619)</b>       |

**Interest Expense.** Interest expense decreased \$1.4 million or 43.6%, to \$1.8 million for the three months ended March 31, 2011 from \$3.2 million for the three months ended March 31, 2010. Interest expense on deposits decreased \$1.0 million, or 44.3%, to \$1.3 million for the three months ended March 31, 2011 from \$2.3 million for the three months ended March 31, 2010. The primary factor for the decrease was a \$29.6 million decrease in the average balance of deposits from \$669.0 million for the three months ended March, 31 2010 to \$639.4 million for the three months ended March 31, 2011 as well as a decline in the Company's overall cost of deposits to 80 basis points for the period ending March 31, 2011. This decline in the Company's cost of funds reflects the overall decrease in short term market interest rates as a result of the continued stress in the credit markets.

Interest expense on FHLB advances decreased \$371 thousand, or 41.8% to \$517 thousand for the three months ended March 31, 2011 from \$888 thousand for the three months ended March 31, 2010. This decrease was primarily due to a reduction in the average balances of advances. The average balance of the Federal Home Loan Bank advances decreased \$51.3 million from \$120.0 million for the three months ended March 31, 2010 to \$68.8 million for the three months ended March 31, 2011 due to the maturity of \$50.0 million of FHLB advances during the period.

**Net Interest Income.** As a result of the combined effect of the factors mentioned above, net interest income before the provision for loan losses decreased \$185 thousand, or 2.5%, to \$7.2 million for the three months ended March 31, 2011 from \$7.3 million for the three months ended March 31, 2010. The Company's net interest margin declined marginally from 3.68% as of December 31, 2010 to 3.63% as of March 31, 2011. Continued improvement in the Bank's liability mix and cost of deposits resulted in 14 basis point (17%) reduction in the cost of deposits from 0.94% at December 13, 2010 to 0.80% at March 31, 2011. These benefits were offset by a 42 basis point reduction in yields on the Bank's loan portfolio due to the repricing of adjustable rate loans and reversal of accrued interest on a number of loans delinquent more than 90 days. The Company also experienced declines in the yield on securities as the Company diluted the high yields on its core portfolio by investing excess liquidity into shorter term securities. Continued reductions in the Bank's cost of funds, the impact of recent lending initiatives and expected reductions in the level of non-performing loans are expected to enhance the Bank's core earnings model in coming quarters.

**Provision for Loan Losses.** The Company maintains an allowance for loan losses to absorb probable incurred losses presently inherent in the loan portfolio. The allowance is based on ongoing assessments of the estimated probable losses presently inherent in the loan portfolio. In evaluating the level of the allowance for loan losses, management considers the types of loans and the amount of loans in the loan portfolio, peer group information, historical loss experience, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. The Company currently uses a rolling 12 month history of actual losses incurred, adjusted for

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numerous factors including those found in the Interagency Guidance on Allowance for Loan and Lease Losses, which include current economic conditions, loan seasoning and underwriting experience, among others. This analysis is combined with a current loan to value analysis to analyze the associated risks in the current loan portfolio. The Company evaluates all impaired loans individually, primarily through the evaluation of collateral values and cash flows. Management uses available information to recognize loan losses, however, future loan loss provisions may be necessary based on changes in the above mentioned factors. In addition, regulatory agencies, as an integral part of their examination process, periodically review the allowance for loan losses and may require the Bank to recognize additional provisions based on their judgment of information available to them at the time of their examination. The allowance for loan losses as of March 31, 2011 was maintained at a level that represented management's best estimate of incurred losses in the loan portfolio to the extent they were both probable and

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reasonably estimable. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available or as future events occur.

Provisions for loan losses are charged to operations at a level required to reflect probable incurred credit losses in the loan portfolio. In this regard, approximately 95% of the Company's loans are to individuals and businesses in southern California, in general, and more specifically, San Diego County. The strong level of available allowances during the quarter combined with further improvement in the Bank's core loan portfolio and reductions in overall portfolio risk allowed the Bank to absorb these charges without increasing reserves during the first quarter. This compared to a \$2.2 million provision for loan losses recorded for the three months ended March 31, 2010. The decline in the provision was related primarily to the charge offs of specific valuation allowances related to loans that were 180 days or more delinquent.

During the first quarter, the Company disposed of \$2.7 million in OREO at a net loss of \$761.0 thousand, while charging off \$420.8 thousand on new or existing OREO. As of March 31, 2011, the Company's OREO balances totaled \$6.4 million (0.77% of total assets), compared to \$6.6 million (0.76% of total assets) as of December 31, 2010. Non-performing loans increased by \$7.7 million and totaled \$27.6 million as of March 31, 2011, compared to \$19.9 million at December 31, 2010. The increase was primarily due to the following loans: a \$3.7 million multi-family loan and related \$1.0 million HELOC, and a \$1.8 million land loan. Since the end of the first quarter, \$1.7 million of these loans have cured and the Company expects up to \$6.5 million of the remaining loan balances will be paid off, cured or restructured during the second quarter. Net charge-offs totaled \$2.7 million for the current quarter which primarily resulted in the charge-offs of specific valuation allowances for various one-to four- family properties and one land loan. These levels compare to \$1.2 million in net charge-offs in the prior year's quarter.

**Noninterest Income.** Noninterest income increased \$400 thousand for the three months ended March 31, 2011 to \$767 thousand compared to \$367 thousand for the same period of the prior year primarily due to a gain on sale of available-for-sale securities totaling \$319 thousand.

**Noninterest Expense.** Noninterest expense increased \$2.5 million, or 60.0%, to \$6.8 million for the three months ended March 31, 2011 compared to \$4.3 million for the same period of the prior year. This net increase was primarily the result of the establishment of an \$863.5 thousand accrual for certain Change of Control benefits resulting from our November 2010 recapitalization effort, a \$889.5 thousand increase in salaries and employee benefits, a \$768 thousand loss on sale of other real estate owned assets, a \$421 thousand increase in valuation allowance for other real estate owned, a \$176 thousand increase in occupancy and equipment expenses, and a \$167 thousand increase in professional expenses.

Salaries and employee benefits represented 49.6% and 38.2% of total noninterest expense for the three months ended March 31, 2011 and March 31, 2010, respectively. Total salaries and employee benefits increased \$1.8 million, or 107.7%, to \$3.4 million for the three months ended March 31, 2011 from \$1.6 million for the same period in 2010, primarily due to a \$863.5 thousand accrual for change of control benefits resulting from restructuring costs as well as the hiring of new officers, production personal and support staff needed to execute the Company's growth strategy. There remain \$883.2 thousand of potential change of Control payments should the contractual provisions be triggered in the future.

Occupancy and equipment expenses increased \$176 thousand, or 36.1% to \$664 thousand for the three months ended March 31, 2011 from \$488 thousand in the same period in 2010 primarily due to increased building and equipment maintenance, primarily related to the newly acquired branch locations during the period. The Company opened an office in La Jolla, California during the first quarter and expects to open a San Marcos, California branch location in the second quarter.

Total professional fees increased \$167 thousand, or 99.4% to \$335 thousand for the three months ended March 31, 2011 from \$168 thousand for the same period in 2010, due to increased consulting and legal fees related to required regulatory changes to the Company's 401(k) plan as well as increased audit and executive search fees due to the recruitment of additional executive officers.

**Income Tax Expense/(Benefit).** An income tax expense of \$413 thousand was recorded for the three months ended March 31, 2011 compared to income tax expense of \$359 thousand for the three months ended March 31, 2010. The effective tax rate for the three months period ending March 31, 2011 was in accordance with the guidelines of ASC 740.

## **Liquidity and Commitments**

The Bank is required to have enough liquid assets in order to maintain sufficient liquidity to ensure a safe and sound operation. Liquidity may increase or decrease depending upon availability of funds and comparative yields on investments in relation to the return on loans. Historically, the Bank has maintained liquid assets above levels believed to be adequate to meet the requirements of normal operations, including potential deposit outflows. Cash flow projections are regularly reviewed and updated to ensure that adequate liquidity is maintained.

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The Bank's liquidity, represented by cash and cash equivalents, is a product of its operating, investing, and financing activities. The Bank's primary sources of funds are deposits, payments and maturities of outstanding loans and investment securities; and other short-term investments and funds provided from operations. While scheduled payments from the amortization of loans and mortgage-backed securities and maturing securities and short-term investments are relatively predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions, and competition. In addition, the Bank invests excess funds in interest-earning assets, which provide liquidity to meet lending requirements. The Bank also generates cash through borrowings. The Bank utilizes Federal Home Loan Bank advances to leverage its capital base, to provide funds for its lending activities, as a source of liquidity, and to enhance its interest rate risk management. The Bank also has the ability to obtain brokered

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certificates of deposit, however, historically it has not issued significant amounts. The Bank had no brokered certificates of deposit at March 31, 2011, and has limited future brokered deposit activity to \$20.0 million.

Liquidity management is both a daily and long-term function of business management. Any excess liquidity would be invested in federal funds or authorized investments such as mortgage-backed or U.S. Agency securities. On a longer-term basis, the Bank maintains a strategy of investing in various lending products. The Bank uses its sources of funds primarily to meet its ongoing commitments, to pay maturing certificates of deposit and savings withdrawals, to fund loan commitments, and to maintain its portfolio of mortgage-backed securities and investment securities. At March 31, 2011, there were \$0 outstanding approved loan origination commitments. At the same date, unused lines of credit were \$46.4 million and outstanding letters of credit totaled \$20 thousand. One government agency security is scheduled to mature in one year or less with a book value of \$5.0 million at March 31, 2011. Certificates of deposit scheduled to mature in one year or less at March 31, 2011, totaled \$251.6 million. Based on the competitive rates offered and on historical experience, management believes that a significant portion of maturing deposits will remain with the Bank. In addition, the Bank had the ability at March 31, 2011 to borrow an additional \$155.3 million from the Federal Home Loan Bank of San Francisco, \$129.2 million at the Federal Reserve Bank as well as \$8.0 million from Pacific Coast Bankers Bank as additional funding sources to meet commitments and for liquidity purposes. The Bank has Federal Home Loan Bank advances of \$50.0 million maturing within the next 12 months, with \$5.0 million maturing in early April 2011. The Bank intends to replace these advances with deposits.

**Capital**

Consistent with its goals to operate a sound and profitable financial organization, Pacific Trust Bank actively seeks to maintain a well capitalized institution in accordance with regulatory standards. Total capital of the Bank was \$99.3 million at March 31, 2011, or 12.22% of total assets on that date. As of March 31, 2011, Pacific Trust Bank exceeded all capital requirements of the Office of Thrift Supervision. Pacific Trust Bank's regulatory capital ratios at March 31, 2011 were as follows: core capital 12.12%; Tier I risk-based capital, 16.02%; and total risk-based capital, 17.27%. The regulatory capital requirements to be considered well capitalized are 5.0%, 6.0% and 10.0%, respectively. However, the Bank has committed to its regulatory agency to maintain core and risk-based capital ratios of 8.0% and 12.0% respectively, while the Bank is facing adverse market conditions.

The following table sets forth the Bank's capital components:

|                                      | March 31,  |            | December    |
|--------------------------------------|------------|------------|-------------|
|                                      | 2011       | 2010       | 31,<br>2010 |
| Capital components                   |            |            |             |
| Tier 1 Capital                       | \$ 98,317  | \$ 84,139  | \$ 95,637   |
| Tier 2 Capital                       | 7,673      | 7,273      | 8,015       |
| Total risk-based capital             | \$ 105,990 | \$ 91,412  | \$ 103,652  |
| Risk-weighted assets                 | \$ 613,827 | \$ 676,704 | \$ 641,205  |
| Average assets (regulatory purposes) | \$ 848,096 | \$ 890,594 | \$ 875,615  |

|                           | March 31, |        | December 31, | Minimum      |
|---------------------------|-----------|--------|--------------|--------------|
|                           | 2011      | 2011   | 2010         | Regulatory   |
|                           |           |        |              | Requirements |
| Capital ratios:           |           |        |              |              |
| Total core capital        | 12.12%    | 9.33%  | 11.14%       | 4.00%        |
| Tier 1 risk-based capital | 16.02%    | 12.43% | 14.92%       | 4.00%        |
| Total risk-based capital  | 17.27%    | 13.51% | 16.17%       | 8.00%        |

**Impact of Inflation**

The unaudited consolidated financial statements presented herein have been prepared in accordance with U. S. generally accepted accounting principles. These principles require the measurement of financial position and operating results in terms of historical dollars, without considering

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changes in the relative purchasing power of money over time due to inflation.

The Company's primary assets and liabilities are monetary in nature. As a result, interest rates have a more significant impact on the Company's performance than the effects of general levels of inflation. Interest rates, however, do not necessarily move in the same direction or with the same magnitude as the price of goods and services, since such prices are affected by inflation. In a period of rapidly rising interest rates, the liquidity and maturities structures of the Company's assets and liabilities are critical to the maintenance of acceptable performance levels.

The principal effect of inflation, as distinct from levels of interest rates, on earnings is in the area of noninterest expense. Such expense items as employee compensation, employee benefits, and occupancy and equipment costs may be subject to increases as a

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result of inflation. An additional effect of inflation is the possible increase in the dollar value of the collateral securing loans that the Company has made. The Company is unable to determine the extent, if any, to which properties securing our loans have appreciated in dollar value due to inflation.

**ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Bank's interest rate sensitivity is monitored by management through the use of a model that estimates the change in net portfolio value (NPV) over a range of interest rate scenarios. NPV is the present value of expected cash flows from assets, liabilities, and off-balance-sheet contracts. An NPV Ratio, in any interest rate scenario, is defined as the NPV in that scenario divided by the market value of assets in the same scenario. The Sensitivity Measure is the decline in the NPV Ratio, in basis points, caused by a 2% increase or decrease in rates, whichever produces a larger decline. The higher an institution's Sensitivity Measure is, the greater its exposure to interest rate risk is considered to be. The Office of Thrift Supervision (OTS) has incorporated an interest rate risk component into its regulatory capital rule. Under the rule, an institution whose Sensitivity Measure exceeds 200 basis points may be required to deduct an interest rate risk component in calculating its total capital for purposes of the risk-based capital requirement. Increases in interest rates would be expected to have a negative impact on the Bank's operating results. As of December 31, 2010, the latest date for which information is available, the Bank's Sensitivity Measure, as measured by the OTS, resulting from a 1% decrease in interest rates was a decrease of 6 basis points and would result in a \$1.1 million decrease in the NPV of the Bank. The Sensitivity Measure is less than the threshold at which the Bank could be required to hold additional risk-based capital under OTS regulations.

The OTS uses certain assumptions in assessing the interest rate risk of savings associations. These assumptions relate to interest rates, loan prepayment rates, deposit decay rates, and the market values of certain assets under differing interest rate scenarios, among others.

As with any method of measuring interest rate risk, certain shortcomings are inherent in the method of analysis used in the forthcoming table. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. Additionally, certain assets, such as adjustable rate mortgage loans, have features which restrict changes in interest rates on a short-term basis and over the life of the asset. Further, if interest rates change, expected rates of prepayments on loans and early withdrawals from certificates could deviate significantly from those assumed in calculating the table.

The following table shows the NPV and projected change in the NPV of the Bank at December 31, 2010, the latest date for which information is available, assuming an instantaneous and sustained change in market rates of interest of minus 100 and plus 100, 200, and 300 basis points. The net portfolio value analysis was unable to produce results for the minus 200 and 300 basis point scenario for the quarter ended December 31, 2010.

**Interest Rate Sensitivity of Net Portfolio Value (NPV)**

| Change in Rates | Net Portfolio Value |            |          | NPV as a % of<br>PV of Assets |        |
|-----------------|---------------------|------------|----------|-------------------------------|--------|
|                 | \$ Amount           | \$ Change  | % Change | NPV Ratio                     | Change |
| + 300 bp        | \$ 116,963          | \$ -10,799 | (8)%     | 13.35%                        | -92bp  |
| + 200 bp        | 123,860             | -3,902     | (3)%     | 13.98%                        | -29bp  |
| + 100 bp        | 126,649             | -1,113     | (1)%     | 14.21%                        | -6bp   |
| 0 bp            | 127,762             |            |          | 14.27%                        |        |
| - 100 bp        | 128,022             | 260        | 0%       | 14.27%                        | 0bp    |

The Bank does not maintain any securities for trading purposes. The Bank does not currently engage in trading activities or use derivative instruments in a material amount to control interest rate risk. In addition, interest rate risk is the most significant market risk affecting the Bank. Other types of market risk, such as foreign currency exchange risk and commodity price risk, do not arise in the normal course of the Bank's business activities and operations.

**ITEM 4. CONTROLS AND PROCEDURES**

Evaluation of Disclosure Controls and Procedures: An evaluation of the Company's disclosure controls and procedures (as defined in Section 13(a)-15(e) of the Securities Exchange Act of 1934 (the "Act")) as of March 31, 2011 was carried out under the supervision and with the

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participation of the Company's Chief Executive Officer, Principal Financial Officer and other members of the Company's senior management as of the end of the period preceding the filing of this quarterly report. The Company's Chief Executive Officer and Principal Financial Officer concluded that the Company's disclosure controls and procedures as currently in effect are effective in ensuring that the information required to be disclosed by the Company in the reports it files or submits under the Act is (i) accumulated and communicated to the Company's management (including the Chief Executive Officer and Principal Financial Officer) in a timely manner, and (ii) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

There have been no changes in internal controls over financial reporting (as defined in Rule 13a-15(f) under the Activities) that occurred during the quarter ended March 31, 2011 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

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The Company does not expect that its disclosure controls and procedures and internal control over financial reporting will prevent all errors and fraud. A control procedure, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control procedure is met. Because of the inherent limitations in all control procedures, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any control procedure also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control procedure, misstatements due to error or fraud may occur and not be detected.

The Company intends to continually review and evaluate the design and effectiveness of its disclosure controls and procedures and to improve controls and procedures over time and to correct any deficiencies that may be discovered in the future. The goal is to ensure that senior management has timely access to all material financial and non-financial information concerning the Company's business. While the Company believes that the present design of its disclosure controls and procedures is effective to achieve this goal, future events affecting the Company's business may cause modifications of disclosure controls and procedures.

## **PART II OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

None

### **ITEM 1A. RISK FACTORS**

There were no changes to the risk factors previously disclosed in the Company's Form 10-K for the year ended December 31, 2010 except as set forth below.

The Dodd-Frank Wall Street Reform and Consumer Protection Act that was enacted on July 21, 2010, provides for, among other things, for new restrictions and an expanded framework of regulatory oversight for financial institutions and their holding companies, including the Company and the Bank. Under the new law, the Bank's primary regulator, the Office of Thrift Supervision, will be eliminated and existing federal thrifts will be subject to regulation and supervision by the Office of Comptroller of the Currency, which currently supervises and regulates all national banks. In addition, beginning in 2011, all financial holding companies, including First PacTrust Bancorp, Inc. will be regulated by the Board of Governors of the Federal Reserve System, including imposing federal capital requirements and may result in additional restrictions on investments and other holding company activities. The law also creates a new consumer financial protection bureau that will have the authority to promulgate rules intended to protect consumers in the financial products and services market. The creation of this independent bureau could result in new regulatory requirements and raise the cost of regulatory compliance. In addition, new regulations mandated by the law could require changes in regulatory capital requirements, loan loss provisioning practices, and compensation practices and require holding companies to serve as a source of strength for their financial institution subsidiaries. Effective July 21, 2011, financial institutions may pay interest on demand deposits, which could increase our interest expense. We cannot determine the full impact of the new law on our business and operations at this time. Any legislative or regulatory changes in the future could adversely affect our operations and financial condition.

In response to the financial crisis of 2008 and early 2009, Congress has taken actions that are intended to strengthen confidence and encourage liquidity in financial institutions, and the Federal Deposit Insurance Corporation has taken actions to increase insurance coverage on deposit accounts. The recently enacted Dodd-Frank Wall Street Reform and Consumer Protection Act provides for the creation of a consumer protection division at the Board of Governors of the Federal Reserve System that will have broad authority to issue regulations governing the services and products we provide consumers. This additional regulation could increase our compliance costs and otherwise adversely impact our operations. That legislation also contains provisions that, over time, could result in higher regulatory capital requirements and loan loss provisions for First PacTrust Bancorp, Inc. and Pacific Trust Bank and may increase interest expense due to the ability in July 2011 to pay interest on all demand deposits. There have also been proposals made by members of Congress and others that would reduce the amount delinquent borrowers are otherwise contractually obligated to pay under their mortgage loans and limit an institution's ability to foreclose on mortgage collateral. Recent regulatory changes impose limits on our ability to change overdraft fees, which may decrease our non-interest income as compared to more recent prior periods. The potential exists for additional federal or state laws and regulations, or changes in policy, affecting lending funding practices and liquidity standards. See [How We Are Regulated](#).

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The Company has a significant deferred tax asset and cannot assure that it will be fully realized. Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between the carrying amounts and the tax basis of assets and liabilities computed using enacted tax rates. If we determine that we will not achieve sufficient future taxable income to realize our net deferred tax asset, we are required under generally accepted accounting principles to establish a full or partial valuation allowance. If we determine that a valuation allowance is necessary, we are required to incur a charge to operations. We regularly assess available positive and negative evidence to determine whether it is more likely than not that our net deferred tax asset will be realized. Realization of a deferred tax asset requires us to apply significant judgment and is inherently speculative because it requires estimates that cannot be made with certainty. At March 31, 2011, we had a net deferred tax asset of \$7.9 million. Although realization is not assured, the Company believes that the realization of the recognized net deferred tax asset at March 31, 2011 is more likely than not based upon available tax planning strategies and expectations as to future taxable income.

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- (c) The following table sets forth information for the three months ended March 31, 2011 with respect to the repurchase of outstanding common stock.

**ISSUER PURCHASES OF EQUITY SECURITIES**

| <b>Period</b>    | <b>Total # of shares<br/>Purchased</b> | <b>Average price paid<br/>per share</b> | <b>Total # of shares<br/>purchased as<br/>part of a publicly<br/>announced program</b> | <b>Maximum # of<br/>shares that may<br/>yet be<br/>purchased</b> |
|------------------|--|---|--|--|
| 01/1/11-01/31/11 | 318                                    | 13.60                                   |  | 0  |
| 02/1/11-02/28/11 |  |   |  | 0  |
| 03/1/11-03/31/11 |  |   |  | 0  |

The Company has terminated the buyback plan, however, future purchases may be made by the Company if they are related to employee stock benefit plans, consistent with past practices.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES.**

None

**ITEM 4. RESERVED.**

None

**ITEM 5. OTHER INFORMATION.**

None

**ITEM 6. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

(a)(1) Financial Statements: See Part II Item 8. Financial Statements and Supplementary Data

(a)(2) Financial Statement Schedule: All financial statement schedules have been omitted as the information is not required under the related instructions or is not applicable.

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(a)(3) Exhibits

| <b>Regulation S-K<br/>Exhibit Number</b> | <b>Document</b>   | <b>Reference to<br/>Prior Filing<br/>or Exhibit Number<br/>Attached Hereto</b> |
|--|---|--|
| 2.0                                      | Plan of acquisition, reorganization, arrangement, liquidation or succession   | None   |
| 3.1                                      | Charter for First PacTrust Bancorp, Inc.  | *  |
| 3.2                                      | Articles supplementary to the Charter of the Registrant containing the terms of the Registrant's Fixed Rate Cumulative Perpetual Preferred Stock, Series A.   | ****   |
| 3.3                                      | Bylaws of First PacTrust Bancorp, Inc.  | *  |
| 4.0                                      | Form of Stock Certificate of First PacTrust Bancorp, Inc.   | *  |
| 4.1                                      | Form of Preferred Stock Certificate of First PacTrust Bancorp, Inc.   | ****   |
| 4.2                                      | Warrant to purchase shares of the Registrant's common stock dated November 21, 2008   | ****   |
| 9.0                                      | Voting Trust Agreement  | None   |
| 10.1                                     | Severance Agreement with Hans Ganz  | ***  |
| 10.2                                     | Severance Agreement with Melanie Yaptangco, formerly Stewart  | ***  |
| 10.3                                     | Severance Agreement with James P. Sheehy  | ***  |
| 10.4                                     | 401(k) Employee Stock Ownership Plan  | *  |
| 10.5                                     | Registrant's Stock Option and Incentive Plan  | **   |
| 10.6                                     | Registrant's Recognition and Retention Plan   | **   |
| 10.7                                     | Named Executive Officers Salary and Bonus Arrangements for 2009 and Director Fee Arrangements for 2009.   | *****  |
| 10.8                                     | Letter Agreement, including Schedule A, and Securities Purchase Agreement, dated November 21, 2008, between First PacTrust Bancorp, Inc. and United States Department of the Treasury, with respect to the issuance and sale of the Series A Preferred Stock and the warrant. | ****   |
| 10.9                                     | Form of Compensation Modification Agreement and Waiver, executed by each of Hans R. Ganz, James P. Sheehy, Melanie M. Yaptangco, Regan J. Lauer, Rachel M. Carrillo, and Lisa R. Goodwin.   | ****   |
| 11.0                                     | Statement regarding computation of ratios   | None   |
| 14.0                                     | Code of Ethics  | ***  |
| 16.0                                     | Letter regarding change in certifying accountant  | None   |
| 18.0                                     | Letter regarding change in accounting principles  | None   |
| 21.0                                     | Subsidiaries of the Registrant  | *  |
| 22.0                                     | Published Report regarding matters submitted to vote of security holders  | None   |
| 23.0                                     | Consent of Crowe Horwath LLP  | None   |
| 24.0                                     | Power of Attorney, included in signature pages  | None   |
| 31.1                                     | Rule 13(a)-14(a) Certification (Chief Executive Officer)  | 31.1   |
| 31.2                                     | Rule 13(a)-14(a) Certification (Chief Financial Officer)  | 31.2   |

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|      |  |      |
|------|--|------|
| 32.1 | Section 1350 of The Sarbanes-Oxley Act Certification (Chief Executive Officer) | 32.1 |
| 32.2 | Section 1350 of The Sarbanes-Oxley Act Certification (Chief Financial Officer) | 32.2 |

\* Filed in First PacTrust's Registration Statement on Form S-1. Filed on March 28, 2002. Such information is hereby incorporated by reference.

\*\* Filed as an appendix to the Registrant's definitive proxy statement filed on March 21, 2003. Such previously filed document is incorporated herein by reference in accordance with Item 601 of Regulation S-K.

\*\*\* Filed as an Exhibit to the Company's annual report on Form 10-K for the year ended December 31, 2005.

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\*\*\*\* Filed as an Exhibit to the Registrant's Current Report on Form 8-K. Filed on November 21, 2008. Such information is hereby incorporated by reference.

\*\*\*\*\* Included in the Registrant's definitive proxy statement filed on March 23, 2009. Such previously filed document is incorporated herein by reference in accordance with Item 601 of Regulation S-K.

(b) Exhibits Included, see list in (a)(3).

(c) Financial Statement Schedules None

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FIRST PACTRUST BANCORP, INC.

Date: April 29, 2011

/s/ Gregory A. Mitchell  
Gregory A. Mitchell  
President and Chief Executive Officer

Date: April 29, 2011

/s/ Regan Lauer  
Regan Lauer  
Senior Vice President/ Controller  
(Principal Financial and Accounting Officer)