

WESTAMERICA BANCORPORATION

Form 10-Q

July 30, 2010

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q**

(Mark One)

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

**For the quarterly period ended June 30, 2010**

**or**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_.**

**Commission file number: 001-9383**

**WESTAMERICA BANCORPORATION**

(Exact Name of Registrant as Specified in Its Charter)

**CALIFORNIA**

(State or Other Jurisdiction of  
Incorporation or Organization)

**94-2156203**

(I.R.S. Employer  
Identification No.)

**1108 FIFTH AVENUE, SAN RAFAEL, CALIFORNIA 94901**

(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code (707) 863-6000

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting  
company

(Do not check if a 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 registrant's classes of common stock, as of the latest practicable date:

Title of Class

Shares outstanding as of July 23, 2010

Common Stock,  
No Par Value

29,142,315

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| <u>EX-101 INSTANCE DOCUMENT</u>                                                                                             |      |
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**FORWARD-LOOKING STATEMENTS**

This report on Form 10-Q contains forward-looking statements about Westamerica Bancorporation for which it claims the protection of the safe harbor provisions contained in the Private Securities Litigation Reform Act of 1995. Examples of forward-looking statements include, but are not limited to: (i) projections of revenues, expenses, income or loss, earnings or loss per share, the payment or nonpayment of dividends, capital structure and other financial items; (ii) statements of plans, objectives and expectations of the Company or its management or board of directors, including those relating to products or services; (iii) statements of future economic performance; and (iv) statements of assumptions underlying such statements. Words such as believes, anticipates, expects, intends, targeted, plan, continue, remain, will, should, may and other similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

These forward-looking statements are based on Management's current knowledge and belief and include information concerning the Company's possible or assumed future financial condition and results of operations. A number of factors, some of which are beyond the Company's ability to predict or control, could cause future results to differ materially from those contemplated. These factors include but are not limited to (1) the length and severity of current difficulties in the national and California economies and the effects of federal government efforts to address those difficulties; (2) liquidity levels in capital markets; (3) fluctuations in asset prices including, but not limited to stocks, bonds, real estate, and commodities; (4) the effect of acquisitions and integration of acquired businesses including the recent acquisition of County Bank assets and assumption of County Bank liabilities from the Federal Deposit Insurance Corporation; (5) economic uncertainty created by terrorist threats and attacks on the United States, the actions taken in response, and the uncertain effect of these events on the national and regional economies; (6) changes in the interest rate environment; (7) changes in the regulatory environment; (8) competitive pressure in the banking industry; (9) operational risks including data processing system failures or fraud; (10) volatility of interest rate sensitive loans, deposits and investments; (11) asset/liability management risks and liquidity risks; and (12) changes in the securities markets. The Company undertakes no obligation to update any forward-looking statements in this report. The reader is directed to the Company's annual report on Form 10-K for the year ended December 31, 2009, for further discussion of factors which could affect the Company's business and cause actual results to differ materially from those expressed in any forward-looking statement made in this report. The Company undertakes no obligation to update any forward-looking statements in this report.

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1 Financial Statements**

**WESTAMERICA BANCORPORATION**  
**CONSOLIDATED BALANCE SHEETS**  
(unaudited)

|                                                              | At June 30,<br><b>2010</b> | At December 31,<br><b>2009</b> |
|--------------------------------------------------------------|----------------------------|--------------------------------|
|                                                              | (In thousands)             |                                |
| <b>Assets:</b>                                               |                            |                                |
| Cash and due from banks                                      | \$ 294,240                 | \$ 361,135                     |
| Money market assets                                          | 342                        | 442                            |
| Investment securities available for sale                     | 466,500                    | 384,208                        |
| Investment securities held to maturity, with fair values of: |                            |                                |
| \$669,319 at June 30, 2010                                   | 652,958                    |                                |
| \$736,270 at December 31, 2009                               |                            | 726,935                        |
| Non-covered loans                                            | 2,124,570                  | 2,201,088                      |
| Allowance for loan losses                                    | (39,716)                   | (41,043)                       |
| Non-covered loans, net of allowance for loan losses          | 2,084,854                  | 2,160,045                      |
| Covered loans                                                | 763,619                    | 855,301                        |
| Total loans                                                  | 2,848,473                  | 3,015,346                      |
| Non-covered other real estate owned                          | 18,028                     | 12,642                         |
| Covered other real estate owned                              | 23,670                     | 23,297                         |
| Premises and equipment, net                                  | 36,816                     | 38,098                         |
| Identifiable intangibles, net                                | 32,529                     | 35,667                         |
| Goodwill                                                     | 121,673                    | 121,699                        |
| Interest receivable and other assets                         | 231,857                    | 256,032                        |
| <b>Total Assets</b>                                          | <b>\$ 4,727,086</b>        | <b>\$ 4,975,501</b>            |
| <b>Liabilities:</b>                                          |                            |                                |
| Noninterest bearing deposits                                 | \$ 1,427,611               | \$ 1,428,432                   |
| Interest bearing deposits                                    | 2,462,949                  | 2,631,776                      |
| Total deposits                                               | 3,890,560                  | 4,060,208                      |
| Short-term borrowed funds                                    | 210,503                    | 227,178                        |
| Federal Home Loan Bank advances                              | 10,223                     | 85,470                         |
| Debt financing and notes payable                             | 26,430                     | 26,497                         |
| Liability for interest, taxes and other expenses             | 61,689                     | 70,700                         |
| <b>Total Liabilities</b>                                     | <b>4,199,405</b>           | <b>4,470,053</b>               |
| <b>Shareholders Equity:</b>                                  |                            |                                |
| Common stock, authorized - 150,000 shares                    |                            |                                |
| Issued and outstanding:                                      |                            |                                |

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|                                                  |                     |                     |
|--------------------------------------------------|---------------------|---------------------|
| 29,118 at June 30, 2010                          | 372,989             |                     |
| 29,208 at December 31, 2009                      |                     | 366,247             |
| Deferred compensation                            | 2,724               | 2,485               |
| Accumulated other comprehensive income           | 6,314               | 3,714               |
| Retained earnings                                | 145,654             | 133,002             |
| <b>Total Shareholders Equity</b>                 | <b>527,681</b>      | <b>505,448</b>      |
| <b>Total Liabilities and Shareholders Equity</b> | <b>\$ 4,727,086</b> | <b>\$ 4,975,501</b> |

See accompanying notes to unaudited condensed consolidated financial statements.



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**WESTAMERICA BANCORPORATION**  
**CONSOLIDATED STATEMENTS OF INCOME**  
(unaudited)

|                                                            | Three months ended<br>June 30,        |           | Six months ended<br>June 30, |           |
|------------------------------------------------------------|---------------------------------------|-----------|------------------------------|-----------|
|                                                            | 2010                                  | 2009      | 2010                         | 2009      |
|                                                            | (In thousands, except per share data) |           |                              |           |
| <b>Interest Income:</b>                                    |                                       |           |                              |           |
| Loans                                                      | \$ 44,060                             | \$ 49,523 | \$ 88,762                    | \$ 94,618 |
| Money market assets and funds sold                         |                                       | 1         | 1                            | 2         |
| Investment securities available for sale                   | 4,026                                 | 4,539     | 7,921                        | 8,278     |
| Investment securities held to maturity                     | 6,992                                 | 9,009     | 14,397                       | 19,359    |
| <b>Total Interest Income</b>                               | 55,078                                | 63,072    | 111,081                      | 122,257   |
| <b>Interest Expense:</b>                                   |                                       |           |                              |           |
| Deposits                                                   | 2,180                                 | 4,468     | 4,668                        | 8,252     |
| Short-term borrowed funds                                  | 491                                   | 568       | 1,028                        | 1,063     |
| Federal Home Loan Bank advances                            | 52                                    | 288       | 136                          | 419       |
| Notes payable                                              | 422                                   | 421       | 847                          | 844       |
| <b>Total Interest Expense</b>                              | 3,145                                 | 5,745     | 6,679                        | 10,578    |
| <b>Net Interest Income</b>                                 | 51,933                                | 57,327    | 104,402                      | 111,679   |
| <b>Provision for Loan Losses</b>                           | 2,800                                 | 2,600     | 5,600                        | 4,400     |
| <b>Net Interest Income After Provision For Loan Losses</b> | 49,133                                | 54,727    | 98,802                       | 107,279   |
| <b>Noninterest Income:</b>                                 |                                       |           |                              |           |
| Service charges on deposit accounts                        | 8,629                                 | 9,116     | 17,371                       | 17,538    |
| Merchant credit card                                       | 2,176                                 | 2,223     | 4,397                        | 4,655     |
| Debit card                                                 | 1,245                                 | 1,323     | 2,419                        | 2,389     |
| ATM and interchange                                        | 1,021                                 | 1,013     | 1,912                        | 1,826     |
| Trust fees                                                 | 448                                   | 373       | 829                          | 737       |
| Financial services commissions                             | 223                                   | 137       | 372                          | 291       |
| Other                                                      | 2,028                                 | 2,201     | 3,940                        | 4,074     |
| Gain on acquisition                                        |                                       |           |                              | 48,844    |
| <b>Total Noninterest Income</b>                            | 15,770                                | 16,386    | 31,240                       | 80,354    |
| <b>Noninterest Expense:</b>                                |                                       |           |                              |           |
| Salaries and related benefits                              | 15,476                                | 17,448    | 31,368                       | 33,819    |
| Occupancy                                                  | 3,822                                 | 5,413     | 7,599                        | 10,823    |
| Outsourced data processing services                        | 2,202                                 | 2,378     | 4,442                        | 4,482     |
| Amortization of identifiable intangibles                   | 1,540                                 | 1,695     | 3,138                        | 3,380     |
| Furniture and equipment                                    | 1,116                                 | 1,607     | 2,167                        | 2,829     |
| Courier service                                            | 903                                   | 994       | 1,810                        | 1,892     |

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|                                                  |                  |                  |                  |                  |
|--------------------------------------------------|------------------|------------------|------------------|------------------|
| Professional fees                                | 867              | 779              | 1,530            | 1,667            |
| FDIC insurance assessments                       | 1,260            | 3,221            | 2,580            | 3,378            |
| Other                                            | 4,909            | 5,131            | 9,492            | 10,519           |
| <b>Total Noninterest Expense</b>                 | <b>32,095</b>    | <b>38,666</b>    | <b>64,126</b>    | <b>72,789</b>    |
| <b>Income Before Income Taxes</b>                | <b>32,808</b>    | <b>32,447</b>    | <b>65,916</b>    | <b>114,844</b>   |
| Provision for income taxes                       | 9,247            | 9,264            | 18,779           | 38,836           |
| <b>Net Income</b>                                | <b>23,561</b>    | <b>23,183</b>    | <b>47,137</b>    | <b>76,008</b>    |
| Preferred stock dividends and discount accretion |                  | 1,107            |                  | 1,685            |
| <b>Net Income Applicable to Common Equity</b>    | <b>\$ 23,561</b> | <b>\$ 22,076</b> | <b>\$ 47,137</b> | <b>\$ 74,323</b> |
| <b>Average Common Shares Outstanding</b>         | <b>29,207</b>    | <b>29,126</b>    | <b>29,217</b>    | <b>29,002</b>    |
| <b>Diluted Average Common Shares Outstanding</b> | <b>29,568</b>    | <b>29,403</b>    | <b>29,582</b>    | <b>29,254</b>    |
| <b>Per Common Share Data:</b>                    |                  |                  |                  |                  |
| Basic earnings                                   | \$ 0.81          | \$ 0.76          | \$ 1.61          | \$ 2.56          |
| Diluted earnings                                 | 0.80             | 0.75             | 1.59             | 2.54             |
| Dividends paid                                   | 0.36             | 0.35             | 0.72             | 0.71             |

See accompanying notes to unaudited condensed consolidated financial statements.

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**WESTAMERICA BANCORPORATION**  
**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY AND**  
**COMPREHENSIVE INCOME**

(unaudited)

|                                                                           | Common<br>Shares<br>Outstanding | Preferred<br>Stock | Common<br>Stock | Accumulated<br>Deferred<br>Compensation<br>(In thousands) | Comprehensive<br>Income | Retained<br>Earnings | Total      |
|---------------------------------------------------------------------------|---------------------------------|--------------------|-----------------|-----------------------------------------------------------|-------------------------|----------------------|------------|
| <b>Balance,<br/>December 31, 2008</b>                                     | 28,880                          | \$                 | \$ 352,265      | \$ 2,409                                                  | \$ 1,040                | \$ 54,138            | \$ 409,852 |
| Comprehensive<br>income                                                   |                                 |                    |                 |                                                           |                         |                      |            |
| Net income for the<br>period                                              |                                 |                    |                 |                                                           |                         | 76,008               | 76,008     |
| Other comprehensive<br>income, net of tax:                                |                                 |                    |                 |                                                           |                         |                      |            |
| Increase in net<br>unrealized gain on<br>securities available for<br>sale |                                 |                    |                 |                                                           | 689                     |                      | 689        |
| Post-retirement<br>benefit transition<br>obligation<br>amortization       |                                 |                    |                 |                                                           | 18                      |                      | 18         |
| Total comprehensive<br>income                                             |                                 |                    |                 |                                                           |                         |                      | 76,715     |
| Issuance of preferred<br>stock and related<br>warrants                    |                                 | 82,519             | 1,207           |                                                           |                         |                      | 83,726     |
| Preferred stock<br>dividends and<br>discount accretion                    |                                 | 92                 |                 |                                                           |                         | (1,685)              | (1,593)    |
| Exercise of stock<br>options                                              | 350                             |                    | 9,070           |                                                           |                         |                      | 9,070      |
| Stock option tax<br>benefits                                              |                                 |                    | 2,179           |                                                           |                         |                      | 2,179      |
| Restricted stock<br>activity                                              | 7                               |                    | 251             | 76                                                        |                         |                      | 327        |
| Stock based<br>compensation                                               |                                 |                    | 594             |                                                           |                         |                      | 594        |
| Stock awarded to<br>employees                                             | 1                               |                    | 62              |                                                           |                         |                      | 62         |
| Purchase and<br>retirement of stock                                       | (24)                            |                    | (273)           |                                                           |                         | (814)                | (1,087)    |
| Dividends                                                                 |                                 |                    |                 |                                                           |                         | (20,614)             | (20,614)   |

|                                                                  |        |           |            |          |          |            |            |
|------------------------------------------------------------------|--------|-----------|------------|----------|----------|------------|------------|
| <b>Balance, June 30, 2009</b>                                    | 29,214 | \$ 82,611 | \$ 365,355 | \$ 2,485 | \$ 1,747 | \$ 107,033 | \$ 559,231 |
| <b>Balance, December 31, 2009</b>                                | 29,208 | \$        | \$ 366,247 | \$ 2,485 | \$ 3,714 | \$ 133,002 | \$ 505,448 |
| Comprehensive income                                             |        |           |            |          |          |            |            |
| Net income for the period                                        |        |           |            |          |          | 47,137     | 47,137     |
| Other comprehensive income, net of tax:                          |        |           |            |          |          |            |            |
| Increase in net unrealized gain on securities available for sale |        |           |            |          |          | 2,582      | 2,582      |
| Post-retirement benefit transition obligation amortization       |        |           |            |          |          | 18         | 18         |
| Total comprehensive income                                       |        |           |            |          |          |            | 49,737     |
| Exercise of stock options                                        | 210    |           | 8,783      |          |          |            | 8,783      |
| Stock option tax benefits                                        |        |           | 796        |          |          |            | 796        |
| Restricted stock activity                                        | 7      |           | 194        | 239      |          |            | 433        |
| Stock based compensation                                         |        |           | 720        |          |          |            | 720        |
| Stock awarded to employees                                       | 1      |           | 77         |          |          |            | 77         |
| Purchase and retirement of stock                                 | (308)  |           | (3,828)    |          |          | (13,392)   | (17,220)   |
| Dividends                                                        |        |           |            |          |          | (21,093)   | (21,093)   |
| <b>Balance, June 30, 2010</b>                                    | 29,118 | \$        | \$ 372,989 | \$ 2,724 | \$ 6,314 | \$ 145,654 | \$ 527,681 |

See accompanying notes to unaudited condensed consolidated financial statements.

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**WESTAMERICA BANCORPORATION**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(unaudited)

|                                                                                   | For the six months<br>ended June 30, |                |
|-----------------------------------------------------------------------------------|--------------------------------------|----------------|
|                                                                                   | <b>2010</b>                          | <b>2009</b>    |
|                                                                                   | (In thousands)                       |                |
| <b>Operating Activities:</b>                                                      |                                      |                |
| Net income                                                                        | \$ 47,137                            | \$ 76,008      |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                      |                |
| Depreciation and amortization                                                     | 7,589                                | 4,762          |
| Loan loss provision                                                               | 5,600                                | 4,400          |
| Net amortization of deferred loan cost                                            | 28                                   | 124            |
| Decrease (increase) in interest income receivable                                 | 657                                  | (3,306)        |
| Gain on acquisition                                                               |                                      | (48,844)       |
| (Increase) decrease in other assets                                               | (10,872)                             | 55,701         |
| Increase (decrease) in income taxes payable                                       | 2,899                                | (7,366)        |
| (Decrease) increase in interest expense payable                                   | (1)                                  | 275            |
| (Decrease) increase in other liabilities                                          | (13,866)                             | 11,316         |
| Stock option compensation expense                                                 | 720                                  | 594            |
| Stock option tax benefits                                                         | (796)                                | (2,179)        |
| Gain on sale of other assets                                                      | (608)                                |                |
| Gain on sale of property and equipment                                            | (447)                                |                |
| Originations of mortgage loans for resale                                         | (277)                                | (68)           |
| Net proceeds from sale of mortgage loans originated for resale                    | 288                                  | 70             |
| Net gain on sale of foreclosed assets                                             | (478)                                | (166)          |
| Writedown of foreclosed assets                                                    | 399                                  | 83             |
| <b>Net Cash Provided by Operating Activities</b>                                  | <b>37,972</b>                        | <b>91,404</b>  |
| <b>Investing Activities:</b>                                                      |                                      |                |
| Net repayments of loans                                                           | 145,389                              | 184,065        |
| Proceeds from FDIC loss-sharing indemnification                                   | 29,841                               | 6,421          |
| Purchases of investment securities available for sale                             | (149,493)                            |                |
| Proceeds from maturity/calls of securities available for sale                     | 73,064                               | 53,289         |
| Proceeds from maturity/calls of securities held to maturity                       | 73,977                               | 121,708        |
| Net change in FRB/FHLB* securities                                                | 3,121                                | 1,502          |
| Proceeds from sale of foreclosed assets                                           | 8,071                                | 5,557          |
| Purchases of property, plant and equipment                                        | (448)                                | (566)          |
| Proceeds from sale of property, plant and equipment                               | 603                                  |                |
| Net cash acquired from acquisitions                                               |                                      | 44,397         |
| <b>Net Cash Provided by Investing Activities</b>                                  | <b>184,125</b>                       | <b>416,373</b> |
| <b>Financing Activities:</b>                                                      |                                      |                |
| Net change in deposits                                                            | (168,106)                            | (168,279)      |

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|                                                        |                   |                   |
|--------------------------------------------------------|-------------------|-------------------|
| Net change in short-term borrowings                    | (92,152)          | (381,808)         |
| Exercise of stock options                              | 8,783             | 9,070             |
| Proceeds from issuance of preferred stock              |                   | 83,726            |
| Stock option tax benefits                              | 796               | 2,179             |
| Repurchases/retirement of stock                        | (17,220)          | (1,087)           |
| Dividends paid                                         | (21,093)          | (20,614)          |
| Preferred dividends                                    |                   | (1,070)           |
| <b>Net Cash Used in Financing Activities</b>           | <b>(288,992)</b>  | <b>(477,883)</b>  |
| <b>Net Change In Cash and Due from Banks</b>           | <b>(66,895)</b>   | <b>29,894</b>     |
| <b>Cash and Due from Banks at Beginning of Period</b>  | <b>361,135</b>    | <b>138,883</b>    |
| <b>Cash and Due from Banks at End of Period</b>        | <b>\$ 294,240</b> | <b>\$ 168,777</b> |
| <b>Supplemental Cash Flow Disclosures:</b>             |                   |                   |
| Supplemental disclosure of non cash activities:        |                   |                   |
| Loan collateral transferred to other real estate owned | \$ 13,749         | \$ 14,668         |
| Unrealized gain on securities available for sale, net  | 2,582             | 689               |
| Supplemental disclosure of cash flow activities:       |                   |                   |
| Interest paid for the period                           | 8,058             | 14,413            |
| Income tax payments for the period                     | 27,257            | 19,144            |
| Acquisitions:                                          |                   |                   |
| Assets acquired                                        | \$                | \$ 1,624,464      |
| Liabilities assumed                                    |                   | 1,575,620         |
| Net                                                    | \$                | \$ 48,844         |

See accompanying notes to unaudited condensed consolidated financial statements.

\* Federal Reserve  
Bank/Federal  
Home Loan  
Bank  
( FRB/FHLB )

**Table of Contents****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****Note 1: Basis of Presentation**

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. The results of operations reflect interim adjustments, all of which are of a normal recurring nature and which, in the opinion of Management, are necessary for a fair presentation of the results for the interim periods presented. The interim results for the three and six months ended June 30, 2010 and 2009 are not necessarily indicative of the results expected for the full year. These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes as well as other information included in the Company's Annual Report on Form 10-K for the year ended December 31, 2009.

The Company has evaluated events and transactions subsequent to the balance sheet date. Based on this evaluation, the Company is not aware of any events or transactions that occurred subsequent to the balance sheet date but prior to filing that would require recognition or disclosure in its consolidated financial statements.

**Note 2: Accounting Policies**

Certain accounting policies underlying the preparation of these financial statements require Management to make estimates and judgments. These estimates and judgments may significantly affect reported amounts of assets and liabilities, revenues and expenses, and disclosures of contingent assets and liabilities.

Management exercises judgment to estimate the appropriate level of the allowance for credit losses and purchased impaired loans, which are discussed in Note 1 to the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2009. Certain amounts in prior periods have been reclassified to conform to the current presentation.

**Recently Adopted Accounting Standards**

In the first quarter of 2010, the Company adopted the following new accounting guidance:

Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 860 as amended, *Transfers and Servicing* (formerly FASB Statement No. 166, *Accounting for Transfers of Financial Assets – an amendment of the provisions contained in FASB ASC 860*)

FASB ASC 810, *Consolidation* as amended (formerly FASB Statement No. 167, *Amendments to FASB ASC 810, Consolidation*)

FASB Accounting Standards Update (ASU) 2010-06, Fair Value Measurements and Disclosure (Topic 820)

FASB ASC 860, as amended, *Transfers and Servicing*, has been amended to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. Specifically to address: (1) practices that have developed since initial issuance, that are not consistent with the original intent and key requirements of that Standard and (2) concerns of financial statement users that many of the financial assets (and related obligations) that have been derecognized should continue to be reported in the financial statements of transferors. This Standard must be applied to transfers occurring on or after January 1, 2010, the effective date. Additionally, on and after the effective date, the concept of a qualifying special-purpose entity is no longer relevant for accounting purposes. The adoption of this Statement did not have any effect on the Company's financial statements at the date of adoption.

FASB ASC 810, as amended, *Consolidation*, has been amended to improve financial reporting by enterprises involved with variable interest entities. Specifically to address: (1) the effects on certain provisions as a result of the elimination of the qualifying special-purpose entity concept in ASC 860, *Transfers and Servicing*, and (2) constituent concerns about the application of certain key provisions of the Standard, including those in which the accounting and disclosures do not always provide timely and useful information about an enterprise's involvement in a variable interest entity. The adoption of this Statement did not have any effect on the Company's financial statements at the date of adoption.





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FASB ASU 2010-06, *Fair Value Measurements and Disclosures (Topic 820)*, issued January 2010 and effective January 1, 2010, requires new disclosures for: (1) transfers in and out of Levels 1 and 2, including separate disclosure of significant amounts and a description of the reasons for the transfers; and (2) separate presentation of information about purchases, sales, issuances, and settlements (on a gross basis rather than net) in the reconciliation for fair value measurements using significant unobservable inputs (Level 3). The Update clarifies existing disclosure requirements for: (1) Level of disaggregation, which provides measurement disclosures for each class of assets and liabilities. Emphasizing that judgment should be used in determining the appropriate classes of assets and liabilities; and (2) inputs and valuation techniques for both recurring and nonrecurring Level 2 and Level 3 fair value measurements. This update also includes conforming amendments to the guidance on employer's disclosures about postretirement benefit plan assets changing the terminology of major categories of assets to classes of assets and providing a cross reference to the guidance in Subtopic 820-10 on how to determine appropriate classes to present fair value disclosures. The adoption of this Update did not have a significant effect on the Company's financial statements at the date of adoption.

**Recently Issued Accounting Standards**

FASB ASU 2010-18, *Effect of a Loan Modification When the Loan is Part of a Pool that is Accounted for as a Single Asset (Topic 310)*, was issued April 2010 and is effective for modifications of loans accounted for within pools under Subtopic 310-30 occurring in the first interim or annual period ending after July 15, 2010. As a result of the amendments in this Update, modification of loans within the pool does not result in the removal of those loans from the pool even if the modification of those loans would otherwise be considered a troubled debt restructuring. An entity will continue to be required to consider whether the pool of assets in which the loan is included is impaired if expected cash flows for the pool change. However, loans within the scope of Subtopic 310-30 that are accounted for individually will continue to be subject to the troubled debt restructuring accounting provisions.

The provisions of this Update will be applied prospectively with early application permitted. Upon initial adoption of the guidance in this Update, an entity may make a one-time election to terminate accounting for loans as a pool under Subtopic 310-30. The election may be applied on a pool-by-pool basis and does not preclude an entity from applying pool accounting to subsequent acquisitions of loans with credit deterioration.

The Company does not have any pools of loans accounted for in accordance with Subtopic 310-30, and therefore, the adoption of this Update will not have a significant effect on the Company's financial statements.

FASB ASU 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses (Topic 310)*, was issued July 2010. The guidance will significantly expand the disclosures that the Company must make about the credit quality of financing receivables and the allowance for credit losses. The objectives of the enhanced disclosures are to provide financial statement users with additional information about the nature of credit risks inherent in the Company's financing receivables, how credit risk is analyzed and assessed when determining the allowance for credit losses, and the reasons for the change in the allowance for credit losses.

The disclosures as of the end of the reporting period are effective for the Company's interim and annual periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for the Company's interim and annual periods beginning on or after December 15, 2010. The adoption of this Update requires enhanced disclosures and is not expected to have a significant effect on the Company's financial statements.

**Table of Contents****Note 3: Investment Securities**

The amortized cost, unrealized gains and losses accumulated in other comprehensive income, and fair value of the available for sale investment securities portfolio as of June 30, 2010, follows:

|                                                  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|--------------------------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| (In thousands)                                   |                   |                              |                               |               |
| U.S. Treasury securities                         | \$ 2,994          | \$ 3                         | \$                            | \$ 2,997      |
| Securities of U.S. Government sponsored entities | 72,140            | 279                          | (12)                          | 72,407        |
| Residential mortgage-backed securities           | 123,326           | 5,555                        |                               | 128,881       |
| Commercial mortgage-backed securities            | 5,305             |                              | (49)                          | 5,256         |
| Obligations of States and political subdivisions | 185,229           | 4,062                        | (704)                         | 188,587       |
| Residential collateralized mortgage obligations  | 28,362            | 1,153                        | (5)                           | 29,510        |
| Asset-backed securities                          | 9,741             |                              | (1,212)                       | 8,529         |
| FHLMC and FNMA stock                             | 824               | 53                           | (88)                          | 789           |
| Corporate securities                             | 24,442            |                              | (158)                         | 24,284        |
| Other securities                                 | 2,778             | 2,496                        | (14)                          | 5,260         |
| Total                                            | \$ 455,141        | \$ 13,601                    | \$ (2,242)                    | \$ 466,500    |

The amortized cost, unrealized gains and losses, and fair value of the held to maturity investment securities portfolio as of June 30, 2010, follows:

|                                                  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|--------------------------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| (In thousands)                                   |                   |                              |                               |               |
| Residential mortgage-backed securities           | \$ 52,490         | \$ 2,101                     | \$ (2)                        | \$ 54,589     |
| Obligations of States and political subdivisions | 481,895           | 16,341                       | (918)                         | 497,318       |
| Residential collateralized mortgage obligations  | 118,573           | 3,037                        | (4,198)                       | 117,412       |
| Total                                            | \$ 652,958        | \$ 21,479                    | \$ (5,118)                    | \$ 669,319    |

The amortized cost, unrealized gains and losses accumulated in other comprehensive income, and fair value of the available for sale investment securities portfolio as of December 31, 2009, follows:

|                                                  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|--------------------------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| (In thousands)                                   |                   |                              |                               |               |
| U.S. Treasury securities                         | \$ 2,987          | \$                           | \$                            | \$ 2,987      |
| Securities of U.S. Government sponsored entities | 21,018            | 48                           | (25)                          | 21,041        |
| Residential mortgage-backed securities           | 143,625           | 2,504                        | (124)                         | 146,005       |
| Obligations of States and political subdivisions | 155,093           | 4,077                        | (977)                         | 158,193       |
| Residential collateralized mortgage obligations  | 40,981            | 652                          | (223)                         | 41,410        |
| Asset-backed securities                          | 10,000            |                              | (1,661)                       | 8,339         |
| FHLMC and FNMA stock                             | 824               | 750                          | (1)                           | 1,573         |
| Other securities                                 | 2,778             | 1,926                        | (44)                          | 4,660         |

|       |            |          |            |            |
|-------|------------|----------|------------|------------|
| Total | \$ 377,306 | \$ 9,957 | \$ (3,055) | \$ 384,208 |
|-------|------------|----------|------------|------------|

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The amortized cost, unrealized gains and losses, and fair value of the held to maturity investment securities portfolio as of December 31, 2009 follows:

|                                                  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|--------------------------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| (In thousands)                                   |                   |                              |                               |               |
| Residential mortgage-backed securities           | \$ 61,893         | \$ 1,752                     | \$                            | \$ 63,645     |
| Obligations of States and political subdivisions | 516,596           | 12,528                       | (2,190)                       | 526,934       |
| Residential collateralized mortgage obligations  | 148,446           | 3,352                        | (6,107)                       | 145,691       |
| Total                                            | \$ 726,935        | \$ 17,632                    | \$ (8,297)                    | \$ 736,270    |

The amortized cost and fair value of securities as of June 30, 2010, by contractual maturity, are shown in the following table:

|                                                                       | Securities Available<br>for Sale |               | Securities Held<br>to Maturity |               |
|-----------------------------------------------------------------------|----------------------------------|---------------|--------------------------------|---------------|
|                                                                       | Amortized<br>Cost                | Fair<br>Value | Amortized<br>Cost              | Fair<br>Value |
| (In thousands)                                                        |                                  |               |                                |               |
| Maturity in years:                                                    |                                  |               |                                |               |
| 1 year or less                                                        | \$ 24,498                        | \$ 24,568     | \$ 7,691                       | \$ 7,727      |
| Over 1 to 5 years                                                     | 163,183                          | 164,854       | 70,312                         | 72,966        |
| Over 5 to 10 years                                                    | 47,155                           | 48,921        | 385,367                        | 397,843       |
| Over 10 years                                                         | 59,710                           | 58,461        | 18,525                         | 18,782        |
| Subtotal                                                              | 294,546                          | 296,804       | 481,895                        | 497,318       |
| Mortgage-backed securities and collateralized<br>mortgage obligations | 156,993                          | 163,647       | 171,063                        | 172,001       |
| Other securities                                                      | 3,602                            | 6,049         |                                |               |
| Total                                                                 | \$ 455,141                       | \$ 466,500    | \$ 652,958                     | \$ 669,319    |

The amortized cost and fair value of securities as of December 31, 2009, by contractual maturity, are shown in the following table:

|                    | Securities Available<br>for Sale |               | Securities Held<br>to Maturity |               |
|--------------------|----------------------------------|---------------|--------------------------------|---------------|
|                    | Amortized<br>Cost                | Fair<br>Value | Amortized<br>Cost              | Fair<br>Value |
| (In thousands)     |                                  |               |                                |               |
| Maturity in years: |                                  |               |                                |               |
| 1 year or less     | \$ 12,763                        | \$ 12,852     | \$ 8,303                       | \$ 8,389      |
| Over 1 to 5 years  | 86,757                           | 88,759        | 58,111                         | 60,075        |
| Over 5 to 10 years | 61,532                           | 62,933        | 413,720                        | 421,955       |
| Over 10 years      | 28,046                           | 26,016        | 36,462                         | 36,515        |
| Subtotal           | 189,098                          | 190,560       | 516,596                        | 526,934       |

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|                                                                    |            |            |            |            |
|--------------------------------------------------------------------|------------|------------|------------|------------|
| Mortgage-backed securities and collateralized mortgage obligations | 184,606    | 187,415    | 210,339    | 209,336    |
| Other securities                                                   | 3,602      | 6,233      |            |            |
| Total                                                              | \$ 377,306 | \$ 384,208 | \$ 726,935 | \$ 736,270 |

Expected maturities of mortgage-backed securities can differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call or prepayment penalties. In addition, such factors as prepayments and interest rates may affect the yield on the carrying value of mortgage-backed securities.

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An analysis of gross unrealized losses of the available for sale investment securities portfolio as of June 30, 2010, follows:

|                                                  | Less than 12 months |                   | 12 months or longer |                   | Total            |                   |
|--------------------------------------------------|---------------------|-------------------|---------------------|-------------------|------------------|-------------------|
|                                                  | Fair Value          | Unrealized Losses | Fair Value          | Unrealized Losses | Fair Value       | Unrealized Losses |
|                                                  | (In thousands)      |                   |                     |                   |                  |                   |
| Securities of U.S. Government sponsored entities | \$ 10,075           | \$ (12)           | \$                  | \$                | \$ 10,075        | \$ (12)           |
| Commercial mortgage-backed securities            | 5,275               | (49)              |                     |                   | 5,275            | (49)              |
| Obligations of States and political subdivisions | 25,893              | (366)             | 10,314              | (338)             | 36,207           | (704)             |
| Residential collateralized mortgage obligations  | 641                 | (1)               | 890                 | (4)               | 1,531            | (5)               |
| Asset-backed securities                          |                     |                   | 8,529               | (1,212)           | 8,529            | (1,212)           |
| FHLMC and FNMA stock                             | 462                 | (88)              |                     |                   | 462              | (88)              |
| Corporate securities                             | 20,343              | (158)             |                     |                   | 20,343           | (158)             |
| Other securities                                 |                     |                   | 1,986               | (14)              | 1,986            | (14)              |
| <b>Total</b>                                     | <b>\$ 62,689</b>    | <b>\$ (674)</b>   | <b>\$ 21,719</b>    | <b>\$ (1,568)</b> | <b>\$ 84,408</b> | <b>\$ (2,242)</b> |

An analysis of gross unrealized losses of the held to maturity investment securities portfolio as of June 30, 2010, follows:

|                                                  | Less than 12 months |                   | 12 months or longer |                   | Total            |                   |
|--------------------------------------------------|---------------------|-------------------|---------------------|-------------------|------------------|-------------------|
|                                                  | Fair Value          | Unrealized Losses | Fair Value          | Unrealized Losses | Fair Value       | Unrealized Losses |
|                                                  | (In thousands)      |                   |                     |                   |                  |                   |
| Residential mortgage backed securities           | \$ 677              | \$ (2)            | \$                  | \$                | \$ 677           | \$ (2)            |
| Obligations of States and political subdivisions | 23,554              | (829)             | 7,658               | (89)              | 31,212           | (918)             |
| Residential collateralized mortgage obligations  | 2,620               | (6)               | 27,748              | (4,192)           | 30,368           | (4,198)           |
| <b>Total</b>                                     | <b>\$ 26,851</b>    | <b>\$ (837)</b>   | <b>\$ 35,406</b>    | <b>\$ (4,281)</b> | <b>\$ 62,257</b> | <b>\$ (5,118)</b> |

The unrealized losses on the Company's investments in collateralized mortgage obligations and asset backed securities were caused by market conditions for these types of investments. The Company evaluates these securities on a quarterly basis including changes in security ratings issued by ratings agencies, delinquency and loss information with respect to the underlying collateral, changes in the levels of subordination for the Company's particular position within the repayment structure, and remaining credit enhancement as compared to expected credit losses of the security. Substantially all of these securities continue to be AAA rated by one or more major rating agencies.

The unrealized losses on the Company's investments in obligations of states and political subdivisions were caused by conditions in the municipal securities market. The Company's investments in obligations of states and political subdivisions primarily finance essential community services such as school districts, water delivery systems, hospitals

and fire protection services. Further, these bonds are primarily bank qualified issues whereby the issuing authority's total debt issued in any one year does not exceed \$30 million, thereby qualifying the bonds for tax-exempt status for federal income tax purposes. Therefore, bank qualified bonds are relatively small in amount providing a high degree of diversification within the Company's investment portfolio. The Company evaluates these securities quarterly to determine if a change in security rating has occurred or the municipality has experienced financial difficulties. Substantially all of these securities continue to be investment grade rated.

The Company does not intend to sell any investments and has concluded that it is more likely than not that it will not be required to sell the investments prior to recovery of the amortized cost basis. Therefore, the Company does not consider these investments to be other-than-temporarily impaired as of June 30, 2010.

The fair values of the investment securities could decline in the future if the general economy deteriorates, credit ratings decline, or the liquidity for securities is low. As a result, other than temporary impairments may occur in the future.

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An analysis of gross unrealized losses of the available for sale investment securities portfolio as of December 31, 2009, follows:

|                                                  | Less than 12 months |                   | 12 months or longer |                   | Total            |                   |
|--------------------------------------------------|---------------------|-------------------|---------------------|-------------------|------------------|-------------------|
|                                                  | Fair Value          | Unrealized Losses | Fair Value          | Unrealized Losses | Fair Value       | Unrealized Losses |
|                                                  | (In thousands)      |                   |                     |                   |                  |                   |
| U.S. Treasury securities                         | \$ 2,987            | \$                | \$                  | \$                | \$ 2,987         | \$                |
| Securities of U.S. Government sponsored entities | 19,979              | (25)              |                     |                   | 19,979           | (25)              |
| Residential mortgage-backed securities           | 17,885              | (124)             |                     |                   | 17,885           | (124)             |
| Obligations of States and political subdivisions | 25,050              | (795)             | 3,866               | (182)             | 28,916           | (977)             |
| Residential collateralized mortgage obligations  | 9,896               | (37)              | 5,002               | (186)             | 14,898           | (223)             |
| Asset-backed securities                          |                     |                   | 8,339               | (1,661)           | 8,339            | (1,661)           |
| FHLMC and FNMA stock                             | 4                   | (1)               |                     |                   | 4                | (1)               |
| Other securities                                 |                     |                   | 1,956               | (44)              | 1,956            | (44)              |
| <b>Total</b>                                     | <b>\$ 75,801</b>    | <b>\$ (982)</b>   | <b>\$ 19,163</b>    | <b>\$ (2,073)</b> | <b>\$ 94,964</b> | <b>\$ (3,055)</b> |

An analysis of gross unrealized losses of the held to maturity investment securities portfolio as of December 31, 2009, follows:

|                                                  | Less than 12 months |                   | 12 months or longer |                   | Total             |                   |
|--------------------------------------------------|---------------------|-------------------|---------------------|-------------------|-------------------|-------------------|
|                                                  | Fair Value          | Unrealized Losses | Fair Value          | Unrealized Losses | Fair Value        | Unrealized Losses |
|                                                  | (In thousands)      |                   |                     |                   |                   |                   |
| Obligations of States and political subdivisions | \$ 46,111           | \$ (995)          | \$ 16,964           | \$ (1,195)        | \$ 63,075         | \$ (2,190)        |
| Residential collateralized mortgage obligations  | 7,639               | (42)              | 30,674              | (6,065)           | 38,313            | (6,107)           |
| <b>Total</b>                                     | <b>\$ 53,750</b>    | <b>\$ (1,037)</b> | <b>\$ 47,638</b>    | <b>\$ (7,260)</b> | <b>\$ 101,388</b> | <b>\$ (8,297)</b> |

**Note 4: Loans and Allowance for Credit Losses**

A summary of the major categories of non-covered and covered loans outstanding is shown in the following tables:

|                         | At June 30,<br>2010 | At December 31,<br>2009 |
|-------------------------|---------------------|-------------------------|
|                         | (In thousands)      |                         |
| Non-covered loans:      |                     |                         |
| Commercial              | \$ 509,601          | \$ 498,594              |
| Commercial real estate  | 780,757             | 801,008                 |
| Construction            | 28,220              | 32,156                  |
| Residential real estate | 336,897             | 371,197                 |



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|                              |              |              |
|------------------------------|--------------|--------------|
| Consumer installment & other | 469,095      | 498,133      |
| Gross Loans                  | 2,124,570    | 2,201,088    |
| Allowance for loan losses    | (39,716)     | (41,043)     |
| Net Loans                    | \$ 2,084,854 | \$ 2,160,045 |

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The carrying amount of the covered loans at June 30, 2010, consisted of impaired and non impaired purchased loans in the following table.

|                              | Impaired<br>Purchased<br>Loans | Non Impaired<br>Purchased<br>Loans<br>(In thousands) | Total<br>Covered<br>Loans |
|------------------------------|--------------------------------|------------------------------------------------------|---------------------------|
| Covered loans:               |                                |                                                      |                           |
| Commercial                   | \$ 11,040                      | \$ 193,953                                           | \$ 204,993                |
| Commercial real estate       | 14,132                         | 402,975                                              | 417,107                   |
| Construction                 | 10,583                         | 19,750                                               | 30,333                    |
| Residential real estate      | 138                            | 18,059                                               | 18,197                    |
| Consumer installment & other | 260                            | 92,729                                               | 92,989                    |
| Total loans                  | \$ 36,153                      | \$ 727,466                                           | \$ 763,619                |

The carrying amount of the covered loans at December 31, 2009, consisted of impaired and non impaired purchased loans in the following table (refined).

|                              | Impaired<br>Purchased<br>Loans | Non Impaired<br>Purchased<br>Loans<br>(In thousands) | Total<br>Covered<br>Loans |
|------------------------------|--------------------------------|------------------------------------------------------|---------------------------|
| Covered loans:               |                                |                                                      |                           |
| Commercial                   | \$ 8,538                       | \$ 244,811                                           | \$ 253,349                |
| Commercial real estate       | 19,870                         | 425,570                                              | 445,440                   |
| Construction                 | 14,378                         | 26,082                                               | 40,460                    |
| Residential real estate      | 138                            | 18,383                                               | 18,521                    |
| Consumer installment & other | 272                            | 97,259                                               | 97,531                    |
| Total loans                  | \$ 43,196                      | \$ 812,105                                           | \$ 855,301                |

Changes in the carrying amount of impaired purchased loans were as follows for the six months ended June 30, 2010 and the period February 6, 2009 (acquisition date) through December 31, 2009:

|                                                | Six months<br>ended<br>June 30,<br>2010 | February 6, 2009<br>through<br>December 31,<br>2009<br>(refined) |
|------------------------------------------------|-----------------------------------------|------------------------------------------------------------------|
|                                                | (In thousands)                          |                                                                  |
| Carrying amount at the beginning of the period | \$ 43,196                               | \$ 80,544                                                        |
| Reductions during the period                   | (7,043)                                 | (37,348)                                                         |
| Carrying amount at the end of the period       | \$ 36,153                               | \$ 43,196                                                        |

Impaired purchased loans had an unpaid principal balance (less prior charge-offs) of \$55 million, \$70 million and \$164 million at June 30, 2010, December 31, 2009 and February 6, 2009, respectively.

The Company pledges loans to secure borrowings from the Federal Home Loan Bank (FHLB). At June 30, 2010, loans pledged to secure borrowing totaled \$80.4 million. The FHLB does not have the right to sell or repledge such loans.

There were no loans held for sale at June 30, 2010 and December 31, 2009.

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The following summarizes the allowance for credit losses of the Company for the periods indicated:

|                                            | Three months ended<br>June 30, |           | Six months ended<br>June 30, |           |
|--------------------------------------------|--------------------------------|-----------|------------------------------|-----------|
|                                            | 2010                           | 2009      | 2010                         | 2009      |
|                                            | (In thousands)                 |           |                              |           |
| Balance, beginning of period               | \$ 43,009                      | \$ 46,896 | \$ 43,736                    | \$ 47,563 |
| Provision for loan losses                  | 2,800                          | 2,600     | 5,600                        | 4,400     |
| Provision for unfunded commitments         |                                | (400)     |                              | (400)     |
| Loans charged off                          | (4,255)                        | (3,937)   | (8,711)                      | (6,865)   |
| Recoveries of previously charged off loans | 855                            | 656       | 1,784                        | 1,117     |
| Net loan losses                            | (3,400)                        | (3,281)   | (6,927)                      | (5,748)   |
| Balance, end of period                     | \$ 42,409                      | \$ 45,815 | \$ 42,409                    | \$ 45,815 |
| Components:                                |                                |           |                              |           |
| Allowance for loan losses                  | \$ 39,716                      | \$ 43,122 |                              |           |
| Reserve for unfunded credit commitments    | 2,693                          | 2,693     |                              |           |
| Allowance for credit losses                | \$ 42,409                      | \$ 45,815 |                              |           |

Allowance for loan losses / non-covered loans  
outstanding

1.87%                      1.86%

Management determined the credit default fair value discounts assigned to covered loans purchased on February 6, 2009 remained adequate as an estimate of credit losses inherent in covered loans as of June 30, 2010.

Non-covered nonaccrual loans at June 30, 2010 and December 31, 2009 were \$20.0 million and \$19.9 million, respectively. Covered nonaccrual loans at June 30, 2010 and December 31, 2009 were \$60.3 million and \$85.1 million, respectively.

There were no commitments to lend additional funds to borrowers whose loans were on nonaccrual status at June 30, 2010.

**Note 5: Goodwill and Other Identifiable Intangible Assets**

The Company has recorded goodwill and other identifiable intangibles associated with purchase business combinations. Goodwill is not amortized, but is periodically evaluated for impairment. The Company did not recognize impairment during the six months ended June 30, 2010.

The changes in the carrying value of goodwill were (in thousands):

|                                                                                            |            |
|--------------------------------------------------------------------------------------------|------------|
| December 31, 2009                                                                          | \$ 121,699 |
| Recognition of stock option tax benefits for the exercise of options converted upon merger | (26)       |
| June 30, 2010                                                                              | \$ 121,673 |

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Identifiable intangibles are amortized to their estimated residual values over their expected useful lives. Such lives and residual values are also periodically reassessed to determine if any amortization period adjustments are indicated. During the six months ended June 30, 2010, no such adjustments were recorded. The gross carrying amount of identifiable intangible assets and accumulated amortization was:

|                                      | At June 30,<br>2010         |                             | At December 31,<br>2009     |                             |
|--------------------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
|                                      | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization |
|                                      | (In thousands)              |                             |                             |                             |
| Core Deposit Intangibles             | \$ 51,538                   | \$ (21,896)                 | \$ 51,538                   | \$ (19,160)                 |
| Merchant Draft Processing Intangible | 10,300                      | (7,413)                     | 10,300                      | (7,011)                     |
| Total Identifiable Intangible Assets | \$ 61,838                   | \$ (29,309)                 | \$ 61,838                   | \$ (26,171)                 |

As of June 30, 2010, the current year and estimated future amortization expense for identifiable intangible assets was:

|                                           | Core<br>Deposit<br>Intangibles | Merchant<br>Draft<br>Processing<br>Intangible | Total    |
|-------------------------------------------|--------------------------------|-----------------------------------------------|----------|
|                                           | (In thousands)                 |                                               |          |
| Six months ended June 30, 2010 (actual)   | \$ 2,736                       | \$ 402                                        | \$ 3,138 |
| Estimate for year ended December 31, 2010 | 5,361                          | 774                                           | 6,135    |
| 2011                                      | 4,817                          | 624                                           | 5,441    |
| 2012                                      | 4,372                          | 500                                           | 4,872    |
| 2013                                      | 3,842                          | 400                                           | 4,242    |
| 2014                                      | 3,516                          | 324                                           | 3,840    |
| 2015                                      | 3,193                          | 262                                           | 3,455    |

**Note 6: Post Retirement Benefits**

The Company offers a continuation of group insurance coverage to qualifying employees electing early retirement, for the period from the date of retirement until age 65. For eligible employees the Company pays a portion of these early retirees' insurance premiums. The Company also reimburses a portion of Medicare Part B premiums for all qualifying retirees over age 65 and their qualified spouses. Eligibility for post-retirement medical benefits is based on age and years of service, and restricted to employees hired prior to February 1, 2006. The Company uses an actuarial-based accrual method of accounting for post-retirement benefits.

The following table sets forth the net periodic post-retirement benefit costs:

|                                                    | For the six months ended<br>June 30, |          |
|----------------------------------------------------|--------------------------------------|----------|
|                                                    | 2010                                 | 2009     |
|                                                    | (In thousands)                       |          |
| Service cost (benefit)                             | \$ (180)                             | \$ (158) |
| Interest cost                                      | 96                                   | 110      |
| Amortization of unrecognized transition obligation | 30                                   | 30       |
| Net periodic cost (benefit)                        | \$ (54)                              | \$ (18)  |

The Company does not fund plan assets for any post-retirement benefit plans.

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**Table of Contents****Note 7: Commitments and Contingent Liabilities**

Loan commitments are agreements to lend to a customer provided there is no violation of any condition established in the agreement. Commitments generally have fixed expiration dates or other termination clauses. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future funding requirements. Loan commitments are subject to the Company's normal credit policies and collateral requirements. Unfunded loan commitments were \$407.9 million and \$482.0 million at June 30, 2010 and December 31, 2009, respectively. Standby letters of credit commit the Company to make payments on behalf of customers when certain specified future events occur. Standby letters of credit are primarily issued to support customers' short-term financing requirements and must meet the Company's normal credit policies and collateral requirements. Standby letters of credit outstanding totaled \$25.2 million and \$27.4 million at June 30, 2010 and December 31, 2009, respectively. The Company also had commitments for commercial and similar letters of credit of \$2.0 million and \$176 thousand at June 30, 2010 and December 31, 2009, respectively.

Due to the nature of its business, the Company is subject to various threatened or filed legal cases. Based on the advice of legal counsel, the Company does not expect such cases will have a material, adverse effect on its financial position or results of operations. Legal costs related to covered assets are 80 percent indemnified under loss-sharing agreements with the FDIC if certain conditions are met.

**Note 8: Fair Value Measurements**

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Available for sale investment securities are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as certain loans held for investment and other assets. These nonrecurring fair value adjustments typically involve the lower-of-cost-or-fair value accounting or impairment or write-down of individual assets.

In accordance with the Fair Value Measurement and Disclosure topic of the Codification, the Company bases its fair values on the price that would be received to sell an asset or paid to transfer a liability in the principal market or most advantageous market for an asset or liability in an orderly transaction between market participants on the measurement date. A fair value measurement reflects all of the assumptions that market participants would use in pricing the asset or liability, including assumptions about the risk inherent in a particular valuation technique, the effect of a restriction on the sale or use of an asset, and the risk of nonperformance.

The Company groups its assets and liabilities measured at fair value into a three-level hierarchy, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

**Level 1** Valuation is based upon quoted prices for identical instruments traded in active exchange markets, such as the New York Stock Exchange. Level 1 includes U.S. Treasury and federal agency securities, which are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

**Level 2** Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market. Level 2 includes mortgage-backed securities, municipal bonds and collateralized mortgage obligations as well as other real estate owned and impaired loans collateralized by real property where the fair value is generally based upon independent market prices or appraised values of the collateral.

**Level 3** Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company's estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques. Level 3 includes those impaired loans collateralized by other business assets where the expected cash flow has been used in determining the fair value.





**Table of Contents****Assets Recorded at Fair Value on a Recurring Basis**

The table below presents assets measured at fair value on a recurring basis.

|                                                                | Fair Value | At June 30, 2010                                                              |                                                           |                                                    |
|----------------------------------------------------------------|------------|-------------------------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|
|                                                                |            | Quoted Prices<br>in Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| (In thousands)                                                 |            |                                                                               |                                                           |                                                    |
| U.S. Treasury securities                                       | \$ 2,997   | \$ 2,997                                                                      | \$                                                        | \$                                                 |
| Securities of U.S. Government sponsored entities               | 72,407     | 72,407                                                                        |                                                           |                                                    |
| Municipal bonds:                                               |            |                                                                               |                                                           |                                                    |
| Federally Tax-exempt California                                | 76,294     |                                                                               | 76,294                                                    |                                                    |
| Federally Tax-exempt 27 other states                           | 106,976    |                                                                               | 106,976                                                   |                                                    |
| Taxable California                                             | 4,817      |                                                                               | 4,817                                                     |                                                    |
| Taxable 1 other state                                          | 500        |                                                                               | 500                                                       |                                                    |
| Residential mortgage-backed securities ( MBS ):                |            |                                                                               |                                                           |                                                    |
| Guaranteed by GNMA                                             | 50,235     |                                                                               | 50,235                                                    |                                                    |
| Issued by FNMA and FHLMC                                       | 78,647     |                                                                               | 78,647                                                    |                                                    |
| Residential collateralized mortgage obligations:               |            |                                                                               |                                                           |                                                    |
| Issued or guaranteed by FNMA, FHLMC, or<br>GNMA                | 19,386     |                                                                               | 19,386                                                    |                                                    |
| All other                                                      | 10,124     |                                                                               | 10,124                                                    |                                                    |
| Commercial mortgage-backed securities                          | 5,255      |                                                                               | 5,255                                                     |                                                    |
| Asset-backed securities government guaranteed<br>student loans | 8,529      |                                                                               | 8,529                                                     |                                                    |
| FHLMC and FNMA stock                                           | 789        | 789                                                                           |                                                           |                                                    |
| Corporate securities                                           | 24,284     | 24,284                                                                        |                                                           |                                                    |
| Other securities                                               | 5,260      | 3,274                                                                         | 1,986                                                     |                                                    |
| Total securities available for sale                            | \$ 466,500 | \$ 103,751                                                                    | \$ 362,749                                                | \$                                                 |

|                                                  | Fair Value | At December 31, 2009                                                             |                                                           |                                                    |
|--------------------------------------------------|------------|----------------------------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|
|                                                  |            | Quoted<br>Prices<br>in Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| (In thousands)                                   |            |                                                                                  |                                                           |                                                    |
| U.S. Treasury securities                         | \$ 2,987   | \$ 2,987                                                                         | \$                                                        | \$                                                 |
| Securities of U.S. Government sponsored entities | 21,041     | 21,041                                                                           |                                                           |                                                    |
| Municipal bonds:                                 |            |                                                                                  |                                                           |                                                    |
| Federally Tax-exempt California                  | 56,431     |                                                                                  | 56,431                                                    |                                                    |
| Federally Tax-exempt 25 other states             | 97,094     |                                                                                  | 97,094                                                    |                                                    |

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|                                                  |            |           |            |
|--------------------------------------------------|------------|-----------|------------|
| Taxable California                               | 4,668      |           | 4,668      |
| Residential mortgage-backed securities ( MBS ):  |            |           |            |
| Guaranteed by GNMA                               | 54,361     |           | 54,361     |
| Issued by FNMA and FHLMC                         | 91,644     |           | 91,644     |
| Residential collateralized mortgage obligations: |            |           |            |
| Issued or guaranteed by FNMA, FHLMC, or          |            |           |            |
| GNMA                                             | 29,536     |           | 29,536     |
| All other                                        | 11,874     |           | 11,874     |
| Asset-backed securities government guaranteed    |            |           |            |
| student loans                                    | 8,339      |           | 8,339      |
| FHLMC and FNMA stock                             | 1,573      | 1,573     |            |
| Other securities                                 | 4,660      | 2,703     | 1,957      |
| Total securities available for sale              | \$ 384,208 | \$ 28,304 | \$ 355,904 |

There were no significant transfers in or out of Levels 1 and 2 for the six months ended June 30, 2010.

**Table of Contents****Assets Recorded at Fair Value on a Nonrecurring Basis**

The Company may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with GAAP. These adjustments to fair value usually result from application of lower-of-cost-or-market accounting or write-downs of individual assets. For assets measured at fair value on a nonrecurring basis during the first six months ended June 30, 2010 and year ended December 31, 2009 that were still held in the balance sheet at the end of such periods, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related assets at the dates indicated.

|                                                             | At June 30, 2010 |         |         |         | Total losses |
|-------------------------------------------------------------|------------------|---------|---------|---------|--------------|
|                                                             | Fair Value       | Level 1 | Level 2 | Level 3 |              |
|                                                             | (In thousands)   |         |         |         |              |
| Non-covered other real estate owned (1)                     | \$ 180           | \$      | \$ 180  | \$      | \$ (466)     |
| Non-covered impaired loans (2)                              | 500              |         |         | 500     | (530)        |
| Total assets measured at fair value on a nonrecurring basis | \$ 680           | \$      | \$ 180  | \$ 500  | \$ (996)     |

|                                                             | At December 31, 2009 |         |          |         | Total losses |
|-------------------------------------------------------------|----------------------|---------|----------|---------|--------------|
|                                                             | Fair Value           | Level 1 | Level 2  | Level 3 |              |
|                                                             | (In thousands)       |         |          |         |              |
| Non-covered other real estate owned (1)                     | \$ 413               | \$      | \$ 413   | \$      | \$ (233)     |
| Non-covered impaired loans (2)                              | 2,447                |         | 2,447    |         |              |
| Total assets measured at fair value on a nonrecurring basis | \$ 2,860             | \$      | \$ 2,860 | \$      | \$ (233)     |

(1) Represents the fair value of foreclosed real estate owned that was measured at fair value subsequent to their initial classification as foreclosed assets.

(2) Represents carrying value of loans for which adjustments are predominantly

based on the  
appraised value  
of the collateral  
and loans  
considered  
impaired under  
FASB ASC  
310-10-35,  
Subsequent  
Measurement of  
Receivables,  
where a specific  
reserve has been  
established.

**Disclosures about Fair Value of Financial Instruments**

The following section describes the valuation methodologies used by the Company for estimating fair value of financial instruments not recorded at fair value.

**Cash and Due from Banks** The carrying amount of cash and amounts due from banks approximate fair value due to the relatively short period of time between their origination and their expected realization.

**Money Market Assets** The carrying amount of money market assets approximate fair value due to the relatively short period of time between their origination and their expected realization.

**Investment Securities Held to Maturity** The fair values of investment securities were estimated using quoted prices as described above for Level 1 and Level 2 valuation.

**Loans** Loans were separated into two groups for valuation. Variable rate loans, except for those described below, which reprice frequently with changes in market rates were valued using historical cost. Fixed rate loans and variable rate loans that have reached their minimum contractual interest rates were valued by discounting the future cash flows expected to be received from the loans using current interest rates charged on loans with similar characteristics. Additionally, the allowance for loan losses of \$39.7 million at June 30, 2010 and \$41.0 million at December 31, 2009 and the fair value discount due to credit default risk associated with purchased loans of \$75.5 million at June 30, 2010 and \$93.3 million at December 31, 2009 were applied against the estimated fair values to recognize estimated future defaults of contractual cash flows. The Company does not consider these values to be a liquidation price for the loans.

**FDIC Receivable** The fair value of the FDIC receivable recorded in Other Assets was estimated by discounting estimated future cash flows using current market rates for financial instruments with similar characteristics.

**Deposit Liabilities** The carrying amount of demand deposits, savings accounts and money market accounts approximates fair value due to the relatively short period of time between their origination and their expected realization. The fair values of the time deposits were estimated by discounting estimated future cash flows related to these financial instruments using current market rates for financial instruments with similar characteristics.

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**Short-Term Borrowed Funds** The carrying amount of securities sold under agreement to repurchase and other short-term borrowed funds approximate fair value due to the relatively short period of time between their origination and their expected realization. The fair values of term repurchase agreements were estimated by using interpolated yields for financial instruments with similar characteristics.

**Federal Home Loan Bank Advances** The fair values of FHLB advances were estimated by using interpolated yields for financial instruments with similar characteristics.

**Debt Financing and Notes Payable** The fair values of debt financing and notes payable were estimated by using interpolated yields for financial instruments with similar characteristics.

**Restricted Performance Share Grants** The fair value of liabilities for unvested restricted performance share grants recorded in Other Liabilities were estimated using quoted prices as described above for Level 1 valuation.

The table below is a summary of fair value estimates for financial instruments, excluding financial instruments recorded at fair value on a recurring basis. The values assigned do not necessarily represent amounts which ultimately may be realized. In addition, these values do not give effect to discounts to fair value which may occur when financial instruments are sold in larger quantities. The carrying amounts in the following table are recorded in the balance sheet under the indicated captions.

The Company has not included assets and liabilities that are not financial instruments, such as goodwill, long-term relationships with deposit, merchant processing and trust customers, other purchased intangibles, premises and equipment, deferred taxes and other assets and liabilities. The total estimated fair values do not represent, and should not be construed to represent, the underlying value of the Company.

|                                                       | At June 30, 2010 |                      | At December 31, 2009 |                      |
|-------------------------------------------------------|------------------|----------------------|----------------------|----------------------|
|                                                       | Carrying Amount  | Estimated Fair Value | Carrying Amount      | Estimated Fair Value |
|                                                       | (In thousands)   |                      |                      |                      |
| <b>Financial Assets</b>                               |                  |                      |                      |                      |
| Cash and due from banks                               | \$ 294,240       | \$ 294,240           | \$ 361,135           | \$ 361,135           |
| Money market assets                                   | 342              | 342                  | 442                  | 442                  |
| Investment securities held to maturity                | 652,658          | 669,319              | 726,935              | 736,270              |
| Loans                                                 | 2,848,473        | 2,857,783            | 3,015,346            | 3,024,866            |
| Other assets FDIC receivable                          | 55,945           | 55,386               | 85,787               | 83,806               |
| <b>Financial Liabilities</b>                          |                  |                      |                      |                      |
| Deposits                                              | 3,890,560        | 3,891,086            | 4,060,208            | 4,061,380            |
| Short-term borrowed funds                             | 210,503          | 210,642              | 227,178              | 228,463              |
| Federal Home Loan Bank Advances                       | 10,223           | 10,330               | 85,470               | 85,601               |
| Debt financing and notes payable                      | 26,430           | 26,265               | 26,497               | 23,520               |
| Other liabilities restricted performance share grants | 1,829            | 1,829                | 1,942                | 1,942                |

The majority of the Company's standby letters of credit and other commitments to extend credit carry current market interest rates if converted to loans. No premium or discount was ascribed to these commitments because virtually all funding would be at current market rates.

**Note 9: Shareholders' Equity**

On February 13, 2009, the Company issued to the United States Department of the Treasury (the "Treasury") 83,726 shares of Series A Fixed Rate Cumulative Perpetual Preferred Stock (the "Series A Preferred Stock"), having a liquidation preference of \$1,000 per share. The structure of the Series A Preferred Stock included cumulative dividends at a rate of 5% per year for the first five years and thereafter at a rate of 9% per year. On September 2, 2009 and November 18, 2009, the Company redeemed 41,863 shares and 41,863 shares, respectively, of its Series A Preferred Stock at \$1,000 per share. Prior to redemption, under the terms of the Series A Preferred Stock, the Company could not declare or pay any dividends or make any distribution on its common stock, other than regular

quarterly cash dividends not exceeding \$0.35 or dividends payable only in shares of its common stock, or repurchase its common stock or other equity or capital securities, other than in connection with benefit plans consistent with past practice and certain other circumstances specified in the Securities Purchase Agreement with the Treasury. The Treasury, as part of the preferred stock issuance, received a warrant to purchase 246,640 shares of the Company's common stock at an exercise price of \$50.92. The proceeds from Treasury were allocated based on the relative fair value of the warrant as compared with the fair value of the preferred stock. The fair value of the warrant was determined using a valuation model which incorporates assumptions including the Company's common stock price, dividend yield, stock price volatility, the risk-free interest rate, and other assumptions. The Company allocated \$1.2 million of the proceeds from the Series A Preferred Stock to the warrant. The discount on the preferred stock was accreted to par value during the period the Series A Preferred Stock was outstanding, and reported as a reduction to net income applicable to common equity over that period.

**Table of Contents****Note 10: Earnings Per Common Share**

The table below shows earnings per common share and diluted earnings per common share. Basic earnings per common share are computed by dividing net income applicable to common equity by the average number of common shares outstanding during the period. Diluted earnings per common share are computed by dividing net income applicable to common equity by the average number of common shares outstanding during the period plus the impact of common stock equivalents.

|                                                                                                                                 | For the three months ended<br>June 30, |           | For the six months ended<br>June 30, |           |
|---------------------------------------------------------------------------------------------------------------------------------|----------------------------------------|-----------|--------------------------------------|-----------|
|                                                                                                                                 | 2010                                   | 2009      | 2010                                 | 2009      |
|                                                                                                                                 | (In thousands, except per share data)  |           |                                      |           |
| Weighted average number of common shares<br>outstanding basic                                                                   | 29,207                                 | 29,126    | 29,217                               | 29,002    |
| Add exercise of options reduced by the number of<br>shares that could have been purchased with the<br>proceeds of such exercise | 361                                    | 277       | 365                                  | 252       |
| Weighted average number of common shares<br>outstanding diluted                                                                 | 29,568                                 | 29,403    | 29,582                               | 29,254    |
| Net income applicable to common equity                                                                                          | \$ 23,561                              | \$ 22,076 | \$ 47,137                            | \$ 74,323 |
| Basic earnings per common share                                                                                                 | \$ 0.81                                | \$ 0.76   | \$ 1.61                              | \$ 2.56   |
| Diluted earnings per common share                                                                                               | 0.80                                   | 0.75      | 1.59                                 | 2.54      |

For the three months and six months ended June 30, 2010, options to purchase 287 thousand and 290 thousand shares of common stock, respectively, were outstanding but not included in the computation of diluted net income per share because the option exercise price exceeded the fair value of the stock such that their inclusion would have had an anti-dilutive effect. For the three and six months ended June 30, 2009, options and warrants to purchase 733 thousand and 1.2 million shares of common stock, respectively, were outstanding but not included in the computation of diluted net income per share because the option exercise price exceeded the fair value of the stock such that their inclusion would have had an anti-dilutive effect.

**Table of Contents****WESTAMERICA BANCORPORATION  
FINANCIAL SUMMARY**

|                                                    | Three months ended<br>June 30,        |              | Six months ended<br>June 30, |              |
|----------------------------------------------------|---------------------------------------|--------------|------------------------------|--------------|
|                                                    | 2010                                  | 2009         | 2010                         | 2009         |
|                                                    | (In thousands, except per share data) |              |                              |              |
| <b>Net Interest Income (FTE)*</b>                  | \$ 56,573                             | \$ 62,318    | \$ 113,602                   | \$ 121,677   |
| <b>Provision for Loan Losses</b>                   | 2,800                                 | 2,600        | 5,600                        | 4,400        |
| <b>Noninterest Income:</b>                         |                                       |              |                              |              |
| Gain on acquisition                                |                                       |              |                              | 48,844       |
| Deposit service charges and other                  | 15,770                                | 16,386       | 31,240                       | 31,510       |
| <b>Total Noninterest Income</b>                    | 15,770                                | 16,386       | 31,240                       | 80,354       |
| <b>Noninterest Expense</b>                         | 32,095                                | 38,666       | 64,126                       | 72,789       |
| <b>Income Before Income Taxes (FTE)*</b>           | 37,448                                | 37,438       | 75,116                       | 124,842      |
| <b>Income Tax Provision (FTE)*</b>                 | 13,887                                | 14,255       | 27,979                       | 48,834       |
| <b>Net Income</b>                                  | 23,561                                | 23,183       | 47,137                       | 76,008       |
| Preferred stock dividends and discount accretion   |                                       | 1,107        |                              | 1,685        |
| <b>Net Income Applicable to Common Equity</b>      | \$ 23,561                             | \$ 22,076    | \$ 47,137                    | \$ 74,323    |
| <b>Average Common Shares Outstanding</b>           | 29,207                                | 29,126       | 29,217                       | 29,002       |
| <b>Diluted Average Common Shares Outstanding</b>   | 29,568                                | 29,403       | 29,582                       | 29,254       |
| <b>Common Shares Outstanding at Period End</b>     | 29,118                                | 29,214       | 29,118                       | 29,214       |
| <b>As Reported:</b>                                |                                       |              |                              |              |
| Basic Earnings Per Common Share                    | \$ 0.81                               | \$ 0.76      | \$ 1.61                      | \$ 2.56      |
| Diluted Earnings Per Common Share                  | 0.80                                  | 0.75         | 1.59                         | 2.54         |
| Return On Assets                                   | 2.00%                                 | 1.68%        | 1.99%                        | 2.92%        |
| Return On Common Equity                            | 18.24%                                | 19.03%       | 18.54%                       | 33.06%       |
| Net Interest Margin (FTE)*                         | 5.62%                                 | 5.34%        | 5.61%                        | 5.35%        |
| Net Loan Losses to Average Gross Non-Covered Loans | 0.64%                                 | 0.56%        | 0.65%                        | 0.49%        |
| Efficiency Ratio**                                 | 44.4%                                 | 49.1%        | 44.3%                        | 36.0%        |
| <b>Average Balances:</b>                           |                                       |              |                              |              |
| Total Assets                                       | \$ 4,731,270                          | \$ 5,265,101 | \$ 4,771,872                 | \$ 5,133,941 |
| Earning Assets                                     | 4,033,831                             | 4,678,615    | 4,072,374                    | 4,577,554    |
| Non-covered Loans                                  | 2,136,407                             | 2,338,294    | 2,150,857                    | 2,356,288    |
| Covered Loans                                      | 788,108                               | 1,045,360    | 809,515                      | 904,195      |
| Total Deposits                                     | 3,895,671                             | 4,202,607    | 3,925,321                    | 4,033,461    |
| Shareholders Equity                                | 518,128                               | 547,816      | 512,796                      | 516,608      |



**Balances at Period End:**

|                      |              |              |
|----------------------|--------------|--------------|
| Total Assets         | \$ 4,727,086 | \$ 5,193,595 |
| Earning Assets       | 4,007,989    | 4,591,907    |
| Non-covered Loans    | 2,124,570    | 2,322,005    |
| Covered Loans        | 763,619      | 1,031,643    |
| Total Deposits       | 3,890,560    | 4,157,137    |
| Shareholders' Equity | 527,681      | 559,231      |

**Financial Ratios at Period End:**

|                                                |          |          |
|------------------------------------------------|----------|----------|
| Allowance for Loan Losses to Non-Covered Loans | 1.87%    | 1.86%    |
| Book Value Per Common Share                    | \$ 18.12 | \$ 16.31 |
| Equity to Assets                               | 11.16%   | 10.77%   |
| Total Capital to Risk Adjusted Assets          | 15.72%   | 15.85%   |

|                                        |         |         |         |         |
|----------------------------------------|---------|---------|---------|---------|
| <b>Dividends Paid Per Common Share</b> | \$ 0.36 | \$ 0.35 | \$ 0.72 | \$ 0.71 |
| <b>Common Dividend Payout Ratio</b>    | 45%     | 47%     | 45%     | 28%     |

The above financial summary has been derived from the Company's unaudited consolidated financial statements. This information should be read in conjunction with those statements, notes and the other information included elsewhere herein. Percentages under the heading "As Reported" are annualized with the exception of the efficiency ratio.

\* Yields on securities and certain loans have been adjusted upward to a fully taxable equivalent (FTE) basis, which is a non-GAAP financial measure, in order to reflect the effect of income which is exempt from federal income taxation at the current statutory tax rate.

\*\* The efficiency ratio is defined as noninterest expense divided by total revenue (net interest income on an FTE basis,

which is a non-GAAP financial measure, and noninterest income).

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**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

Westamerica Bancorporation and subsidiaries (the Company) reported second quarter 2010 net income applicable to common equity of \$23.6 million or \$0.80 diluted earnings per common share. These results compare to net income applicable to common equity of \$22.1 million or \$0.75 diluted earnings per common share for the same period of 2009.

The Company reported net income applicable to common equity of \$47.1 million or \$1.59 diluted earnings per common share for the six months ended June 30, 2010, compared with \$74.3 million or \$2.54 diluted earnings per common share for the same period of 2009. The first half of 2009 included a \$48.8 million gain on the acquisition of County Bank (County) which increased net income by \$28.3 million and earnings per diluted common share by \$0.98.

**Net Income**

Following is a summary of the components of net income for the periods indicated:

|                                                                                            | Three months ended<br>June 30,        |              | Six months ended<br>June 30, |              |
|--------------------------------------------------------------------------------------------|---------------------------------------|--------------|------------------------------|--------------|
|                                                                                            | 2010                                  | 2009         | 2010                         | 2009         |
|                                                                                            | (In thousands, except per share data) |              |                              |              |
| Net interest income (FTE)                                                                  | \$ 56,573                             | \$ 62,318    | \$ 113,602                   | \$ 121,677   |
| Provision for loan losses                                                                  | (2,800)                               | (2,600)      | (5,600)                      | (4,400)      |
| Noninterest income                                                                         | 15,770                                | 16,386       | 31,240                       | 80,354       |
| Noninterest expense                                                                        | (32,095)                              | (38,666)     | (64,126)                     | (72,789)     |
| Income before taxes (FTE)                                                                  | 37,448                                | 37,438       | 75,116                       | 124,842      |
| Income tax provision (FTE)                                                                 | (13,887)                              | (14,255)     | (27,979)                     | (48,834)     |
| Net income                                                                                 | \$ 23,561                             | \$ 23,183    | \$ 47,137                    | \$ 76,008    |
| Net income applicable to common equity                                                     | \$ 23,561                             | \$ 22,076    | \$ 47,137                    | \$ 74,323    |
| Average diluted common shares                                                              | 29,568                                | 29,403       | 29,582                       | 29,254       |
| Diluted earnings per common share                                                          | \$ 0.80                               | \$ 0.75      | \$ 1.59                      | \$ 2.54      |
| Average total assets                                                                       | \$ 4,731,270                          | \$ 5,265,101 | \$ 4,771,872                 | \$ 5,133,941 |
| Net income applicable to common equity to average total assets (annualized)                | 2.00%                                 | 1.68%        | 1.99%                        | 2.92%        |
| Net income applicable to common equity to average common stockholders' equity (annualized) | 18.24%                                | 19.03%       | 18.54%                       | 33.06%       |

Net income applicable to common equity for the second quarter of 2010 was \$1.5 million or 6.7% more than the same quarter of 2009, largely attributable to lower noninterest expense and income tax provision (FTE) and the elimination of preferred stock dividends and discount accretion, partially offset by lower net interest income (FTE), higher loan loss provision and lower noninterest income. A \$5.7 million or 9.2% decrease in net interest income (FTE) was mostly attributed to lower average balances of interest earning assets and lower yields on investments, partially offset by higher yields on loans, lower average balances of interest-bearing liabilities and lower rates paid on interest-bearing deposits. The provision for loan losses increased \$200 thousand, reflecting Management's evaluation of losses inherent in the loan portfolio not covered by loss-sharing agreements with the FDIC. Noninterest income decreased \$616 thousand mainly due to lower service charges on deposit accounts. Noninterest expense decreased \$6.6 million mostly due to lower personnel, occupancy and equipment expenses resulting from the systems integrations and branch consolidations following the County acquisition and lower FDIC insurance assessments. The provision for income

taxes (FTE) decreased \$368 thousand. Net income applicable to common equity in the second quarter of 2009 reflected \$1.1 million in preferred stock dividends and discount accretion.

Comparing the first half of 2010 to the first half of 2009, net income applicable to common equity decreased \$27.2 million, primarily due to a \$48.8 million gain on acquisition in the first half of 2009, lower net interest income (FTE) and higher provision for loan losses, partially offset by decreases in noninterest expense and income tax provision (FTE) and the elimination of preferred stock dividends and discount accretion. The lower net interest income (FTE) was primarily caused by a lower volume of average earning assets and lower yields on investments, partially offset by higher yields on loans, lower average balances of interest-bearing liabilities and lower rates paid on interest-bearing deposits. The provision for loan losses increased \$1.2 million, reflecting Management's evaluation of losses inherent in the loan portfolio not covered by loss-sharing agreements with the FDIC. Noninterest income decreased \$49.1 million largely due to a \$48.8 million acquisition gain in the first half of 2009. Noninterest expense declined \$8.7 million primarily due to decreases in personnel, occupancy and equipment expenses subsequent to integrating the acquired County Bank and lower FDIC insurance assessments. The income tax provision (FTE) decreased \$20.9 million. Net income applicable to common equity in the first half of 2009 reflected \$1.7 million in preferred stock dividends and discount accretion. The preferred stock was redeemed during the fourth quarter of 2009.

**Table of Contents****Net Interest Income**

Following is a summary of the components of net interest income for the periods indicated:

|                           | Three months ended<br>June 30, |           | Six months ended<br>June 30, |            |
|---------------------------|--------------------------------|-----------|------------------------------|------------|
|                           | 2010                           | 2009      | 2010                         | 2009       |
|                           | (In thousands)                 |           |                              |            |
| Interest and fee income   | \$ 55,078                      | \$ 63,072 | \$ 111,081                   | \$ 122,257 |
| Interest expense          | (3,145)                        | (5,745)   | (6,679)                      | (10,578)   |
| FTE adjustment            | 4,640                          | 4,991     | 9,200                        | 9,998      |
| Net interest income (FTE) | \$ 56,573                      | \$ 62,318 | \$ 113,602                   | \$ 121,677 |

|                                        |              |              |              |              |
|----------------------------------------|--------------|--------------|--------------|--------------|
| Average earning assets                 | \$ 4,033,831 | \$ 4,678,615 | \$ 4,072,374 | \$ 4,577,554 |
| Net interest margin (FTE) (annualized) | 5.62%        | 5.34%        | 5.61%        | 5.35%        |

Net interest income (FTE) decreased during the second quarter of 2010 by \$5.7 million or 9.2% from the same period in 2009 to \$56.6 million, mainly due to lower average balances of earning assets (down \$645 million), lower yields on investments (down 0.11%) and higher rates on short-term borrowings (up 0.17%), partially offset by higher yields on loans (up 0.18%), lower average balances of interest-bearing liabilities (down \$557 million) and lower rates paid on interest-bearing deposits (down 0.27%).

Comparing the first half of 2010 with the first half of 2009, net interest income (FTE) decreased \$8.1 million or 6.6%, primarily due to a lower volume of average earning assets (down \$505 million) and lower yields on investments (down 0.06%) and higher rates on short-term borrowings (up 0.4%), partially offset by higher yields on loans (up 0.2%), lower average balances of interest-bearing liabilities (down \$434 million) and lower rates paid on interest-bearing deposits (down 0.24%).

At June 30, 2010, FDIC covered loans represented 26 percent of the Company's loan portfolio. Under the terms of the FDIC loss-sharing agreements, the FDIC is obligated to reimburse the Bank 80 percent of loan interest income foregone on covered loans. Such reimbursements are limited to the lesser of 90 days contractual interest or actual unpaid contractual interest at the time a principal loss is recognized in respect to the underlying loan.

**Interest and Fee Income**

Interest and fee income (FTE) for the second quarter of 2010 decreased \$8.3 million or 12.3% from the same period in 2009. The decrease was caused by lower average balances of earning assets (down \$645 million) and lower yields on investments (down 0.11%), partially offset by higher yields on loans (up 0.18%). The total average balances of loans declined \$459 million or 13.6% due to decreases in the average balances of commercial real estate loans (down \$137 million), taxable commercial loans (down \$131 million), residential real estate loans (down \$82 million), direct consumer loans (down \$21 million), indirect auto loans (down \$49 million), construction loans (down \$20 million) and tax-exempt commercial loans (down \$19 million). The average investment portfolio decreased \$186 million largely due to declines in average balances of collateralized mortgage obligations (down \$92 million), residential mortgage backed securities (down \$56 million), and municipal securities (down \$54 million), partially offset by a \$12 million increase in the average balances of corporate and other securities. The average yield on the Company's earning assets increased from 5.83% in the second quarter of 2009 to 5.93% in the corresponding period of 2010. The composite yield on loans rose 0.18% to 6.18% due to increases in yields on construction loans (up 1.5%), taxable commercial loans (up 0.73%), tax-exempt commercial loans (up 0.26%) and commercial real estate loans (up 0.06%), partially offset by decreases in yields on residential real estate loans (down 0.3%) and indirect auto loans (down 0.02%). Nonperforming loans are included in average loan volumes used to compute loan yields; fluctuations in nonaccrual loan volumes impact loan yields. The investment portfolio yield decreased 0.11% to 5.28%, mainly due to declines in yields on U.S. government sponsored entity obligations (down 2.82%) and municipal securities (down 0.03%), partially offset by a 0.20% increase in yields on collateralized mortgage obligations.



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Comparing the first half of 2010 with the first half of 2009, interest and fee income (FTE) was down \$12.0 million or 9.1%. The decrease resulted from a lower volume of average earning assets and lower yields on investment securities, partially offset by higher yields on loans. Average earning assets decreased \$505 million or 11.0% in the first half of 2010 compared with the first half of 2009 due to a \$300 million decrease in average loans and a \$205 million decrease in average investments. The decrease in the average balance of the loan portfolio was mainly attributable to decreases in average balances of taxable commercial loans (down \$94 million), residential real estate loans (down \$82 million), indirect auto loans (down \$46 million), commercial real estate loans (down \$45 million), tax-exempt commercial loans (down \$19 million) and construction loans (down \$17 million). The average investment portfolio decreased \$205 million largely due to declines in average balances of collateralized mortgage obligations (down \$92 million), municipal securities (down \$52 million), U.S. government sponsored entity obligations (down \$41 million) and residential mortgage backed securities (down \$33 million), partially offset by a \$10 million increase in the average balances of corporate and other securities. The average yield on earning assets for the first half of 2010 was 5.94% compared with 5.82% in the first half of 2009. The loan portfolio yield for the first half of 2010 compared with the corresponding 2009 period was higher by 0.2%, due to increases in yields on construction loans (up 1.59%), taxable commercial loans (up 0.59%), commercial real estate loans (up 0.1%) and a 0.01% increase in yields on indirect auto loans, partially offset by a 0.25% decrease in yields on residential real estate loans. The investment portfolio yield decreased by 0.06%, reflecting lower yields on U.S. government sponsored entity obligations (down 2.8%), municipal securities (down 0.07%) and residential mortgage backed securities (down 0.02%), partially offset by a 0.17% increase in the yield on collateralized mortgage obligations.

**Interest Expense**

Interest expense in the second quarter of 2010 decreased \$2.6 million compared with the same period in 2009. The decrease was attributable to lower average balances of interest-bearing liabilities and lower rates paid on the interest-bearing deposits and, partially offset by higher rates paid on short-term borrowings. The average rate paid on interest-bearing liabilities decreased from 0.70% in the second quarter of 2009 to 0.46% in the same quarter of 2010. Rates on interest-bearing deposits decreased 0.27% to 0.35% primarily due to decreases in rates paid on time deposits less than \$100 thousand (down 0.53%), time deposits \$100 thousand or more (down 0.48%), preferred money market savings (down 0.13%), money market savings down 0.18%) and regular savings (down 0.14%). Rates on short-term borrowings increased 0.17% mostly due to a 0.69% increase in the rates on FHLB advances as FHLB advances maturing in January 2010 carried a lower rate than FHLB advances which remain outstanding. Average interest-bearing liabilities declined \$557 million. Interest-bearing deposits decreased \$358 million mostly due to decreases in the average balance of time deposits less than \$100 thousand (down \$180 million), time deposits \$100 thousand or more (down \$88 million), money market checking accounts (down \$76 million) and money market savings (down \$23 million). Average short-term borrowings declined \$199 million in the second quarter of 2010 over the same period of 2009 primarily due to declines in the average balances of federal funds purchased (down \$120 million) and FHLB advances (down \$76 million).

Comparing the first half of 2010 with the first half of 2009, interest expense declined \$3.9 million, due to lower average balances of interest-bearing liabilities and lower rates on interest-bearing deposits, offset by higher rates paid on short-term borrowings. Average interest-bearing liabilities during the first half of 2010 fell by \$434 million over the same period of 2009 mainly due to decreases in average balances of federal funds purchased (down \$217 million), FHLB advances (down \$55 million), time deposits \$100 thousand or more (down \$94 million), time deposits less than \$100 thousand (down \$83 million), money market checking accounts (down \$40 million), partially offset by increases in the average balance of repurchases facilities (up \$17 million), money market savings (up \$17 million) and regular savings (up \$16 million). Rates paid on liabilities averaged 0.48% during the first six months of 2010 compared with 0.66% for the first six months of 2009. The average rate paid on interest-bearing deposits declined 0.24% to 0.37% in the first half 2010 compared with the same period of 2009 mainly due to lower rates on time deposits less than \$100 thousand (down 0.68%), time deposits \$100 thousand or more (down 0.28%), preferred money market savings (down 0.14%), money market savings (down 0.14%) and regular savings (down 0.12%).





**Table of Contents****Net Interest Margin (FTE)**

The following summarizes the components of the Company's net interest margin for the periods indicated:

|                                               | Three months ended<br>June 30, |       | Six months ended<br>June 30, |       |
|-----------------------------------------------|--------------------------------|-------|------------------------------|-------|
|                                               | 2010                           | 2009  | 2010                         | 2009  |
| Yield on earning assets (FTE)                 | 5.93%                          | 5.83% | 5.94%                        | 5.82% |
| Rate paid on interest-bearing liabilities     | 0.46%                          | 0.70% | 0.48%                        | 0.66% |
| Net interest spread (FTE)                     | 5.47%                          | 5.13% | 5.46%                        | 5.16% |
| Impact of noninterest bearing demand deposits | 0.15%                          | 0.21% | 0.15%                        | 0.19% |
| Net interest margin (FTE)                     | 5.62%                          | 5.34% | 5.61%                        | 5.35% |

During the second quarter of 2010, the net interest margin (FTE) increased 0.28% compared with the same period in 2009. Higher yields on earning assets (FTE) and lower rates paid on interest-bearing liabilities resulted in a 0.34% increase in net interest spread. The increase in the net interest spread was partially reduced by the lower net interest margin contribution of noninterest-bearing demand deposits. The net interest margin (FTE) in the first six months of 2010 rose by 0.26% compared with the corresponding period of 2009. Earning asset yields increased 0.12% while the cost of interest-bearing liabilities declined by 0.18%, resulting in a 0.30% increase in the net interest spread. The 0.04% decrease in margin contribution from noninterest bearing funding sources resulted in the net interest margin of 5.61%.

**Table of Contents****Summary of Average Balances, Yields/Rates and Interest Differential**

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

|                                          | For the three months ended<br>June 30, 2010 |                                                  |                                    |
|------------------------------------------|---------------------------------------------|--------------------------------------------------|------------------------------------|
|                                          | Average<br>Balance                          | Interest<br>Income/<br>Expense<br>(In thousands) | Yields<br>Earned/<br>Rates<br>Paid |
| Assets:                                  |                                             |                                                  |                                    |
| Money market assets and funds sold       | \$ 703                                      | \$                                               | %                                  |
| Investment securities:                   |                                             |                                                  |                                    |
| Available for sale                       |                                             |                                                  |                                    |
| Taxable                                  | 266,180                                     | 2,156                                            | 3.24%                              |
| Tax-exempt (1)                           | 169,137                                     | 2,800                                            | 6.62%                              |
| Held to maturity                         |                                             |                                                  |                                    |
| Taxable                                  | 186,367                                     | 2,043                                            | 4.38%                              |
| Tax-exempt (1)                           | 486,929                                     | 7,636                                            | 6.27%                              |
| Loans:                                   |                                             |                                                  |                                    |
| Commercial:                              |                                             |                                                  |                                    |
| Taxable                                  | 545,959                                     | 8,511                                            | 6.25%                              |
| Tax-exempt (1)                           | 170,341                                     | 2,948                                            | 6.94%                              |
| Commercial real estate                   | 1,224,442                                   | 20,240                                           | 6.63%                              |
| Real estate construction                 | 57,514                                      | 843                                              | 5.88%                              |
| Real estate residential                  | 358,887                                     | 4,016                                            | 4.48%                              |
| Consumer                                 | 567,372                                     | 8,525                                            | 6.03%                              |
| Total loans (1)                          | 2,924,515                                   | 45,083                                           | 6.18%                              |
| Total earning assets (1)                 | 4,033,831                                   | \$ 59,718                                        | 5.93%                              |
| Other assets                             | 697,439                                     |                                                  |                                    |
| Total assets                             | \$ 4,731,270                                |                                                  |                                    |
| Liabilities and shareholders' equity     |                                             |                                                  |                                    |
| Deposits:                                |                                             |                                                  |                                    |
| Noninterest bearing demand               | \$ 1,384,249                                | \$                                               | %                                  |
| Savings and interest-bearing transaction | 1,619,319                                   | 877                                              | 0.22%                              |
| Time less than \$100,000                 | 350,890                                     | 449                                              | 0.51%                              |
| Time \$100,000 or more                   | 541,213                                     | 854                                              | 0.63%                              |

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|                                                 |              |           |       |
|-------------------------------------------------|--------------|-----------|-------|
| Total interest-bearing deposits                 | 2,511,422    | 2,180     | 0.35% |
| Short-term borrowed funds                       | 216,586      | 543       | 1.00% |
| Debt financing and notes payable                | 26,450       | 422       | 6.38% |
| Total interest-bearing liabilities              | 2,754,458    | \$ 3,145  | 0.46% |
| Other liabilities                               | 74,435       |           |       |
| Shareholders' equity                            | 518,128      |           |       |
| Total liabilities and shareholders' equity      | \$ 4,731,270 |           |       |
| Net interest spread (1) (2)                     |              |           | 5.47% |
| Net interest income and interest margin (1) (3) |              | \$ 56,573 | 5.62% |

(1) Interest and rates calculated on a fully taxable equivalent basis using the current statutory federal tax rate.

(2) Net interest spread represents the average yield earned on earning assets minus the average rate paid on interest-bearing liabilities.

(3) Net interest margin is computed by calculating the difference between interest income and expense (annualized), divided by the average balance of earning

assets.

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|                                          | For the three months ended<br>June 30, 2009 |                                                  |                          |
|------------------------------------------|---------------------------------------------|--------------------------------------------------|--------------------------|
|                                          | Average<br>Balance                          | Interest<br>Income/<br>Expense<br>(In thousands) | Rates<br>Earned/<br>Paid |
| Assets:                                  |                                             |                                                  |                          |
| Money market assets and funds sold       | \$ 1,349                                    | \$ 1                                             | 0.30%                    |
| Investment securities:                   |                                             |                                                  |                          |
| Available for sale                       |                                             |                                                  |                          |
| Taxable                                  | 259,331                                     | 2,556                                            | 3.94%                    |
| Tax-exempt (1)                           | 173,734                                     | 2,937                                            | 6.76%                    |
| Held to maturity                         |                                             |                                                  |                          |
| Taxable                                  | 325,154                                     | 3,569                                            | 4.39%                    |
| Tax-exempt (1)                           | 535,393                                     | 8,389                                            | 6.27%                    |
| Loans:                                   |                                             |                                                  |                          |
| Commercial:                              |                                             |                                                  |                          |
| Taxable                                  | 677,176                                     | 9,325                                            | 5.52%                    |
| Tax-exempt (1)                           | 189,521                                     | 3,155                                            | 6.68%                    |
| Commercial real estate                   | 1,361,420                                   | 22,316                                           | 6.57%                    |
| Real estate construction                 | 77,560                                      | 847                                              | 4.38%                    |
| Real estate residential                  | 440,929                                     | 5,271                                            | 4.78%                    |
| Consumer                                 | 637,048                                     | 9,697                                            | 6.11%                    |
| Total loans (1)                          | 3,383,654                                   | 50,611                                           | 6.00%                    |
| Total earning assets (1)                 | 4,678,615                                   | \$ 68,063                                        | 5.83%                    |
| Other assets                             | 586,486                                     |                                                  |                          |
| Total assets                             | \$ 5,265,101                                |                                                  |                          |
| Liabilities and shareholders' equity     |                                             |                                                  |                          |
| Deposits:                                |                                             |                                                  |                          |
| Noninterest bearing demand               | \$ 1,333,412                                | \$                                               | %                        |
| Savings and interest-bearing transaction | 1,709,132                                   | 1,352                                            | 0.32%                    |
| Time less than \$100,000                 | 530,417                                     | 1,381                                            | 1.04%                    |
| Time \$100,000 or more                   | 629,646                                     | 1,735                                            | 1.11%                    |
| Total interest-bearing deposits          | 2,869,195                                   | 4,468                                            | 0.62%                    |
| Short-term borrowed funds                | 415,871                                     | 856                                              | 0.83%                    |
| Debt financing and notes payable         | 26,584                                      | 421                                              | 6.35%                    |
| Total interest-bearing liabilities       | 3,311,650                                   | \$ 5,745                                         | 0.70%                    |
| Other liabilities                        | 72,223                                      |                                                  |                          |
| Shareholders' equity                     | 547,816                                     |                                                  |                          |

|                                                 |              |       |
|-------------------------------------------------|--------------|-------|
| Total liabilities and shareholders' equity      | \$ 5,265,101 |       |
| Net interest spread (1) (2)                     |              | 5.13% |
| Net interest income and interest margin (1) (3) | \$ 62,318    | 5.34% |

(1) Interest and rates calculated on a fully taxable equivalent basis using the current statutory federal tax rate.

(2) Net interest spread represents the average yield earned on earning assets minus the average rate paid on interest-bearing liabilities.

(3) Net interest margin is computed by calculating the difference between interest income and expense (annualized), divided by the average balance of earning assets.

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|                                          | For the six months ended<br>June 30, 2010 |                                                  |                          |
|------------------------------------------|-------------------------------------------|--------------------------------------------------|--------------------------|
|                                          | Average<br>Balance                        | Interest<br>Income/<br>Expense<br>(In thousands) | Rates<br>Earned/<br>Paid |
| Assets:                                  |                                           |                                                  |                          |
| Money market assets and funds sold       | \$ 672                                    | \$ 1                                             | 0.30%                    |
| Investment securities:                   |                                           |                                                  |                          |
| Available for sale                       |                                           |                                                  |                          |
| Taxable                                  | 256,874                                   | 4,307                                            | 3.35%                    |
| Tax-exempt (1)                           | 162,846                                   | 5,404                                            | 6.64%                    |
| Held to maturity                         |                                           |                                                  |                          |
| Taxable                                  | 196,350                                   | 4,321                                            | 4.40%                    |
| Tax-exempt (1)                           | 495,260                                   | 15,541                                           | 6.28%                    |
| Loans:                                   |                                           |                                                  |                          |
| Commercial:                              |                                           |                                                  |                          |
| Taxable                                  | 550,923                                   | 17,127                                           | 6.27%                    |
| Tax-exempt (1)                           | 171,588                                   | 5,612                                            | 6.60%                    |
| Commercial real estate                   | 1,231,354                                 | 40,534                                           | 6.64%                    |
| Real estate construction                 | 62,459                                    | 1,769                                            | 5.71%                    |
| Real estate residential                  | 367,523                                   | 8,360                                            | 4.55%                    |
| Consumer                                 | 576,525                                   | 17,305                                           | 6.05%                    |
| Total loans (1)                          | 2,960,372                                 | 90,707                                           | 6.18%                    |
| Total earning assets (1)                 | 4,072,374                                 | \$ 120,281                                       | 5.94%                    |
| Other assets                             | 699,498                                   |                                                  |                          |
| Total assets                             | \$ 4,771,872                              |                                                  |                          |
| Liabilities and shareholders' equity     |                                           |                                                  |                          |
| Deposits:                                |                                           |                                                  |                          |
| Noninterest bearing demand               | \$ 1,382,036                              | \$                                               | %                        |
| Savings and interest-bearing transaction | 1,624,137                                 | 1,833                                            | 0.23%                    |
| Time less than \$100,000                 | 370,611                                   | 1,066                                            | 0.58%                    |
| Time \$100,000 or more                   | 548,537                                   | 1,769                                            | 0.65%                    |
| Total interest-bearing deposits          | 2,543,285                                 | 4,668                                            | 0.37%                    |
| Short-term borrowed funds                | 230,295                                   | 1,164                                            | 1.02%                    |
| Debt financing and notes payable         | 26,467                                    | 847                                              | 6.40%                    |
| Total interest-bearing liabilities       | 2,800,047                                 | \$ 6,679                                         | 0.48%                    |
| Other liabilities                        | 76,993                                    |                                                  |                          |
| Shareholders' equity                     | 512,796                                   |                                                  |                          |

|                                                 |              |       |
|-------------------------------------------------|--------------|-------|
| Total liabilities and shareholders' equity      | \$ 4,771,872 |       |
| Net interest spread (1) (2)                     |              | 5.46% |
| Net interest income and interest margin (1) (3) | \$ 113,602   | 5.61% |

(1) Interest and rates calculated on a fully taxable equivalent basis using the current statutory federal tax rate.

(2) Net interest spread represents the average yield earned on earning assets minus the average rate paid on interest-bearing liabilities.

(3) Net interest margin is computed by calculating the difference between interest income and expense (annualized), divided by the average balance of earning assets.



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|                                          | For the six months ended<br>June 30, 2009 |                                                  |                          |
|------------------------------------------|-------------------------------------------|--------------------------------------------------|--------------------------|
|                                          | Average<br>Balance                        | Interest<br>Income/<br>Expense<br>(In thousands) | Rates<br>Earned/<br>Paid |
| Assets:                                  |                                           |                                                  |                          |
| Money market assets and funds sold       | \$ 1,116                                  | \$ 2                                             | 0.36%                    |
| Investment securities:                   |                                           |                                                  |                          |
| Available for sale                       |                                           |                                                  |                          |
| Taxable                                  | 244,400                                   | 4,423                                            | 3.62%                    |
| Tax-exempt (1)                           | 172,136                                   | 5,745                                            | 6.67%                    |
| Held to maturity                         |                                           |                                                  |                          |
| Taxable                                  | 361,156                                   | 8,359                                            | 4.63%                    |
| Tax-exempt (1)                           | 538,263                                   | 16,928                                           | 6.29%                    |
| Loans:                                   |                                           |                                                  |                          |
| Commercial:                              |                                           |                                                  |                          |
| Taxable                                  | 644,993                                   | 18,174                                           | 5.68%                    |
| Tax-exempt (1)                           | 190,728                                   | 6,319                                            | 6.68%                    |
| Commercial real estate                   | 1,276,810                                 | 41,388                                           | 6.54%                    |
| Real estate construction                 | 79,186                                    | 1,619                                            | 4.12%                    |
| Real estate residential                  | 449,507                                   | 10,798                                           | 4.80%                    |
| Consumer                                 | 619,259                                   | 18,500                                           | 6.02%                    |
| Total loans (1)                          | 3,260,483                                 | 96,798                                           | 5.98%                    |
| Total earning assets (1)                 | 4,577,554                                 | \$ 132,255                                       | 5.82%                    |
| Other assets                             | 556,387                                   |                                                  |                          |
| Total assets                             | \$ 5,133,941                              |                                                  |                          |
| Liabilities and shareholders' equity     |                                           |                                                  |                          |
| Deposits:                                |                                           |                                                  |                          |
| Noninterest bearing demand               | \$ 1,309,844                              | \$                                               | %                        |
| Savings and interest-bearing transaction | 1,627,596                                 | 2,457                                            | 0.30%                    |
| Time less than \$100,000                 | 453,274                                   | 2,833                                            | 1.26%                    |
| Time \$100,000 or more                   | 642,747                                   | 2,962                                            | 0.93%                    |
| Total interest-bearing deposits          | 2,723,617                                 | 8,252                                            | 0.61%                    |
| Short-term borrowed funds                | 483,880                                   | 1,482                                            | 0.62%                    |
| Debt financing and notes payable         | 26,601                                    | 844                                              | 6.35%                    |
| Total interest-bearing liabilities       | 3,234,098                                 | \$ 10,578                                        | 0.66%                    |
| Other liabilities                        | 73,391                                    |                                                  |                          |
| Shareholders' equity                     | 516,608                                   |                                                  |                          |

|                                                 |              |       |
|-------------------------------------------------|--------------|-------|
| Total liabilities and shareholders' equity      | \$ 5,133,941 |       |
| Net interest spread (1) (2)                     |              | 5.16% |
| Net interest income and interest margin (1) (3) | \$ 121,677   | 5.35% |

(1) Interest and rates calculated on a fully taxable equivalent basis using the current statutory federal tax rate.

(2) Net interest spread represents the average yield earned on earning assets minus the average rate paid on interest-bearing liabilities.

(3) Net interest margin is computed by calculating the difference between interest income and expense (annualized), divided by the average balance of earning assets.

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

The following tables set forth a summary of the changes in interest income and interest expense due to changes in average asset and liability balances (volume) and changes in average interest rates for the periods indicated. Changes not solely attributable to volume or rates have been allocated in proportion to the respective volume and rate components.

|                                                          | Three months ended June 30, 2010<br>compared with<br>Three months ended June 30, 2009 |             |              |
|----------------------------------------------------------|---------------------------------------------------------------------------------------|-------------|--------------|
|                                                          | <b>Volume</b>                                                                         | <b>Rate</b> | <b>Total</b> |
|                                                          | (In thousands)                                                                        |             |              |
| Interest and fee income:                                 |                                                                                       |             |              |
| Money market assets and funds sold                       | \$                                                                                    | \$ (1)      | \$ (1)       |
| Investment securities:                                   |                                                                                       |             |              |
| Available for sale                                       |                                                                                       |             |              |
| Taxable                                                  | 66                                                                                    | (466)       | (400)        |
| Tax-exempt (1)                                           | (77)                                                                                  | (60)        | (137)        |
| Held to maturity                                         |                                                                                       |             |              |
| Taxable                                                  | (1,521)                                                                               | (5)         | (1,526)      |
| Tax-exempt (1)                                           | (760)                                                                                 | 7           | (753)        |
| Loans:                                                   |                                                                                       |             |              |
| Commercial:                                              |                                                                                       |             |              |
| Taxable                                                  | (1,949)                                                                               | 1,135       | (814)        |
| Tax-exempt (1)                                           | (328)                                                                                 | 121         | (207)        |
| Commercial real estate                                   | (2,263)                                                                               | 187         | (2,076)      |
| Real estate construction                                 | (251)                                                                                 | 247         | (4)          |
| Real estate residential                                  | (934)                                                                                 | (321)       | (1,255)      |
| Consumer                                                 | (1,048)                                                                               | (124)       | (1,172)      |
| Total loans (1)                                          | (6,773)                                                                               | 1,245       | (5,528)      |
| Total (decrease) increase in interest and fee income (1) | (9,065)                                                                               | 720         | (8,345)      |
| Interest expense:                                        |                                                                                       |             |              |
| Deposits:                                                |                                                                                       |             |              |
| Savings and interest-bearing transaction                 | (68)                                                                                  | (407)       | (475)        |
| Time less than \$100,000                                 | (372)                                                                                 | (560)       | (932)        |
| Time \$100,000 or more                                   | (218)                                                                                 | (663)       | (881)        |
| Total interest-bearing deposits                          | (658)                                                                                 | (1,630)     | (2,288)      |
| Short-term borrowed funds                                | (589)                                                                                 | 276         | (313)        |
| Debt financing and notes payable                         | (2)                                                                                   | 3           | 1            |
| Total decrease in interest expense                       | (1,249)                                                                               | (1,351)     | (2,600)      |

|                                                |    |         |    |       |    |         |
|------------------------------------------------|----|---------|----|-------|----|---------|
| (Decrease) increase in Net Interest Income (1) | \$ | (7,816) | \$ | 2,071 | \$ | (5,745) |
|------------------------------------------------|----|---------|----|-------|----|---------|

(1) Amounts calculated on a fully taxable equivalent basis using the current statutory federal tax rate.

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|                                                          | Six months ended June 30, 2010<br>compared with<br>Six months ended June 30, 2009 |             |              |
|----------------------------------------------------------|-----------------------------------------------------------------------------------|-------------|--------------|
|                                                          | <b>Volume</b>                                                                     | <b>Rate</b> | <b>Total</b> |
|                                                          | (In thousands)                                                                    |             |              |
| Interest and fee income:                                 |                                                                                   |             |              |
| Money market assets and funds sold                       | \$ (1)                                                                            | \$          | \$ (1)       |
| Investment securities:                                   |                                                                                   |             |              |
| Available for sale                                       |                                                                                   |             |              |
| Taxable                                                  | 217                                                                               | (333)       | (116)        |
| Tax-exempt (1)                                           | (308)                                                                             | (33)        | (341)        |
| Held to maturity                                         |                                                                                   |             |              |
| Taxable                                                  | (3,645)                                                                           | (393)       | (4,038)      |
| Tax-exempt (1)                                           | (1,349)                                                                           | (38)        | (1,387)      |
| Loans:                                                   |                                                                                   |             |              |
| Commercial:                                              |                                                                                   |             |              |
| Taxable                                                  | (2,811)                                                                           | 1,764       | (1,047)      |
| Tax-exempt (1)                                           | (627)                                                                             | (80)        | (707)        |
| Commercial real estate                                   | (1,489)                                                                           | 635         | (854)        |
| Real estate construction                                 | (389)                                                                             | 539         | 150          |
| Real estate residential                                  | (1,888)                                                                           | (550)       | (2,438)      |
| Consumer                                                 | (1,282)                                                                           | 87          | (1,195)      |
| Total loans (1)                                          | (8,486)                                                                           | 2,395       | (6,091)      |
| Total (decrease) increase in interest and fee income (1) | (13,572)                                                                          | 1,598       | (11,974)     |
| Interest expense:                                        |                                                                                   |             |              |
| Deposits:                                                |                                                                                   |             |              |
| Savings and interest-bearing transaction                 | (5)                                                                               | (619)       | (624)        |
| Time less than \$100,000                                 | (446)                                                                             | (1,321)     | (1,767)      |
| Time \$100,000 or more                                   | (391)                                                                             | (802)       | (1,193)      |
| Total interest-bearing deposits                          | (842)                                                                             | (2,742)     | (3,584)      |
| Short-term borrowed funds                                | (1,002)                                                                           | 684         | (318)        |
| Debt financing and notes payable                         | (4)                                                                               | 7           | 3            |
| Total decrease in interest expense                       | (1,848)                                                                           | (2,051)     | (3,899)      |
| (Decrease) increase in Net Interest Income (1)           | \$ (11,724)                                                                       | \$ 3,649    | \$ (8,075)   |

(1) Amounts  
calculated on a

fully taxable  
equivalent basis  
using the  
current statutory  
federal tax rate.

**Provision for Loan Losses**

The Company manages credit costs by consistently enforcing conservative underwriting and administration procedures and aggressively pursuing collection efforts with troubled debtors. County loans purchased from the FDIC are covered by loss-sharing agreements the Company entered with the FDIC. Further, the Company recorded the purchased County loans at estimated fair value upon acquisition as of February 6, 2009. Due to the loss-sharing agreements and fair value recognition, the Company did not record a provision for loan losses during the first half of 2010 related to such loans covered by the FDIC loss-sharing agreements. In Management's judgment, the acquisition date loan fair value discounts remaining at June 30, 2010 represent appropriate loss estimates for default risk inherent in the purchased loans. The Company provided \$2.8 million for loan losses related to non-covered loans in the second quarter of 2010, compared with \$2.6 million in the second quarter of 2009. For the first six months of 2010 and 2009, \$5.6 million and \$4.4 million were provided in each respective period. The provision reflects Management's assessment of credit risk in the loan portfolio for each of the periods presented. For further information regarding credit risk, the FDIC loss-sharing agreements, net credit losses and the allowance for loan losses, see the Loan Portfolio Credit Risk and Allowance for Credit Losses sections of this report.

**Table of Contents****Noninterest Income**

The following table summarizes the components of noninterest income for the periods indicated.

|                                     | Three months ended<br>June 30, |           | Six months ended<br>June 30, |           |
|-------------------------------------|--------------------------------|-----------|------------------------------|-----------|
|                                     | 2010                           | 2009      | 2010                         | 2009      |
|                                     | (In thousands)                 |           |                              |           |
| Service charges on deposit accounts | \$ 8,629                       | \$ 9,116  | \$ 17,371                    | \$ 17,538 |
| Merchant credit card                | 2,176                          | 2,223     | 4,397                        | 4,655     |
| Debit card                          | 1,245                          | 1,323     | 2,419                        | 2,389     |
| ATM and interchange                 | 1,021                          | 1,013     | 1,912                        | 1,826     |
| Other service fees                  | 600                            | 540       | 1,235                        | 1,071     |
| Trust fees                          | 448                            | 373       | 829                          | 737       |
| Check sale income                   | 224                            | 215       | 454                          | 438       |
| Safe deposit rental                 | 164                            | 180       | 326                          | 347       |
| Financial services commissions      | 223                            | 137       | 372                          | 291       |
| Gain on acquisition                 |                                |           |                              | 48,844    |
| Other                               | 1,040                          | 1,266     | 1,925                        | 2,218     |
| Total                               | \$ 15,770                      | \$ 16,386 | \$ 31,240                    | \$ 80,354 |

Noninterest income for the second quarter of 2010 declined by \$616 thousand or 3.8% from the same period in 2009. Service charges on deposits decreased \$487 thousand or 5.3%. Other noninterest income fell \$226 thousand or 17.9% mostly due to miscellaneous fees and a gain on sale of foreclosed assets in the second quarter of 2009.

In the first half of 2010, noninterest income decreased \$49.1 million compared with the first half of 2009 primarily due to the \$48.8 million gain on acquisition in the first half of 2009. Merchant credit card fees declined \$258 thousand or 5.5% mainly due to lower transaction volumes and service charges on deposit accounts declined \$167 thousand or 0.95%. Other noninterest income fell \$293 thousand or 13.2% mostly due to miscellaneous fees and a gain on sale of foreclosed assets in the first half of 2009. Other service fees increased \$164 thousand or 15.3% mainly due to increases in internet banking fees and foreign currency commissions.

**Table of Contents****Noninterest Expense**

The following table summarizes the components of noninterest expense for the periods indicated.

|                                          | Three months ended<br>June 30, |                  | Six months ended<br>June 30, |                  |
|------------------------------------------|--------------------------------|------------------|------------------------------|------------------|
|                                          | 2010                           | 2009             | 2009                         | 2009             |
|                                          | (In thousands)                 |                  |                              |                  |
| Salaries and related benefits            | \$ 15,476                      | \$ 17,448        | \$ 31,368                    | \$ 33,819        |
| Occupancy                                | 3,822                          | 5,413            | 7,599                        | 10,823           |
| Outsourced data processing services      | 2,202                          | 2,378            | 4,442                        | 4,482            |
| Amortization of identifiable intangibles | 1,540                          | 1,695            | 3,138                        | 3,380            |
| FDIC insurance assessments               | 1,260                          | 3,221            | 2,580                        | 3,378            |
| Equipment                                | 1,116                          | 1,607            | 2,167                        | 2,829            |
| Courier service                          | 903                            | 994              | 1,810                        | 1,892            |
| Professional fees                        | 867                            | 779              | 1,530                        | 1,667            |
| Loan expense                             | 475                            | 205              | 893                          | 1,199            |
| Postage                                  | 454                            | 531              | 929                          | 993              |
| Telephone                                | 406                            | 478              | 795                          | 865              |
| Stationery and supplies                  | 330                            | 374              | 680                          | 741              |
| OREO expense                             | 314                            | 415              | 464                          | 519              |
| Advertising/public relations             | 266                            | 354              | 476                          | 581              |
| In-house meetings                        | 184                            | 239              | 359                          | 496              |
| Customer checks                          | 162                            | 187              | 333                          | 363              |
| Operational losses                       | 158                            | 221              | 378                          | 416              |
| Correspondent service charges            | 136                            | 333              | 238                          | 589              |
| Other noninterest expense                | 2,024                          | 1,794            | 3,947                        | 3,757            |
| <b>Total</b>                             | <b>\$ 32,095</b>               | <b>\$ 38,666</b> | <b>\$ 64,126</b>             | <b>\$ 72,789</b> |

|                                       |        |        |        |        |
|---------------------------------------|--------|--------|--------|--------|
| Average full time equivalent staff    | 1,018  | 1,176  | 1,025  | 1,160  |
| Noninterest expense to revenues (FTE) | 44.37% | 49.13% | 44.27% | 36.03% |

Noninterest expense decreased \$6.6 million or 17.0% in the second quarter 2010 compared with the same period in 2009 mainly due to declines in personnel, occupancy and equipment expenses resulting from the systems integrations and branch consolidations following the County acquisition and lower FDIC insurance assessments. Salaries and related benefits decreased \$2.0 million or 11.3% primarily due to a reduction in regular salaries and payroll taxes and lower workers compensation expense, partially offset by annual merit increases, higher group health insurance costs, profit sharing and other benefits. FDIC insurance assessments declined \$2.0 million or 60.9% due to a non-routine assessment charged in the second quarter 2009. Occupancy expense decreased \$1.6 million or 29.4% mainly due to branch and administrative office consolidations in May and August of 2009. Equipment expense declined \$491 thousand or 30.6% primarily due to branch and administrative office consolidations. A \$197 thousand or 59.2% decrease in correspondent service charges was mostly attributable to higher interest received on reserve balances held with the Federal Reserve Bank. Other categories which decreased were outsourced data processing services expense (down \$176 thousand or 7.4%), amortization of intangibles (down \$155 thousand or 9.1%) and OREO expense (down \$101 thousand or 24.3%). Loan expense increased \$270 thousand generally due to higher foreclosure and credit report expenses. Other noninterest expense increased \$230 thousand or 12.8% mainly because the second quarter 2009 included a \$400 thousand reduction in provision for loan commitments.



In the first half of 2010, noninterest expense decreased \$8.7 million or 11.9% compared with the corresponding period of 2009 primarily due to lower personnel, occupancy and equipment expenses resulting from the systems integrations and branch consolidations following the County acquisition and lower FDIC insurance assessments. Occupancy expense decreased \$3.2 million or 29.8% mainly due to branch and administrative office consolidations in May and August of 2009. Salaries and related benefits decreased \$2.5 million or 7.2% primarily due to a reduction in regular salaries and incentives and lower workers compensation expense, partially offset by higher group health insurance costs, payroll taxes, annual merit increases and higher profit sharing and other benefit expenses. FDIC insurance assessments decreased \$798 thousand or 23.6%. Equipment expense declined \$662 thousand or 23.4% primarily due to branch and administrative office consolidations. A \$351 thousand decrease in correspondent service charges was mostly attributable to higher interest received on reserve balances held with the Federal Reserve Bank. Loan expense decreased \$306 thousand or 25.5% generally because the first half of 2009 included servicing fees on factoring receivables acquired from County. Such factoring receivables were fully liquidated in April 2009. Offsetting the decline were higher foreclosure and credit report expenses. Amortization of intangibles decreased \$242 thousand or 7.2%. Professional fees decreased \$137 thousand or 8.2% largely due to lower consulting and accounting fees. Other noninterest expense increased \$190 thousand or 5.1% mainly because the first half of 2009 included a \$400 thousand reduction in provision for loan commitments.

**Table of Contents****Provision for Income Tax**

During the second quarter of 2010, the Company recorded income tax expense (FTE) of \$13.9 million compared with \$14.3 million for the second quarter of 2009. The current quarter provision represents an effective tax rate (FTE) of 37.1%, compared with 38.1% for the second quarter of 2009. The lower effective tax rate for the second quarter 2010 reflects increased tax credits and a higher proportion of net interest income which is tax-exempt.

The income tax provision (FTE) was \$28.0 million for the first six months of 2010 compared with \$48.8 million for the corresponding period of 2009. The first half of 2010 effective tax rate was 37.2% compared to 39.1% for the same period of 2009. The lower tax provision and effective tax rate for the first half of 2010 is primarily attributable to lower pre-tax income, increased tax credits, and a higher proportion of net interest income which is tax-exempt, offset in part by a tax refund received in 2009 related to amendment of a prior year tax return.

**Loan Portfolio Credit Risk**

The risk that loan customers do not repay loans granted by the Bank is the most significant risk to the Company. The Company closely monitors the markets in which it conducts its lending operations and follows a strategy to control exposure to loans with high credit risk. The Bank's organization structure separates the functions of business development and loan underwriting; Management believes this segregation of duties avoids inherent conflicts of combining business development and loan approval. In measuring and managing credit risk, the Company adheres to the following practices.

The Bank maintains a Loan Review Department which reports directly to the Board of Directors. The Loan Review Department performs independent evaluations of loans and assigns credit risk grades to evaluated loans using grading standards employed by bank regulatory agencies. Those loans judged to carry higher risk attributes are referred to as classified loans. Classified loans receive elevated management attention to maximize collection.

The Bank maintains two loan administration offices whose sole responsibility is to manage and collect classified loans.

Classified loans with higher levels of credit risk are further designated as nonaccrual loans. Management places loans on nonaccrual status when full collection of contractual interest and principal payments is in doubt. Interest previously accrued on loans placed on nonaccrual status is charged against interest income, net of estimated FDIC reimbursements under loss-sharing agreements. The Company does not accrue interest income on nonaccrual loans. Interest payments received on nonaccrual loans are applied to reduce the carrying amount of the loan unless the carrying amount is well secured by loan collateral or covered by FDIC loss-sharing agreements. Nonperforming assets include nonaccrual loans, loans 90 or more days past due and still accruing, and repossessed loan collateral.

On February 6, 2009, the Bank purchased loans and repossessed loan collateral of the former County Bank from the FDIC. This purchase transaction included loss-sharing agreements with the FDIC wherein the FDIC and the Bank share losses on the purchased assets. The loss-sharing agreements significantly reduce the credit risk of these purchased assets. In evaluating credit risk, Management bifurcates the Bank's total loan portfolio between those loans qualifying under the FDIC loss-sharing agreements (referred to as covered loans) and loans not qualifying under the FDIC loss-sharing agreements (referred to as non-covered loans). At June 30, 2010, covered loans totaled \$764 million, or 26 percent of total loans, and non-covered loans totaled \$2.1 billion, or 74 percent of total loans.

***Covered Loans and Repossessed Loan Collateral (Covered Assets)***

Covered loans and repossessed loan collateral qualify under loss-sharing agreements with the FDIC. Under the terms of the loss-sharing agreements, the FDIC absorbs 80 percent of losses and shares in 80 percent of loss recoveries on the first \$269 million in losses on covered assets (First Tier), and absorbs 95 percent of losses and shares in 95 percent of loss recoveries if losses on covered assets exceed \$269 million (Second Tier). The term of the loss-sharing agreement on residential real estate assets is ten years, while the term for loss-sharing on non-residential real estate assets is five years with respect to losses and eight years with respect to loss recoveries.

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The covered assets are primarily located in the California Central Valley, including Merced County. This geographic area currently has some of the weakest economic conditions within California and has experienced significant declines in real estate values. Management expects higher loss rates on covered assets than on non-covered assets.

The Bank recorded acquired covered assets at estimated fair value on the February 6, 2009 acquisition date. The credit risk discount ascribed to the \$1.2 billion acquired loan and repossessed loan collateral portfolio was \$161 million representing estimated losses inherent in the assets at the acquisition date. The Bank also recorded a related receivable from the FDIC in the amount of \$129 million representing estimated FDIC reimbursements under the loss-sharing agreements.

The maximum risk to future earnings if First Tier losses exceed Management's estimated \$161 million in recognized losses under the FDIC loss-sharing agreements follows (dollars in thousands):

|                                                    |            |
|----------------------------------------------------|------------|
| First Tier Loss Coverage                           | \$ 269,000 |
| Less: Recognized credit risk discount              | 161,203    |
| Exposure to under-estimated risk within First Tier | 107,797    |
| Bank loss-sharing percentage                       | 20 percent |
| First Tier risk to Bank, pre-tax                   | \$ 21,559  |
| First Tier risk to Bank, after-tax                 | \$ 12,494  |

Management has judged the likelihood of experiencing losses of a magnitude to trigger Second Tier FDIC reimbursement as remote. The Bank's maximum after-tax exposure to Second Tier losses is \$19 million as of June 30, 2010, which would be realized only if all covered assets at June 30, 2010 generated no future cash flows.

Covered assets have declined since the acquisition date, and losses have been offset against the estimated credit risk discount. Covered assets totaled \$787 million at June 30, 2010, net of a credit risk discount of \$76 million, compared to \$879 million at December 31, 2009, net of a credit risk discount of \$93 million. Covered Assets are evaluated for risk classification without regard to FDIC indemnification such that Management can identify covered assets with potential payment problems and devote appropriate credit administration practices to maximized collections. Covered assets classified without regard to FDIC indemnification totaled \$195 million and \$182 million at June 30, 2010 and December 31, 2009, respectively. FDIC indemnification limits the Company's loss exposure to covered classified assets.

In Management's judgment, the credit risk discount recognized for the acquired assets remains adequate as an estimate of credit risk inherent in covered assets as of June 30, 2010. In the event credit risk deteriorates beyond that estimated by Management, losses in excess of the credit risk discount would be recognized as an expense, net of related FDIC loss indemnification.

The following is a summary of covered nonperforming assets:

|                                           | At June 30,<br>2010 | At December 31,<br>2009 |
|-------------------------------------------|---------------------|-------------------------|
|                                           | (In thousands)      |                         |
| Covered Nonperforming Assets              |                     |                         |
| Nonperforming, nonaccrual loans           | \$ 37,438           | \$ 66,965               |
| Performing, nonaccrual loans              | 22,908              | 18,183                  |
| Total nonaccrual loans                    | 60,346              | 85,148                  |
| Loans 90 days past due and still accruing | 249                 | 210                     |
| Total nonperforming loans                 | 60,595              | 85,358                  |

|                                     |           |            |
|-------------------------------------|-----------|------------|
| Covered repossessed loan collateral | 23,670    | 23,297     |
| Total                               | \$ 84,265 | \$ 108,655 |

As a percentage of total covered loans and OREO 10.70% 12.37%

The amount of gross interest income that would have been recorded if all covered nonaccrual loans had been current in accordance with their original terms while outstanding was \$1.1 million and \$2.4 million in the second quarter and first half of 2010, respectively, compared with \$913 thousand and \$1.1 million for the second quarter and first half of 2009, respectively. The amount of interest income that was recognized on covered nonaccrual loans from all cash payments made during the three and six months ended June 30, 2010, totaled \$1.5 million and \$3.0 million, respectively, compared with \$-0- thousand and \$-0- thousand, respectively, for the second quarter and first half of 2009, respectively. These cash payments represent annualized yields of 9.14% and 8.13%, respectively, for the second quarter and the first half of 2010 compared with -0-% and -0-%, respectively, for the second quarter and first half of 2009.

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There were no cash payments received, which were applied against the book balance of covered nonaccrual loans outstanding at June 30, 2010 in the second quarter and first half of 2010. Similarly, there were no cash payments received in the second quarter and first half of 2009, which were applied against the book balances of nonaccrual loans outstanding at June 30, 2009.

**Non-covered Classified Loans and Repossessed Loan Collateral (Non-covered Assets)**

The following is a summary of non-covered classified loans and repossessed loan collateral:

|                               | At June 30,<br>2010 | At December 31,<br>2009 |
|-------------------------------|---------------------|-------------------------|
|                               | (In thousands)      |                         |
| Non-covered Classified Assets |                     |                         |
| Classified loans              | \$ 55,750           | \$ 57,241               |
| Repossessed loan collateral   | 18,028              | 12,642                  |
| Total                         | \$ 73,778           | \$ 69,883               |

|                                                          |     |     |
|----------------------------------------------------------|-----|-----|
| Allowance for loan losses / non-covered classified loans | 71% | 72% |
|----------------------------------------------------------|-----|-----|

The following is a summary of non-covered nonperforming assets on the dates indicated:

|                                           | At June 30,<br>2010 | At December 31,<br>2009 |
|-------------------------------------------|---------------------|-------------------------|
|                                           | (In thousands)      |                         |
| Non-covered Nonperforming Assets          |                     |                         |
| Nonperforming, nonaccrual loans           | \$ 19,941           | \$ 19,837               |
| Performing, nonaccrual loans              | 24                  | 25                      |
| Total nonaccrual loans                    | 19,965              | 19,862                  |
| Loans 90 days past due and still accruing | 712                 | 800                     |
| Total nonperforming loans                 | 20,677              | 20,662                  |
| Repossessed loan collateral               | 18,028              | 12,642                  |
| Total                                     | \$ 38,705           | \$ 33,304               |

|                                                                            |       |       |
|----------------------------------------------------------------------------|-------|-------|
| As a percentage of total non-covered loans and repossessed loan collateral | 1.81% | 1.50% |
|----------------------------------------------------------------------------|-------|-------|

The amount of gross interest income that would have been recorded if all non-covered nonaccrual loans had been current in accordance with their original terms while outstanding was \$315 thousand and \$613 thousand in the second quarter and first half of 2010, respectively, compared with \$295 thousand and \$470 thousand for the second quarter and first half of 2009, respectively. The amount of interest income that was recognized on non-covered nonaccrual loans from all cash payments made during the three and six months ended June 30, 2010, totaled \$301 thousand and \$432 thousand, respectively, compared with \$84 thousand and \$123 thousand, respectively, for the second quarter and first half of 2009, respectively. These cash payments represent annualized yields of 5.90% and 4.23%, respectively, for the second quarter and the first half of 2010 compared with 1.53% and 1.45%, respectively, for the second quarter and first half of 2009.

There were no cash payments received, which were applied against the book balance of non-covered nonaccrual loans outstanding at June 30, 2010 in the second quarter and first half of 2010. Total cash payments received during the second quarter and the first half of 2009 which were applied against the book balance of nonaccrual loans outstanding at June 30, 2009 totaled approximately \$1 thousand, all of which was received in the second quarter of 2009.

Fifty six loans comprised the \$20.0 million in nonaccrual loans as of June 30, 2010. During the first half of 2010 one commercial real estate relationship (\$2.2 million) and twelve other loans over \$100 thousand (\$5.8 million) were transferred to OREO while primarily three commercial real estate relationships (\$4.3 million) and one commercial relationship (\$1.6 million) were placed on nonaccrual status.

The Company had no restructured loans as of June 30, 2010 and December 31, 2009.

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Delinquent non-covered commercial loans, non-covered construction loans and non-covered commercial real estate loans on accrual status were as follows:

|                                                              | At June 30,<br><b>2010</b> | At December 31,<br><b>2009</b> |
|--------------------------------------------------------------|----------------------------|--------------------------------|
|                                                              | (In thousands)             |                                |
| Non-covered Commercial Loans:                                |                            |                                |
| 30-89 days delinquent:                                       |                            |                                |
| Dollar amount                                                | \$ 7,705                   | \$ 10,677                      |
| Percentage of total non-covered commercial loans             | 1.51%                      | 2.14%                          |
| 90 or more days delinquent:                                  |                            |                                |
| Dollar amount                                                | \$                         | \$                             |
| Percentage of total non-covered commercial loans             | %                          | %                              |
| Non-covered Construction Loans:                              |                            |                                |
| 30-89 days delinquent:                                       |                            |                                |
| Dollar amount                                                | \$ 599                     | \$ 149                         |
| Percentage of total non-covered construction loans           | 2.12%                      | 0.46%                          |
| 90 or more days delinquent:                                  |                            |                                |
| Dollar amount                                                | \$                         | \$                             |
| Percentage of total non-covered construction loans           | %                          | %                              |
| Non-covered Commercial Real Estate Loans:                    |                            |                                |
| 30-89 days delinquent:                                       |                            |                                |
| Dollar amount                                                | \$ 12,744                  | \$ 12,158                      |
| Percentage of total non-covered commercial real estate loans | 1.63%                      | 1.52%                          |
| 90 or more days delinquent:                                  |                            |                                |
| Dollar amount                                                | \$                         | \$                             |
| Percentage of total non-covered commercial real estate loans | %                          | %                              |

The Company's residential real estate loan underwriting standards for first mortgages limit the loan amount to no more than 80 percent of the appraised value of the property serving as collateral for the loan at the time of origination, and require verification of income of the borrower(s). The Company had no sub-prime non-covered loans as of June 30, 2010 and December 31, 2009. At June 30, 2010, \$2.8 million non-covered residential real estate loans were on nonaccrual status.

Delinquent non-covered residential real estate loans, non-covered automobile loans and non-covered other consumer loans on accrual status were as follows:

|                                                               | At June 30,<br><b>2010</b> | At December 31,<br><b>2009</b> |
|---------------------------------------------------------------|----------------------------|--------------------------------|
|                                                               | (In thousands)             |                                |
| Non-covered Residential Real Estate Loans:                    |                            |                                |
| 30-89 days delinquent:                                        |                            |                                |
| Dollar amount                                                 | \$ 458                     | \$ 3,064                       |
| Percentage of total non-covered residential real estate loans | 0.14%                      | 0.83%                          |
| 90 or more days delinquent:                                   |                            |                                |
| Dollar amount                                                 | \$                         | \$                             |
| Percentage of total non-covered residential real estate loans | %                          | %                              |
| Non-covered Indirect Automobile Loans:                        |                            |                                |
| 30-89 days delinquent:                                        |                            |                                |
| Dollar amount                                                 | \$ 5,552                   | \$ 6,506                       |
| Percentage of total indirect automobile loans                 | 1.37%                      | 1.49%                          |

|                                                      |    |       |        |
|------------------------------------------------------|----|-------|--------|
| 90 or more days delinquent:                          |    |       |        |
| Dollar amount                                        | \$ | 576   | \$ 723 |
| Percentage of total automobile loans                 |    | 0.14% | 0.17%  |
| Non-covered Other Consumer Loans:                    |    |       |        |
| 30-89 days delinquent:                               |    |       |        |
| Dollar amount                                        | \$ | 636   | \$ 762 |
| Percentage of total non-covered other consumer loans |    | 0.99% | 1.25%  |
| 90 or more days delinquent:                          |    |       |        |
| Dollar amount                                        | \$ | 136   | \$ 77  |
| Percentage of total non-covered other consumer loans |    | 0.21% | 0.13%  |



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Management believes the overall credit quality of the non-covered loan portfolio is reasonably stable; however, non-covered nonperforming assets could fluctuate from period to period. The performance of any individual loan can be affected by external factors such as the interest rate environment, economic conditions, collateral values or factors particular to the borrower. No assurance can be given that additional increases in non-covered nonaccrual loans will not occur in the future.

**Allowance for Credit Losses**

The Company's allowance for credit losses represents Management's estimate of credit losses inherent in the loan portfolio. In evaluating credit risk for loans, Management measures loss potential of the carrying value of loans. As described above, payments on nonaccrual loans may be applied against the principal balance of the loans until such time as full collection of the remaining recorded balance is expected. Further, the carrying value of covered loans includes fair value discounts assigned at the time of purchase under the provisions of FASB ASC 805, Business Combinations, and FASB ASC 310-30, Loans or Debt Securities with Deteriorated Credit Quality. The allowance for credit losses represents Management's estimate of credit losses in excess of these principal reductions.

Management determined the credit default fair value discounts assigned to covered loans purchased on February 6, 2009 remained adequate as an estimate of credit losses inherent in covered loans as of June 30, 2010.

The following table summarizes the credit loss provision, net credit losses and allowance for credit losses for the periods indicated:

|                                                         | Three months ended<br>June 30, |              | Six months ended<br>June 30, |              |
|---------------------------------------------------------|--------------------------------|--------------|------------------------------|--------------|
|                                                         | 2010                           | 2009         | 2010                         | 2009         |
|                                                         | (In thousands)                 |              |                              |              |
| Total non-covered loans outstanding at period end       | \$ 2,124,570                   | \$ 2,322,005 | \$ 2,124,570                 | \$ 2,322,005 |
| Average non-covered loans outstanding during the period | 2,136,407                      | 2,338,294    | 2,150,857                    | 2,356,288    |
| Analysis of the allowance                               |                                |              |                              |              |
| Balance, beginning of period                            | 43,009                         | 46,896       | 43,736                       | 47,563       |
| Provision for loan losses                               | 2,800                          | 2,600        | 5,600                        | 4,400        |
| Provision for unfunded credit commitments               |                                | (400)        |                              | (400)        |
| Loans charged off:                                      |                                |              |                              |              |
| Commercial and commercial real estate                   | (1,258)                        | (1,278)      | (2,131)                      | (1,774)      |
| Real estate construction                                | (316)                          | (311)        | (1,115)                      | (311)        |
| Real estate residential                                 | (516)                          | (129)        | (809)                        | (129)        |
| Consumer                                                | (2,165)                        | (2,219)      | (4,656)                      | (4,651)      |
| Total non-covered loans chargeoffs                      | (4,255)                        | (3,937)      | (8,711)                      | (6,865)      |
| Recoveries of previously charged off non-covered loans: |                                |              |                              |              |
| Commercial and commercial real estate                   | 351                            | 58           | 580                          | 148          |
| Real estate construction                                |                                | 8            |                              | 8            |
| Real estate residential                                 |                                |              |                              |              |
| Consumer                                                | 504                            | 590          | 1,204                        | 961          |
| Total recoveries                                        | 855                            | 656          | 1,784                        | 1,117        |
| Net loan losses                                         | (3,400)                        | (3,281)      | (6,927)                      | (5,748)      |
| Balance, end of period                                  | \$ 42,409                      | \$ 45,815    | \$ 42,409                    | \$ 45,815    |

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|                                                          |           |           |       |       |
|----------------------------------------------------------|-----------|-----------|-------|-------|
| Net loan losses to average non-covered loans             | 0.64%     | 0.56%     | 0.65% | 0.49% |
| Components:                                              |           |           |       |       |
| Allowance for loan losses                                | \$ 39,716 | \$ 43,122 |       |       |
| Reserve for unfunded credit commitments                  | 2,693     | 2,693     |       |       |
| Allowance for credit losses                              | \$ 42,409 | \$ 45,815 |       |       |
| Allowance for loan losses /non-covered loans outstanding | 1.87%     | 1.86%     |       |       |

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The Company's allowance for credit losses is maintained at a level considered adequate to provide for losses that can be estimated based upon specific and general conditions. These include conditions unique to individual borrowers, as well as overall credit loss experience, the amount of past due, nonperforming loans and classified loans, FDIC loss-sharing coverage relative to covered loan carrying amounts, recommendations of regulatory authorities, prevailing economic conditions and other factors. A portion of the allowance is specifically allocated to impaired loans whose full collectibility is uncertain. Such allocations are determined by Management based on loan-by-loan analyses. A second allocation is based in part on quantitative analyses of historical credit loss experience, in which criticized and classified credit balances identified through an independent internal credit review process are analyzed using a linear regression model to determine standard loss rates. The results of this analysis are applied to current criticized and classified loan balances to allocate the allowance to the respective segments of the loan portfolio. In addition, loans with similar characteristics not usually criticized using regulatory guidelines are analyzed based on the historical loss rates and delinquency trends, grouped by the number of days the payments on these loans are delinquent. Given currently weak economic conditions, Management is applying further analysis to consumer loans. Current levels of automobile loan losses are compared to initial allowance allocations and, based on Management judgment, additional allocations are applied, if needed, to estimated losses. For residential real estate loans, Management is comparing ultimate loss rates on foreclosed residential real estate properties and applying such loss rates to nonaccrual residential real estate loans. Based on this analysis, Management exercises judgment in allocating additional allowance if deemed appropriate to estimated losses on residential real estate loans. Last, allocations are made to non-criticized and non-classified commercial loans based on historical loss rates and other statistical data. The remainder of the allowance is considered to be unallocated. The unallocated allowance is established to provide for probable losses that have been incurred as of the reporting date but not reflected in the allocated allowance. It addresses additional qualitative factors consistent with Management's analysis of the level of risks inherent in the loan portfolio, which are related to the risks of the Company's general lending activity. Included in the unallocated allowance is the risk of losses that are attributable to national or local economic or industry trends which have occurred but have not yet been recognized in past loan charge-off history (external factors). The external factors evaluated by the Company include: economic and business conditions, external competitive issues, and other factors. Also included in the unallocated allowance is the risk of losses attributable to general attributes of the Company's loan portfolio and credit administration (internal factors). The internal factors evaluated by the Company include: loan review system, adequacy of lending Management and staff, loan policies and procedures, problem loan trends, concentrations of credit, and other factors. By their nature, these risks are not readily allocable to any specific loan category in a statistically meaningful manner and are difficult to quantify with a specific number. Management assigns a range of estimated risk to the qualitative risk factors described above based on Management's judgment as to the level of risk, and assigns a quantitative risk factor from the range of loss estimates to determine the appropriate level of the unallocated portion of the allowance. Management considers the \$42.4 million allowance for credit losses to be adequate as a reserve against non-covered credit losses as of June 30, 2010.

The following table presents the allocation of the allowance for credit losses:

|                          | At June 30,<br>2010                          |                                                                        | At December 31,<br>2009                      |                                                                        |
|--------------------------|----------------------------------------------|------------------------------------------------------------------------|----------------------------------------------|------------------------------------------------------------------------|
|                          | (In thousands)                               |                                                                        |                                              |                                                                        |
|                          | Allocation<br>of the<br>Allowance<br>Balance | Non-covered<br>Loans<br>as Percent of<br>Total<br>Non-covered<br>Loans | Allocation<br>of the<br>Allowance<br>Balance | Non-covered<br>Loans<br>as Percent of<br>Total<br>Non-covered<br>Loans |
| Commercial               | \$ 19,791                                    | 61%                                                                    | \$ 19,108                                    | 59%                                                                    |
| Real estate construction | 2,326                                        | 1%                                                                     | 2,968                                        | 1%                                                                     |
| Real estate residential  | 829                                          | 16%                                                                    | 1,529                                        | 17%                                                                    |

|                     |           |      |           |      |
|---------------------|-----------|------|-----------|------|
| Consumer            | 7,491     | 22%  | 8,424     | 23%  |
| Unallocated portion | 11,972    |      | 11,707    |      |
| Total               | \$ 42,409 | 100% | \$ 43,736 | 100% |

The allocation to loan portfolio segments changed from December 31, 2009 to June 30, 2010. The increase in allocation for commercial loans was substantially attributable to an increase in criticized commercial loans outstanding and Management's evaluation of loss rates against commercial loan performance metrics. The decrease in allocation to real estate construction loans reflects a decline in criticized construction loans outstanding. The decrease in the allocation to real estate residential loans is due to a lower outstanding balance of delinquent real estate residential loans and Management's judgment regarding the appropriate allocation based on recent foreclosure losses and levels of nonaccrual mortgages. The lower allocation for consumer loans was primarily due to a lower outstanding balance of delinquent consumer loans and Management's judgment regarding the appropriate allocation based on current levels of auto loan charge-offs. The unallocated portion of the allowance for credit losses increased \$265 thousand from December 31, 2009 to June 30, 2010. The unallocated allowance is established to provide for probable losses that have been incurred, but not reflected in the allocated allowance. At June 30, 2010 and December 31, 2009, Management's evaluations of the unallocated portion of the allowance for credit losses attributed significant risk levels to developing economic and business conditions (\$2.4 million and \$2.3 million, respectively), external competitive issues (\$0.8 million and \$0.8 million, respectively), internal credit administration considerations (\$2.0 million and \$2.0 million, respectively), and delinquency and problem loan trends (\$3.8 million and \$3.5 million, respectively). The change in the amounts allocated to the above qualitative risk factors was based upon Management's judgment, review of trends in its loan portfolio, extent of migration of previously non-classified loans to classified status, levels of the allowance allocated to portfolio segments, and current economic conditions in its marketplace. Based on Management's analysis and judgment, the amount of the unallocated portion of the allowance for credit losses was \$12.0 million at June 30, 2010, compared to \$11.7 million at December 31, 2009.

**Table of Contents****Asset/Liability and Market Risk Management**

Asset/liability management involves the evaluation, monitoring and management of interest rate risk, market risk, liquidity and funding. The fundamental objective of the Company's management of assets and liabilities is to maximize its economic value while maintaining adequate liquidity and a conservative level of interest rate risk.

**Interest Rate Risk**

Interest rate risk is a significant market risk affecting the Company. Interest rate risk results from many factors. Assets and liabilities may mature or reprice at different times. Assets and liabilities may reprice at the same time but by different amounts. Short-term and long-term market interest rates may change by different amounts. The remaining maturity of various assets or liabilities may shorten or lengthen as interest rates change. In addition, interest rates may have an impact on loan demand, demand for various deposit products, credit losses, and other sources of earnings such as account analysis fees on commercial deposit accounts and correspondent bank service charges.

In adjusting the Company's asset/liability position, Management attempts to manage interest rate risk while enhancing the net interest margin and net interest income. At times, depending on expected increases or decreases in general interest rates, the relationship between long and short term interest rates, market conditions and competitive factors, Management may adjust the Company's interest rate risk position in order to manage its net interest margin and net interest income. The Company's results of operations and net portfolio values remain subject to changes in interest rates and to fluctuations in the difference between long and short term interest rates.

The Company's asset and liability position ranged from neutral to slightly asset sensitive at June 30, 2010, depending on the interest rate assumptions applied to the simulation model employed by Management to measure interest rate risk. A neutral position results in similar amounts of change in interest income and interest expense resulting from application of assumed interest rate changes. A slightly asset sensitive position results in a slightly larger increase in interest income than in interest expense resulting from application of assumed interest rate changes. Management's simulation modeling is currently biased toward rising interest rates. Management continues to monitor the interest rate environment as well as economic conditions and other factors it deems relevant in managing the Company's exposure to interest rate risk.

Management assesses interest rate risk by comparing the Company's most likely earnings plan with various earnings models using many interest rate scenarios that differ in the direction of interest rate changes, the degree of change over time, the speed of change and the projected shape of the yield curve. For example, using the current composition of the Company's balance sheet and assuming no change in the federal funds rate and no change in the 10 year Constant Maturity Treasury Bond yield during the same period, earnings are not estimated to change by a meaningful amount compared to the Company's most likely net income plan for the twelve months ending June 30, 2011. Using the current composition of the Company's balance sheet and assuming an increase of 100 basis points ( bp ) in the federal funds rate and an increase of 80 bp in the 10 year Constant Maturity Treasury Bond yield during the same period, earnings are not estimated to change by a meaningful amount compared to the Company's most likely net income plan for the twelve months ending June 30, 2011. Simulation estimates depend on, and will change with, the size and mix of the actual and projected balance sheet at the time of each simulation. In the current operating environment, Management's objective is to maintain a neutral to slightly asset sensitive interest rate risk position. The Company does not currently engage in trading activities or use derivative instruments to control interest rate risk, even though such activities may be permitted with the approval of the Company's Board of Directors.

**Market Risk – Equity Markets**

Equity price risk can affect the Company. As an example, any preferred or common stock holdings, as permitted by banking regulations, can fluctuate in value. Management regularly assesses the extent and duration of any declines in market value, the causes of such declines, the likelihood of a recovery in market value, and its intent to hold securities until a recovery in value occurs. Declines in value of preferred or common stock holdings that are deemed other than temporary could result in loss recognition in the Company's income statement.

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Fluctuations in the Company's common stock price can impact the Company's financial results in several ways. First, the Company has regularly repurchased and retired its common stock; the market price paid to retire the Company's common stock can affect the level of the Company's shareholders' equity, cash flows and shares outstanding for purposes of computing earnings per share. Second, the Company's common stock price impacts the number of dilutive equivalent shares used to compute diluted earnings per share. Third, fluctuations in the Company's common stock price can motivate holders of options to purchase Company common stock through the exercise of such options thereby increasing the number of shares outstanding. Finally, the amount of compensation expense associated with share based compensation fluctuates with changes in and the volatility of the Company's common stock price.

**Market Risk Other**

Market values of loan collateral can directly impact the level of loan charge-offs and the provision for loan losses. Other types of market risk, such as foreign currency exchange risk and commodity price risk, are not significant in the normal course of the Company's business activities.

**Liquidity and Funding**

The Company generates significant liquidity from its operating activities. The Company's profitability during the first half of 2010 and 2009 contributed substantial operating cash flows of \$38.0 million and \$91.4 million, respectively. Operating cash flows in the first half 2009 increased \$30 million from the settlement of County Bank securities sales which were unsettled trades on the acquisition date. In the first half of 2010, the Company paid \$21.1 million in common shareholder dividends and used \$17.2 million to repurchase and retire common stock. In the first half of 2009, the Company paid \$20.6 million in common shareholder dividends and used \$1.1 million to repurchase and retire common stock.

The Company's routine sources of liquidity include investment securities, consumer and other loans, and other borrowed funds. During the first half of 2010, investment securities provided \$147.0 million in liquidity from paydowns and maturities to purchase securities of \$149.5 million, and loans provided \$145.4 million in liquidity from scheduled payments and maturities, net of loan fundings. First half of 2010 liquidity provided funds to meet a net reduction in deposits totaling \$168.1 million and a reduction in short-term borrowed funds, primarily FHLB advances which declined \$75.2 million.

During the first half of 2009, investment securities provided \$175.0 million in liquidity from paydowns and maturities, and loans provided \$184.1 million in liquidity from scheduled payments and maturities, net of loan fundings. The Company also raised \$83.7 million from the issuance of preferred stock to the United States Treasury in February 2009 which was redeemed in full in September and November of 2009. First half of 2009 liquidity provided funds to meet a net reduction in deposits totaling \$168.3 million and a \$381.8 million reduction in short-term borrowed funds, primarily federal funds purchased which declined \$236.4 million.

The Company projects \$69.6 million in additional liquidity from investment security paydowns and maturities during the three months ending September 30, 2010. At June 30, 2010, indirect automobile loans totaled \$405.1 million, which were experiencing stable monthly principal payments of approximately \$16.3 million during the second quarter of 2010.

The Company held \$1.1 billion in total investment securities at June 30, 2010. Under certain deposit, borrowing and other arrangements, the Company must hold and pledge investment securities as collateral. At June 30, 2010, such collateral requirements totaled approximately \$1.0 billion. At June 30, 2010, \$466.5 million of the Company's investment securities were classified as available-for-sale, and as such, could provide additional liquidity if sold, subject to the Company's ability to meet continuing collateral requirements.

At June 30, 2010, \$329.5 million in residential collateralized mortgage obligations (CMOs) and residential mortgage backed securities (MBSs) were held in the Company's investment portfolios. None of the CMOs or MBSs are backed by sub-prime mortgages. Substantially all of the Non Agency residential CMOs are rated AAA based on their subordination structures without reliance on monoline insurance. Other than nominal amounts of FHLMC and FNMA MBSs purchased for Community Reinvestment Act investment purposes and those securities purchased as part of the County acquisition, the Company has not purchased a residential CMO or residential MBS since November 2005. The residential CMOs and MBSs provided \$35.7 million in liquidity from paydowns during the three months ended June 30, 2010. In addition, at June 30, 2010, the Company had customary lines for overnight borrowings from other

financial institutions in excess of \$700 million, under which \$-0- million was outstanding. Additionally, the Company has access to borrowing from the Federal Reserve. The Company's short-term debt rating from Fitch Ratings is F1. The Company's long-term debt rating from Fitch Ratings is A with a stable outlook. Management expects the Company could access additional long-term debt financing if desired. In Management's judgment, the Company's liquidity position is strong and asset liquidations or additional long-term debt are considered unnecessary to meet the ongoing liquidity needs of the Company.

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The Company anticipates maintaining its cash levels in 2010. It is anticipated that loan demand from credit-worthy borrowers will be weak during 2010, although such demand will be dictated by economic and competitive conditions. The Company aggressively solicits non-interest bearing demand deposits and money market checking deposits, which are the least sensitive to changes in interest rates. The growth of deposit balances is subject to heightened competition, the success of the Company's sales efforts, delivery of superior customer service and market conditions. Changes in interest rates, most notably rising interest rates, could impact deposit volumes in the future. Depending on economic conditions, interest rate levels, and a variety of other conditions, deposit growth may be used to fund loans, to reduce short-term borrowings or purchase investment securities. However, due to concerns such as uncertainty in the general economic environment, competition and political uncertainty, loan demand and levels of customer deposits are not certain. Shareholder dividends are expected to continue subject to the Board's discretion and continuing evaluation of capital levels, earnings, asset quality and other factors.

Westamerica Bancorporation ( Parent Company ) is a separate entity and apart from Westamerica Bank ( Bank ) and must provide for its own liquidity. In addition to its operating expenses, the Parent Company is responsible for the payment of dividends declared for its shareholders, and interest and principal on outstanding debt. Substantially all of the Parent Company's revenues are obtained from subsidiary dividends and service fees. Payment of dividends to the Parent Company by the Bank is limited under California law. The amount that can be paid in any calendar year, without prior approval from the state regulatory agency, cannot exceed the net profits (as defined) for the preceding three calendar years less distributions in that period. The Company believes that such restriction will not have an impact on the Parent Company's ability to meet its ongoing cash obligations.

**Capital Resources**

The Company has historically generated high levels of earnings, which provides a means of raising capital. The Company's net income as a percentage of average common equity ( return on common equity or ROE ) was 18.5% in the first half of 2010, 25.8% in 2009 and 14.8% in 2008. The Company also raises capital as employees exercise stock options, which are awarded as a part of the Company's executive compensation programs to reinforce shareholders interests in the Management of the Company. Capital raised through the exercise of stock options totaled \$8.8 million in the first half of 2010, \$9.6 million in 2009 and \$22.8 million in 2008.

The Company paid dividends totaling \$21.1 million in the first half of 2010, \$41.1 million in 2009 and \$40.2 million in 2008, which represent dividends per share of \$0.72, \$1.41 and \$1.39, respectively. The Company's earnings have historically exceeded dividends paid to shareholders. The amount of earnings in excess of dividends gives the Company resources to finance growth and maintain appropriate levels of shareholders' equity. In the absence of profitable growth opportunities, the Company has repurchased and retired its common stock as another means to return capital to shareholders. The Company repurchased and retired 308 thousand shares of common stock valued at \$17.2 million in the first half of 2010, 42 thousand shares valued at \$2.0 million in 2009 and 719 thousand shares valued at \$35.9 million in 2008. Share repurchases were restricted to amounts conducted in coordination with employee benefit programs under the terms of the February 13, 2009 issuance of preferred stock to the Treasury; such restrictions were removed with full redemption of the preferred stock in November 2009.

The Company's primary capital resource is shareholders' equity, which increased \$22.2 million or 4.4% at June 30, 2010 since December 31, 2009, primarily due to \$47.1 million in profits earned during the first half of 2010 and \$8.8 million in issuance of stock in connection with exercises of employee stock options, offset by \$21.1 million in dividends paid and \$17.2 million in stock repurchases.

**Capital to Risk-Adjusted Assets**

The following summarizes the ratios of capital to risk-adjusted assets for the Company on the date indicated:

|                | At June<br>30,<br><b>2010</b> | At June<br>30,<br><b>2009</b> | At December<br>31,<br><b>2009</b> | Minimum<br>Regulatory<br>Requirement | Well-capitalized<br>by Regulatory<br>Definition |
|----------------|-------------------------------|-------------------------------|-----------------------------------|--------------------------------------|-------------------------------------------------|
| Tier I Capital | 14.42%                        | 14.57%                        | 13.20%                            | 4.00%                                | 6.00%                                           |



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|                |        |        |        |       |        |
|----------------|--------|--------|--------|-------|--------|
| Total Capital  | 15.72% | 15.85% | 14.50% | 8.00% | 10.00% |
| Leverage ratio | 8.53%  | 8.23%  | 7.60%  | 4.00% | 5.00%  |

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The risk-based capital ratios decreased at June 30, 2010 compared with June 30, 2009, due to redemption of the preferred stock, partially offset by increased retained earnings and a decrease in risk-weighted assets. The risk-based capital ratios increased at June 30, 2010, compared with December 31, 2009, due to a decrease in risk-weighted assets and increased retained earnings. FDIC-covered assets are included in the 20% risk-weight category due to the loss-sharing agreements; the residential loss-sharing agreement expires February 6, 2019 and the non-residential loss-sharing agreement expires (as to losses) February 6, 2014.

The following summarizes the ratios of capital to risk-adjusted assets for the Bank on the date indicated:

|                | At June<br>30,<br><b>2010</b> | At June<br>30,<br><b>2009</b> | At December<br>31,<br><b>2009</b> | Minimum<br>Regulatory<br>Requirement | Well-capitalized<br>by Regulatory<br>Definition |
|----------------|-------------------------------|-------------------------------|-----------------------------------|--------------------------------------|-------------------------------------------------|
| Tier I Capital | 13.90%                        | 13.64%                        | 13.39%                            | 4.00%                                | 6.00%                                           |
| Total Capital  | 15.38%                        | 15.11%                        | 14.88%                            | 8.00%                                | 10.00%                                          |
| Leverage ratio | 8.17%                         | 7.66%                         | 7.67%                             | 4.00%                                | 5.00%                                           |

The risk-based capital ratios increased at June 30, 2010, compared with June 30, 2009, due to a decrease in risk-weighted assets. The risk-based capital ratios increased at June 30, 2010, compared with December 31, 2009, due to a decrease in risk-weighted assets.

The Company and the Bank intend to maintain regulatory capital in excess of the highest regulatory standard, referred to as "well capitalized". The Company and the Bank routinely project capital levels by analyzing forecasted earnings, credit quality, securities valuations, shareholder dividends, asset volumes, share repurchase activity, stock option exercise proceeds, and other factors. Based on current capital projections the Company and the Bank expect to maintain regulatory capital levels exceeding the "well capitalized" standard and pay quarterly dividends to shareholders. No assurance can be given that changes in capital management plans will not occur.

**Item 3. Quantitative and Qualitative Disclosures about Market Risk**

The Company does not currently engage in trading activities or use derivative instruments to control interest rate risk, even though such activities may be undertaken with the approval of the Company's Board of Directors. Interest rate risk as discussed above is the most significant market risk affecting the Company. Other types of market risk, such as foreign currency exchange risk, equity price risk and commodity price risk, are not significant in the normal course of the Company's business activities.

**Item 4. Controls and Procedures**

The Company's principal executive officer and principal financial officer have evaluated the effectiveness of the Company's disclosure controls and procedures, as such term is defined in Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended, as of June 30, 2010. Based upon their evaluation, the principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time period specified in the Securities and Exchange Commission's rules and forms and are effective in ensuring that information required to be disclosed in the reports that the Company files or submits under the Exchange Act is accumulated and communicated to Management, including the chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure. The evaluation did not identify any change in the Company's internal control over financial reporting that occurred during the quarter ended June 30, 2010 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

Due to the nature of the banking business, the Bank is at times party to various legal actions; generally such actions are of a routine nature and arise in the normal course of business of the Bank. The Bank is not a party to any pending or threatened legal action that, if determined adversely to the Bank, is likely in Management's opinion to have a

material adverse effect on the Bank's financial condition or results of operations.

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**Item 1A. Risk Factors**

The 2009 Form 10-K includes detailed disclosure about the risks faced by the Company's business. Such risks have not materially changed since December 31, 2009, except as described below:

**Regulatory Risks**

On July 21, 2010, President Obama signed into law the Dodd Frank Wall Street Reform and Consumer Protection Act (the Act). The Act will institute far-reaching reforms, including the creation of an independent Bureau of Consumer Financial Protection inside the Federal Reserve Board and new federal government power to wind down large, failing financial institutions.

The Act permanently raises the current standard maximum deposit insurance amount to \$250,000. The standard maximum insurance amount of \$100,000 had been temporarily raised to \$250,000 until December 31, 2013. This permanent increase in deposit insurance limits could increase the Company's future insurance assessments.

The Act requires the Federal Reserve to issue regulations to ensure that fees charged to merchants for debit card transactions are reasonable and proportional to the cost of processing those transactions. While institutions with less than \$10 billion in assets are exempt from these regulations, the effect of competition on the fee levels has the potential for making that illusory. In all likelihood, all banks will see a loss of revenue from changes that will occur with interchange fees.

The Act will establish a 10-member Financial Stability Oversight Council. The duties of this council include monitoring financial regulatory proposals and accounting issues, facilitating coordination among the regulatory agencies, requiring Federal Reserve supervision of systemically significant non-bank financial companies, recommending new standards and reviewing accounting principles.

The Act places new limits, known as the Volcker Rule, on the amount of money a bank can invest in hedge funds and private equity funds. It also discourages financial institutions from excessive risk-taking by imposing tough new capital and leverage requirements. Further, it allows the Government Accountability Office to conduct a one-time audit of the Federal Reserve's emergency lending activities during the financial crisis and establishes the Federal Insurance Office to supervise insurance products, other than health insurance, at the federal level.

Other provisions will establish closer oversight of the over-the-counter derivatives market, including mandatory clearing and trading and real-time reporting of derivatives trades. Among other measures, the bill will institute numerous investor protections, including stricter oversight of credit rating agencies, securitization reforms and expanded Securities and Exchange Commission enforcement powers. The legislation establishes mortgage protections requiring lenders to ensure that their borrowers can repay their loans by establishing minimum federal standards for all home loans.

No assurance can be given as to the ultimate effect that the Act or any of its provisions may have on the Company, the financial services industry or the nation's economy.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

- (a) Previously reported on Form 8-K.
- (b) None
- (c) Issuer Purchases of Equity Securities

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The table below sets forth the information with respect to purchases made by or on behalf of the Company or any affiliated purchaser (as defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934), of common stock during the quarter ended June 30, 2010.

| Period                   | (a)<br>Total<br>Number<br>of<br>Shares<br>Purchased | (b)<br>Average<br>Price<br>Paid per<br>Share<br><br>(In thousands, except per share data) | (c)<br>Total Number<br>of Shares<br>Purchased as Part<br>of<br>Publicly<br>Announced<br>Plans or<br>Programs* | (d)<br>Maximum<br>Number<br>of Shares that<br>May<br>Yet Be<br>Purchased<br><br>Under the Plans<br>or Programs |
|--------------------------|-----------------------------------------------------|-------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------|
| April 1 through April 30 | 12                                                  | \$ 58.99                                                                                  | 12                                                                                                            | 1,887                                                                                                          |
| May 1 through May 31     | 153                                                 | \$ 56.96                                                                                  | 153                                                                                                           | 1,734                                                                                                          |
| June 1 through June 30   | 55                                                  | \$ 54.09                                                                                  | 55                                                                                                            | 1,679                                                                                                          |
| Total                    | 220                                                 | \$ 56.35                                                                                  | 220                                                                                                           | 1,679                                                                                                          |

\* Includes 4 thousand, 1 thousand and 2 thousand shares purchased in April, May and June, respectively, by the Company in private transactions with the independent administrator of the Company's Tax Deferred Savings/Retirement Plan (ESOP). The Company includes the shares purchased in such transactions within the total number of shares authorized for purchase pursuant to the currently existing publicly announced

program.

The Company repurchases shares of its common stock in the open market to optimize the Company's use of equity capital and enhance shareholder value and with the intention of lessening the dilutive impact of issuing new shares to meet stock performance, option plans, and other ongoing requirements.

Shares were repurchased during the first quarter of 2010 pursuant to a program approved by the Board of Directors on August 27, 2009, authorizing the purchase of up to 2 million shares of the Company's common stock from time to time prior to September 1, 2010.

**Item 3. Defaults upon Senior Securities**

None

**Item 4. Reserved**

**Item 5. Other Information**

None

**Item 6. Exhibits**

(a) The exhibit list required by this item is incorporated by reference to the Exhibit Index filed with this report.

Exhibit 31.1: Certification of Chief Executive Officer pursuant to Securities Exchange Act Rule 13a-14(a)/15d-14(a)

Exhibit 31.2: Certification of Chief Financial Officer pursuant to Securities Exchange Act Rule 13a-14(a)/15d-14(a)

Exhibit 32.1: Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Exhibit 32.2: Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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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 hereunto duly authorized.

WESTAMERICA BANCORPORATION  
(Registrant)

/s/ JOHN ROBERT THORSON

John Robert Thorson  
Senior Vice President and Chief Financial Officer  
(Chief Financial and Accounting Officer)

Date: July 30, 2010

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**EXHIBIT INDEX**

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